



NEW SOLIDARITY International Press Service

P.O. Box 1972, G.P.O.
New York, New York 10001
Editorial (212)279-5950
Customer Service (212)564-8529

Special Briefing On The World Economic Situation

I. INTRODUCTION

The world is now four weeks into the final quarter of the post-war Dollar Empire. To the extent this is recognized even among the purportedly most sophisticated banking circles, it is a cause for hysterical demands for austerity, which would rapidly worsen the financial situation past the point of no return. In general the current proprietors of the Dollar Empire have no grasp whatsoever of the reasons for the imminent collapse of the international financial markets, intertwined with the constriction of international trade and economic activity in the industrialized countries. This accounts for the depth of programmatic bankruptcy which Atlanticist financier and political circles have sunk to since the "recovery" of the third quarter disappeared during the final months of the year.

Therefore, the immediate removal of the Atlanticist debt-collectors from policy direction in the advanced sector, and their replacement by factions who can help bring into being a New World Economic Order, are the only tasks on the world political agenda.

The following analysis of the condition of the world economy is comprehensive proof that any scheme to prop up the \$800 billion in illiquid debt obligations in the dollar sector is a passing annoyance that should not preoccupy serious people.

We shall summarize below the state of the U.S. and European economies, their banking structure, the position of the Third World, and the state of the international markets, and identify the weak links in the chain of dollar indebtedness.

Since approximately the fall of 1974, the continued existence of the dollar reserve system and its associated debt structures has been founded on the collapse and contraction of the post-war dollar system, just as much as its previous endurance was based on the expansion of the same dollar system. Starting with the collapse of U.S. industrial production at the point, with a related sharp decline in purchasing power of the U.S. population, the "balance of payments" crises of 1974 seemed to have ended temporarily. This balance of payments crisis following the oil price increase sponsored by the "Seven Sisters" oil cartel had threatened to provoke a general liquidity crisis throughout the dollar system, and required more than \$20 billion of financing for Japan and a similar amount for the Third World to contain.

During 1975, however, the precipitous drop in industrial production world-wide enabled the weaker European sectors and Japan to ease their balance of payments position considerably, on the basis of depression levels of austerity. This,

in the broadest terms, immediately set the following destructive processes in motion:

1) The Third World's balance of payments deficit, due to the collapse of both the price and volume of its raw materials exports, became uncontrollable. Of the \$40 billion in short-term financing made available through the private banking system between June 1974 and December 1975, approximately half, or \$20 billion, now represents debt in effective or actual default, rolled over on an extremely short-term basis.

2) The income of the oil-producing countries fell sharply, eroding their capacity to purchase Western goods and services, thus cancelling out much of the apparent paper gain in balance of payments, albeit with a six-month lag.

3) A corporate liquidity crisis began to develop in all of the key Western European sectors, averted temporarily through \$15 billion in "countercyclical spending" in Western Europe mainly during the third quarter, and rates of money supply increase exceeding 20 per cent per year in France and West Germany.

4) The dollar regained strength after a period of prolonged collapse through June 1975, on the basis of an \$11 billion annual U.S. surplus in balance-of-payments, and the more rapid collapse of the trade-dependent European economies.

Far from demonstrating the revival of the dollar system, the dollar's strength is an ironic symptom of the state of crisis. The expansion of the Western capitalist economies since the war has been based on the capacity of the dollar to tolerate a deficit, in the process of financing the rest of the world's expansion. The dollar's strengthening relied on the contraction of the income-producing base of the Dollar's Empire satrapies in Western Europe and Japan.

The qualitatively new development, as of the new year, is that the ability of the contraction of the dollar system to finance its collective debt-service burden has come to an end. Simultaneously, crises have broken out in the external positions of France, Italy, Britain, Spain and Scandinavia; in the indebtedness of the Third World, whose short-term obligations are sufficient to provoke a general banking collapse by a factor of four; in the \$35 billion short-term shipping loans sector; in the internal credit systems of France, Germany, and Japan; and in the banking system of the United States, provoked by a second ratchet-collapse of U.S. industrial production.

Taking note of the proclivity of terrified ignoramuses to describe each horrifying symptom of this decay as a new "isolated case," we emphasize that these crises merely reflect

the implosion of the dollar system as a whole. World economic life will cease by the end of March, outside of the relatively insulated socialist sector, unless we take appropriate action.

II. THE UNITED STATES

The economic recovery of the second half of 1975 was a combination of statisticians' bluff and temporary stabilization measures, such as transfer payments and consumer credit expansion, whose effect is already faltering sharply. The capital goods and construction sectors of the U.S. economy, which never experienced a recovery, remain in a depression, while the most recent figures of the Ford Administration on capital spending and housing starts indicate a continued downturn. Only one sector of the U.S. economy has blocked the downward slide of industrial output: the automobile industry, with limited support from other consumer-goods sectors. In this context, the implications of the announcement this week of 17,500 new layoffs in Detroit, due to the fall of new car sales below industry expectations, are clear.

Under current circumstances, the foreign trade prospects for U.S. industry appear even more grim: with the exception of West Germany and Japan, virtually every developed and developing country is under severe financial constraints to reduce imports during the months ahead. During 1975, when the financial strains on the developing countries only began to emerge, their imports fell by 8 per cent in real volume. Brazil, the "model" country for U.S. exports to the developing sector, cut its imports by 30 per cent in dollar terms during the second half of 1975. Collectively, the deficit nations of the Organization for Economic Cooperation and Development (OECD) are projected to show a \$16 billion balance-of-payments deficit during 1976, under the assumption of modest growth in world trade led by a U.S. recovery.

Against this picture, President Ford's proposal to cut the Federal budget by \$70 billion in constant dollars raises some astonishing questions. The Federal government concentrated most of a \$26 billion increase in transfer payments last year into the second half of 1975. Since the banking system's loans outstanding to business contracted by an unprecedented \$30 billion during the year, and continue to contract, the Federal government acted as the financier for the liquidation of inventories during the second and third quarters at an annual rate of \$30 billion. This properly accounts for the impressive rise of third quarter nominal Gross National Product. When the input of Federal transfer payments — through tax reductions, increased social security, and so on — began to peter out, the "recovery" ended. If Administration economists are still at their desks several months from now, they will postulate that the "recession of 1976," following the "recession of 1975," could be traced to November, the month in which manufacturers' shipments and orders turned down, and overall inventories rose.

A Short History of the 'Upturn'

Beginning in November 1975 the economy entered a new phase of industrial collapse, guaranteed to produce a killing magnification of the present disastrous liquidity crisis and a blowout that will make that of the 1930's look small. There will be no recovery for the U.S. economy in 1976.

The reasons for the renewed downturn are rooted in the so-called "upturn" of April-September 1975, which in fact represented no economic upturn at all.

Although industrial output increased 5.6 per cent, the increase came strictly out of workers' hides. During this entire period personal disposable income actually declined in con-

stant dollar terms. The so-called drop in unemployment, from 9.6 to 8.3 per cent, occurred only because government statisticians played their familiar game of writing those unemployed not officially registered as actively looking for work out of the labor force. The total workforce has officially declined by 3 million — a whopping 4 per cent — since June.

These figures make it plain why production in the consumer goods sector, maintained principally by such devices as the five-year auto loan, will not hold up much longer. Workers will soon lack the wherewithal to make consumer purchases on any terms.

This has already become evident in September when the manufacturing sector in the U.S. showed major signs of renewed collapse. Beginning in September wholesalers and retailers experiencing flat sales to cut back orders from manufacturers. The immediate effect of this was that in November, for the first time in 5 months, manufacturing shipments plunged by almost 1 per cent. This was reflected in a sharp drop in business sales. As a result of these developments production began to slow down in October and November.

In the capital goods sector, the picture was far worse. Housing construction last year experienced its worst year since 1945, and housing starts in October and November fell by nearly 10 per cent. Contract awards for construction of new plant and equipment fell by 25 per cent. And in November durable goods orders dropped by 3.2 per cent — with machine tool orders, a key economic indicator for industrial production, falling 33 per cent.

Far from even reproducing plant and equipment, 80 per cent of so-called capital investment during the "upturn" was in inventories. Through the summer months production was fed by a transfer of inventories from the manufacturing to wholesale and retail level. To the extent that there was an increase in sales, it was almost entirely due to workers digging into the personal savings — to the tune of about \$30 billion dollars.

The "upturn" in 1975 should properly be compared with 1934-1937 of the Great Depression, a period of supposed recovery which ended with a sharper collapse than the 1929-1933 period. To the extent that the transfer payments — unemployment compensation for example — financed a certain temporary expansion then as now, the process was cruelly aborted by the fact that it simply generated greater government debt, requiring greater austerity measures to prop it up, and so on in a downward spiral. That is the significance of the Ford administration's projected \$70 billion federal budget deficit for fiscal 1976.

The Expanding Liquidity Crisis

The funds being sucked out of both the reproduction of a skilled working class and the capital goods required to sustain real production showed up as a major inflow to large financial institutions — \$13 billion in life insurance companies and \$41 billion in savings and loan associations, for example. These institutions in turn had nowhere to invest at the rate of return required to refinance their own indebtedness except in sheer speculation — hence the stock market bubble.

Wall Street financial analysts admit this inflow will increase massively — \$16 billion into life insurance firms and \$46 billion into savings and loan associations — even if industrial production continued to increase at a 5 per cent rate. As production has actually entered a new collapse phase, the problem can only intensify.

Analysts already estimate that investments in corporate bonds will be only half what they were a year ago, and that those related to manufacturing production will plunge from

\$11 billion to \$2 billion. Investment in tax exempt securities is expected to drop 30 per cent.

The alternative investment is government securities, but the huge excess of funds is driving down interest rates here to the level of other investments.

This was the situation which produced the 1929 market collapse. But there are two major differences between now and 1929. First, the liquidity crisis is much worse; the ratio of the economy's debt to income is at least four times greater today than in 1929. Put another way, the capacity of the economy to service debt requirements is one-fourth what it was during the last speculative bubble. Second, the present stock market splurge reflects much more a full-scale liquidity crisis throughout the entire dollar sector, centered in the banking system.

Because the ratio of debt to equity in the financial system represented by the relationship of huge bank loans to actual ownership instruments such as stocks, for example — is far worse than in 1929, the outcome of the present crisis will not simply be a stock market crash, but a full scale collapse of the capitalist banking system.

The Banking Collapse

The large New York and related money-center banks are already insolvent by any competent accounting standard. Any renewed economic downturn, as the Comptroller of the Currency has admitted, makes the survival chances of the Chase Manhattan Bank and its New York banking colleagues questionable. These banks comprise one-fifth of the U.S. banking system.

Federal Reserve Chairman Arthur Burns, with more than a little irony, warned Congress last week that the crippling of the banking system would have devastating implications for the U.S. economy and the international community. The banks however, will be crippled. On whose behalf will the Administration act? Set against the rest of the economy, the largest U.S. banks, as the nation's foremost creditors, demand protection at the expense of industry, agriculture, foreign trade, employment, and living standards. President Ford and his advisors are in danger of having no greater historical role than bailiffs in the worst foreclosure in world history.

Contrary to published reports that the potential losses of the largest commercial banks are in the range of 98 per cent of capital in the case of Chase Manhattan and 114 per cent of capital in the case of Citibank, the New York financial community in general is operating on the premise that 50 to 70 per cent of the large banks' loans are questionable — representing 1,000 per cent of capital. That is if only one-tenth of the questionable loans of these institutions must be written off, they will be insolvent.

These banks have concentrated their assets principally in the following lending areas: the \$14 billion of loans to Real Estate Investment Trusts (REITS); the \$12 billion of construction and development loans to developers; the \$80 billion of private credits to the developing countries; \$35 billion in international loans to tanker operators; \$10 billion in loans for international commodity stock-piling and speculation; \$30 billion in short-term loans to Japan; \$14 billion in loans to Italy; \$13 billion in loans to Britain; \$6 billion in loans to France; and related weak sectors.

Not only are the large New York banks heavily immersed in the most illiquid sectors of international lending, but the proportion of their assets representing illiquid loans jumped exponentially during the past year. Net repayment of commercial and industrial loans of \$30 billion during 1975, of

which \$11 billion went to banks in the New York Federal Reserve's district, corresponds to a similar amount of corporate financing on the long-term debt markets. The most creditworthy of the customers of the money-center banks refinanced their short-term debts, repaying the most reliable of the banks' earning assets, and thereby raising the proportion of bad loans in the banks' portfolios.

But even the concern over these banks at the office of the Comptroller of the Currency is fundamentally incompetent. New York banks' deposits at their foreign branches, overwhelmingly engaged in lending to the quadriplegics of the world economy, now total \$74 billion — compared to \$77 billion in total demand deposits.

What Ford and his advisors miserably ignore is the fact that the financial structure on which the U.S. economy depends in an international financial structure. Almost one-fifth of the Federal debt, whose explosive growth the Administration views with such distaste, has been financed through foreign central banks' holdings of dollar reserves. The same process of international expansion, the \$250 billion dollar overhang, that made possible the financing of the hated Federal deficits, will shortly destroy the U.S. credit system.

The actual, near-collapse situation of the banking structure was underscored by government statistics released this week. According to statistics made available by the Federal Reserve Bank Jan. 22, the top ten New York banks which comprise one-third of all U.S.-owned banking activity, are experiencing an "implository" contraction of loans and investments unsurpassed in any three week period in recent history. In the past three weeks alone, commercial and industrial loans have fallen by \$1.7 billion, or an astonishing five per cent.

Meanwhile the renewed economic downturn reflected in this contraction of loans has also created an excess pool of funds so large and so desperate for investment that all short-term interest rates have fallen to a level which makes such loans no longer profitable investments for banks. As a result, during this same three week period the New York banks have also reduced their holdings of U.S. Treasury debt by more than \$1 billion.

With high earning assets in real estate, Third World and municipal bond investment having turned overnight into massive losses, there are only two remaining sources of bank income available to cover bad loans and delay outright bankruptcies: loan shark interest rates on commercial and industrial loans; and swindle-like investment in short-term Treasury bills with cheaper funds slipped to the banks by the Federal Reserve. Now the renewed collapse of production wipes out these two short-term swindle operations by the banking system and throws it over the edge, putting an end to the hope that the banks can recover even a small proportion of their loan losses.

More devastating proof that this is a collapse of the whole banking system and not simply isolated banks was revealed this week in what happened to the marketability of IOUs (blocs of \$100,000 or more deposits negotiated with corporations) of those banks exposed as financially troubled. Since these IOUs reflect a bank's creditworthiness in the eyes of corporate depositors, one would have expected these corporations either to demand much higher interest rates to offset the risk, or to start panic runs of the kind which Federal Reserve Chairman Arthur Burns this week warned might occur. What actually happened was that interest rates on such deposits — including those of exposed "problem"

banks — plunged to everyone's surprise. The reason is simple; the collapse of the loan and investment business by these banks is occurring so rapidly that they themselves are liquidating their own deposits at record rates. Over the past three weeks the New York banks alone have reduced their holdings of these IOUs by \$2.1 billion. This is an actual deposit run — only one induced by the banks themselves in response to the collapse of banking activity in general rather than by depositors in response to the shakiness of individual banks. This has created such an excess of funds that corporations which are desperate to earn income are now investing in banks they would not previously touch with a ten-foot pole.

III. CURRENCY CRISIS

During the past ten weeks, international banks, multinational corporations, and other affiliates of the New York banking community organized a run on the Italian lira, which reduced Italian currency reserves from \$1.8 billion ten weeks ago to \$500 million at the point that the Bank of Italy threw up its hands and shut down the foreign exchange market and stock exchange. In turn, massive pressure "spilled over" this week onto the French franc, British pound, and other currencies of the OECD deficit area, forcing the Bank of France to intervene with several hundred million dollars of its mostly borrowed foreign exchange reserves.

The stated motive of the New York financial community's Italian maneuver, coordinated between Chase Manhattan Bank chairman David Rockefeller and FIAT President Giovanni Agnelli, is to solve the domestic political crisis in Italy through external brute force. The program of the New York banks, which represents de facto the present foreign policy of the United States, is a 15 to 20 per cent devaluation of the weaker European currencies, a consequent cut in Europe's share of world production and international trade, and a teeth-breaking austerity policy for the European workers. This policy, is openly discussed in the New York financial community and the European press.

What prompted Mr. Rockefeller and his collaborators to push a creditor such as Italy to the brink of bankruptcy even though such a bankruptcy would stagger the international banking community? Italy's present \$500 million in reserves represents approximately one-seventh of external debt payments due to banks in the coming year. In fact, the intentional provocation of a currency crisis in Europe reflects principally the horrified awareness of financial circles that such a crisis must emerge whatever their actions during the next several weeks, and comprises an attempt to steer the crisis in a direction favorable to their financial interests.

IV. EUROPE AND JAPAN — AN OVERVIEW

Europe began a second round of trade and international production contraction during the fourth quarter of the past year, for reasons similar to the beginning of the second ratchet of production cutbacks in the United States. Over the year, European national sector had been forced to drastically cut imports as export markets stagnated. This fact provides the principal explanation for positive balance of payments positions reported for 1975. A severe contraction in international borrowing also contributed to this cosmetic "recovery", (Table 1a and 1b) while actual production fell.

Under the orders from the International Monetary Fund and the Organization for Economic Cooperation and Development, Western Europe and Japan undertook last May and June an internal stimulation program which in-

jected \$15 billion into the national sector economies within a three month period. (see Table 2) The Auto, housing, and other select sectors were propped through an expansion of the money supply at annual rates exceeding 20 per cent. This adrenalin shot which created artificial consumer demands mitigated but could not prevent production cuts of 10-25 per cent in basic capital goods industries — the guts of these economies (Table 3) To production cuts caused by decreased demand were added those necessitated by the need to slash operating and capital investment expenses to free funds for corporate debt service. These policies resulted in fantastic illiquidity in the corporate sector.

"Many enterprises are bankrupt but don't know it yet," widely-read West German industrial journal *Handelsblatt* reported (December 22, 1975). "They display profits that stem not from economic gain but dissolving reserves, up-valuing inventory... heavier outside borrowing."

The growing corporate illiquidity in turn, increased the demands on national sector banking systems already overstrained by their shares of bad loans to LDCs, tanker companies, municipalities, etc. "The period seems to have come to an end," states the December 1975 report of the West German central bank, the Bundesbank, "in which corporations, because of pronounced cuts in investment activity and decreases in inventory, can draw on liquidity from current earnings to redeem their bank debts or form financial reserves."

By the fourth quarter 1975, raw materials stocks and corporate reserves had been depleted causing the balance of payments situation to fall through. Bills for increased imports consumed in the artificially created demand boomlet came due simultaneously with a severe fall off in exports to the East bloc, (which was shut off to the credit markets) according to a IMF-Rockefeller-NATO political decision and to OPEC, whose funds declined as the West cut oil imports. The corporate demands for domestic banking funds produced liquidity snaps such as that in Britain where in the first week in January the Bank of England had to release its 1 per cent Special Deposit banking reserves in an emergency action. In turn, the revelation of exacerbated balance of payment problems and demand for overseas funds greatly contributed to runs in January on the lira, franc, and pound (see France below).

The Two Tier Plan

To maintain the ability of these crippled national economies to continue to pay their debts a while longer, a "two tier" currency plan is currently in effect for the other 5 nations that met with the Rambouillet in France last November — Britain, Italy, West Germany, France and Japan.

As proposed one year ago by Willy Brandt, chairman of the West German Social Democratic Party, the plan calls for further austerity cutbacks in Italy and Britain, the proverbial sick men of Europe, and satisfaction of credit demands via hyperinflationary central bank printing press operations elsewhere. This policy is already producing corporate and banking collapse throughout the advanced sector along with the more publicized currency crisis.

The precarious liquidity positions, of the major U.S. international banks — a fact which has recently been made public — has drastically reduced the possibility of additional international loans to this sector. European and Japanese corporate loan demand projected to climb back to 1974 levels and no prospects for funding either domestically or on international markets, analysts and corporate officials are grow-

ing uneasy about an impending wave of corporate bankruptcies.

France, will need somewhere near its 1974 Eurocurrency borrowings of \$3.3 billion, according to one New York bank's international economist, up from a mere \$450 million last year.

"U.S. banks are very nervous about loans to West Europe and Japan," the same source indicated, "especially given their borrowing for debt financing that's not a very attractive investment ... We must look at loans one by one, conservatively, with all these REITS and tanker loans we have and the high reserve ratios we must carry since the Washington Post disclosures on Chase and Citibank. And the European banks are nervous, too, look at the Pfalts Kreditbank (a West German bank which went under two weeks ago) and other recent bank failures in Germany. British banks have the same problem."

"France and Germany will have to stimulate domestic demand," the source continued, "do not expect an export upswing: force down the interest rate by increasing the money supply, making as much money available to the corporations as they need."

This is already happening.

Inside sources at the Paris branch of a major New York bank told IPS last month that French President Giscard d'Estaing is secretly planning a Fr. 120 billion credit expansion to commercial banks in 1976 explicitly for the purpose of financing corporate deficits and debt service. This approaches the equivalent of one third of the French national budget.

In West Germany, a similar situation has existed since October with a 23 per cent annual rate of growth of money supply.

In Italy, if a moratoria on dollar-denominated debt is not instituted the IMF will impose severe austerity. As announced Jan. 28 by Italian Treasury Minister Colombo, conditions for the \$450 million IMF loan under negotiation include drastic government spending cuts, industrial credit restrictions, and speeding up of production.

Similar policies continue in effect in Great Britain and will be imposed soon in Japan if recent proposals by Deputy Prime Minister Takeo Fukuda are followed.

BRD: The End of the Schwindelkonjunktur

Over the last three months, the chief characteristic that has determined West German economic life has been the total collapse of the so-called *schwindelkonjunktur* or fraudulent upswing. This phony recovery, — fueled by the tremendous expansion of consumer credit — was capable of only masking the weaknesses of the economy, not doing away with them. When the export picture deteriorated during the last quarter of 1975, as trade with the East bloc and OPEC nations fell off drastically, the so-called recovery vanished.

As steep as the drop in production in basic industry was over the last year, it would have been far worse were it not for the artificial propping up of the auto sector through consumer credit. This injection ballooned to one tenth the total increase in all new credit during the Aug-Oct. period. Domestic sales for the year rose by 30 per cent, while foreign sales fell 15 per cent, with the key U.S. market suffering a 22 per cent drop. Through such manipulations the industry, which provides demand stimulus for other sectors such as steel, was able to show a modest 3 per cent increase in overall production.

A similar operation was performed in the housing sector where housing loans were twice the volume of consumer credit. A slight variation was used for the machine tool sector, where tax breaks for capital improvements hyped-up domestic orders by 14 per cent; this however was not able to offset a 25 per cent drop in foreign orders, producing a net decrease in production of 8 per cent.

As the Handelsblatt indicated last month, the fag end of the government's credit injection has hit the already nearly illiquid companies quite hard. "The upvaluation of assets may make the books look good," the paper reported, "but then comes debt service, payment for past investments, delivery of pastpaid goods, etc." The fourth quarter spurt in bank lending, over DM 11 billion, was pure refinancing of corporate debt. As workers savings declined due to prolonged unemployment, (reflected in the low growth rate of the broadly-defined money supply (M2) compared to the accelerating growth of the narrowly-defined money supply (M1)) banks increasingly drew their resources from the Bundesbank, borrowing ten day money (DM 4.5 billion at its peak) to make long-term loans to their corporate customers.

The entire West German banking system is thus extremely sensitive to drops in corporate profits and rollover pressure on consumer credit-related loans. The Pfaltz Kreditbank, a consumer credit institution of considerable size, was closed in mid-January by the government control board for "excessive indebtedness," — the third major bank this month to have either collapsed or to be reported near collapse. The head of Citibank's Frankfurt office told IPS bluntly that "even the top addresses" of the German banks are on the U.S. Controller of the Currency's secret list of problem banks. The Italian paper, Corriere de la Serra has predicted that an additional thirty banks will soon have to be closed.

The Lost Gamble

The recent drop in the unsupported value of the franc in the wake of the collapse of the lira was a direct result of France's inability to maintain drastic levels of import cutbacks. Without such cutbacks — the artificial prop behind France's improved 1975 balance of payment's picture — the French economy is quickly revealed to be in disastrous shape.

The entire corporate sector is being overwhelmed by an enormous debt burden. Le Monde, the major French daily, reported last month that the annual debt service of major French concerns averages 20-25 per cent of their turnover, including the following selected debt ratio figures: Michelin, 26.3 per cent; Cements du Nord 25.4 per cent; Renault Industries, 19.5 per cent; Taittinger Champagnes, 15.2 per cent. The state electric monopoly, the EDF, commits its entire annual borrowings of over Fr. 4 billion to debt service.

Under such conditions, all of the Fr. 120 billion in Giscard's heralded "relaunching" program will be sucked into debt service.

"The government has lost its gamble," Le Monde stated on Jan. 19, commenting on the dismal state of the economy and of a reported trade deficit for last month of some Fr. 289 million. Following the release of the trade figures, Banque Parisbas promptly predicted that France's 1976 balance of payments picture will swing back to a deficit of 1974 proportions — somewhere in the Fr. 12 to 15 billion range.

"People don't realize how fast the franc will fall ... much faster than the lira," a Forex trader at a New York brokerage house told IPS. In the first week of the lira crisis, the Banque France spent \$1 billion to support the country's

sagging currency, with undisclosed additional amounts added by the U.S. Federal Reserve.

BRITAIN: The Sick Man Grows Sicker

The already sick British economy deteriorated rapidly over the last quarter of 1975. Final production figures showed a drop of six index points; meanwhile unemployment has shot up to 6.1 per cent — the highest figure since 1939 — with more than 220,000 thrown out of work in the mid-January to mid-February period alone.

Under newly announced government plans, the government's borrowing will total 12 billion - or 25 per cent of the entire government budget for 1976 and 10 per cent of the year's projected Gross National Product.

While French and German auto production was maintained last year by artificial stimulation the British auto industry was allowed to fall apart; domestic sales and exports are down markedly. Steel and other basic industry, which are intimately tied to the fate of auto, are collapsing as well.

Waving the January unemployment figures as its justification for extreme action, the government has called for additional belt tightening — another year of wage controls, cutbacks in credit for industrial production, and a decrease in the rate of the money supply expansion down from 15 per cent in 1975, to 4 per cent.

ITALY: Down to the Wire

The 1975 "miracle" turnaround in Italy's balance of trade (table 1) was accomplished through a 10 per cent drop in imports along with a 15 per cent rise in exports (the later being largely reflective of credits to the Soviet Bloc in the first three quarters of 1975.) Overall industrial production fell 12 per cent under severe import restrictions requiring large advance deposits and under the maintenance of a 12 per cent plus minimum lending rate through the year. Corporate deficits rose \$19 billion during 1975 to \$45 billion, more than double the 1974 figure. Speculation against the lira was in part triggered by official projections of an increased balance of trade deficit in 1976 of from \$5 to \$4 billion.

The new credit and budget restrictions now asked by the IMF will reportedly exceed those measures stipulated by the EEC late last year for renewal of its \$1.8 billion outstanding loan to Italy. The EEC conditions for 1976 included a 13 trillion lira credit ceiling and the elimination of a 14.8 trillion lira budget deficit. New York bankers estimate that this will mean severe privation to Italian industry and greatly increased unemployment.

JAPAN: Production Cut in Effort to Halt Slide of Yen

The pressure on the yen at the end of the last year has now been relieved by policy decision of the Bank of Japan under the control of Deputy Premier Takeo Fukuda to cut production in basic industry. According to sources at the Bank's New York office, the cuts will be even more severe than last year's 10-15 per cent.

As was the case with West Germany, France, and the U.S. the auto sector kept the economy from immediately going down for the count. Overall, auto sales rose 20 per cent, buoyed by gains in the U.S. market where Japan replaced West Germany as the major supplier of imports.

Under a regime of forced import cutbacks, Japanese corporations became net repayers on the U.S. and Euro currency markets by the end of last year. This caused a tremendous demand for dollars which in turn drove the yen down. Under conditions similar to those in France where industry is screaming for lower interest rates so that it can refinance its debt, the Bank of Japan has ruled that there will be no additional loans, that bank interest rates will be kept high to attract dollar inflows — all so that the weak yen might be supported.

It is now openly predicted in the Japanese press that the strategy for this year's spring wage negotiations will be to first offer a 10 per cent (below inflation) wage increase ceiling and then, once the issue is settled, force several million additional layoffs. This roughly corresponds to the number of workers over-employed under the patriarchy system for whose paychecks the industries have run out of reserve funds.

INTERNATIONAL MARKETS

The solvency of the European corporate sector, and even the debt-servicing abilities of countries such as Britain and Italy, take second place to the dangers that the downturn in international trade has set into motion. The fuse which might detonate the world financial structure at any moment is \$40 billion in very short-term debt of the developing countries. Of this, \$30 billion was extended over the eighteen months between June 1974 and December 1975, mostly by U.S. banks and their Eurodollar subsidiaries. The Administration has neglected to inform Congress and the public that this unprecedented growth in bank illiquidity provided the principal means of financing the Third World's massive balance-of-payments deficits during 1974 and 1975. The single underpinning for these loans is the continuity of Third World commodity exports, which were propped up by the temporary effect of government spending in Western Europe and the United States. In effect, the continued flow of internationally-traded commodities, even at half of their peak 1974 prices, represents interest payments on Third World debt, and the last margin of income to permit refinancing. (see charts)

When Ford's advisors were submitting their final drafts of the State of the Union message, the world economy turned the corner, when the international price of copper dropped below the cost of production. To sustain the copper trade after the 1974 price collapse, the banking creditors of the Third World provided a further \$1.5 billion to sustain stockpiles in private hands, held in anticipation of economic recovery. It is now common knowledge in financial circles that this flimsy arrangement is in the process of collapse.

In addition, the \$35 billion of short-term debt extended to tanker operators came under international scrutiny last week when a Greek shipping group defaulted on several hundred millions of bank debt. The tanker industry has collapsed, with one-third of capacity in mothballs, as a direct result of the 20 per cent drop in European foreign-oil consumption. With a renewed downturn in European industry, the banks' gamble in tankers will have lost.

TABLE IA: EUROPEAN AND JAPANESE TRADE TRENDS

COUNTRY	PERCENT CHANGE EXPORTS 1974-5	PERCENT CHANGE IMPORTS 1974-5	TRADE BALANCE (billions) (Current account balance)		
			1974	1975	1976 projected
FRANCE	+118%	-8%	-FF 16 (--)	+FF 6 --)	-FF 10 --)
ITALY	+15%	-10%	-\$11 (-\$4)	-\$3.5 -\$1.5)	-\$5 -\$3)
WEST GERMANY	-4% (+10% volume)	+3%	+\$19.5 (--)	+\$14 +3)	+\$10 +1)
JAPAN	+0.5%	-7%	-\$6.6 (--)	-\$2 --)	(--) (--)
GREAT BRITAIN	+15%	+3%	L5.2 (L3.7)	L3.2 L1.7)	(--) (--)

TABLE IB: INTERNATIONAL LENDING TO EUROPE AND JAPAN (in billions of dollars)

	1974	1975
U.S. Bank Credits to Advanced Nations (excluding U.S.)	6.9	-2.4 (net repayment)
to Japan	4.8	-2.7 (net repayment)
Eurocurrency Credits to Advanced Nations (including U.S.)	20.9	6.4
to France, Italy & Britain	11.2	0.9
U.S. and Eurobond Foreign Bond Issues to Advanced Nations	3.0	9.1

Note: Cutbacks in short and medium term currency lendings were not at all compensated for by the slight rise in long term bond issues. These, in any case, were not for investment funds but were borrowed in order to retire the previous year's short term debt.

Source: Morgan Guaranty Trust Co., World Financial Markets, Dec., 1975

TABLE II: GOVERNMENT DEFLATION PLANS BY NATIONAL SECTORS

U.S.	\$26 billion
France	Fr 30 billion
Italy	\$5.2 billion
BRD	DM 75 billion
U.K.	L145 million
Japan	Y2 trillion

TABLE IIIA: INDUSTRIAL PRODUCTION & EXPORTS 1975

<u>West Germany</u>		<u>France</u>	
Steel	-24%	Steel	-20.4%
Chemical	-16%	Chemical	-18%
Machinery	-9%	Machinery	-24%
Textiles & Clothing	-15%	Oil Refining	-20%
Construction	-10%	Exports (value)	
Machine tools	-8%	(2nd half, 1975)	
Automobile	+3%	Iron & Steel	-20%
		Chemical	-11%
1975 Exports (value)		Fertilizers	-68%
Auto	-15%	Metals Mfr	-25%
Auto to U.S.	-22%	Auto sales	+15%
Machine tools	-25%		

<u>Japan</u>		<u>Great Britain</u> (Index Avg (Dec 1970=100))	
		1974	4th Qtr., 1975
Steel	-12.7%	Overall prod.	106
Machinery	-10%	Manufacturing	107
Chemical	-8%	Chem. Mfr.	125
Textile	-16%	Metals Mfr.	92
Auto	-16%	Engineering	105
(no figures available for exports)		Automobiles	97

(no figures available for exports)

TABLE IIIB: WORLD STEEL PRODUCTION: 1974 vs. 1975 (m. tons)

	1975	1974	% change
Belgium	11.582	16.227	-28.6
Germany	40.418	53.232	-24.0
France	21.520	27.021	-20.4
Italy	21.852	23.804	-8.2
Luxembourg	4.624	6.447	-28.3
Netherlands	4.819	5.837	-17.4
Denmark	0.557	0.535	+3.9
U.K.	19.833	22.404	-11.5
TOTAL EEC	125.205	155.508	-19.5
U.S.	105.972	131.992	-19.7
Japan	102.210	117.131	-12.7
Spain	11.095	11.502	-3.5
Canada	13.015	13.606	-4.3
Soviet Union	142.0	136.2	+4.3
Comecon excl. Soviet Union	53.6	48.9	+9.6
China	36.0	27.0	+11.1
Others	62.80	168.06	-62.64
TOTAL	651.8	799.9	-8.2