Currency Chaos Is Hurting Japan — Deliberately

Using their control over world petrodollar flows, a group of London and New York investment banks were able to force the Japanese yen up 7 percent last month, to a record level of 247 yen to the dollar. The October rise was almost as much as the 11 percent increase over the previous nine months. During the same period, the U.S. Treasury Department — deeply involved in currency operations against the U.S. dollar by the same banking firms — rebuffed all attempts at compromise by Japanese steelmakers and approved an antidumping suit against them; U.S. steel firms had reportedly been incited to launch such suits by the Administration's own trade negotiator, Robert Strauss.

JAPAN ECONOMIC SURVEY

Japanese bankers say that the combination of U.S. protectionism and the outrageous rise of the yen will almost certainly throw the export-dependent Japanese economy into deep recession. In recent interviews several banking spokesmen pointed out that because of the previous appreciation of the yen, Japan's production had been flat since January. (see *Graph 1*) They are even more frightened that a general collapse of the dollar may lead to an international monetary crisis and global depression.

In contrast to earlier pressures on Japan, this time, the investment houses behind the yen rush admit, there are no immediate *economic* objectives involved in their sledge-hammer tactics.

The assault was begun following the utter failure suffered by these London and Wall Street bankers at the International Monetary Fund meeting last month. Prior to that meeting, officials from the powerful London-linked Lazard Freres investment house, Chase Manhattan Bank, and the allied Brookings Institution think tank uniformly urged a "soft" posture toward Japan. While demanding reflation from Europe, they insisted that Japan had done as much as it could regarding reflation and its payments surplus, and that the burden would have to be shifted to other countries.

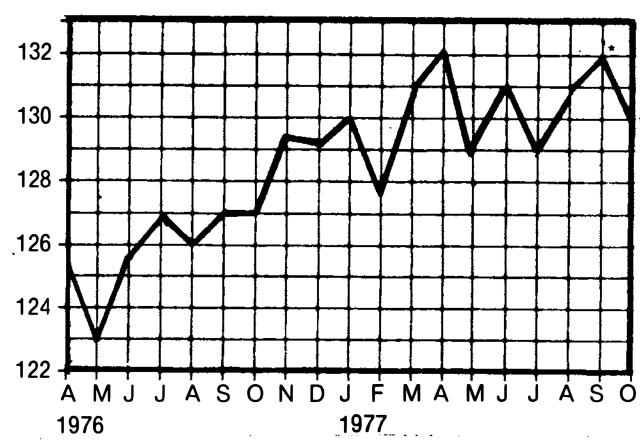
In an interview this week a top official at an investment bank closely tied to Lazard Freres explained what happened to this "soft" approach. "From an economic standpoint it doesn't really matter if the yen is at 260 or 240 (yen to the dollar), or whether the reflation program is \$7.5 billion or \$10 billion," he said. "It may make a difference to Japan's internal economy, but not to world recovery. You must understand that U.S. Treasury Secretary Blumenthal's motivation is not economic but political."

"The Japanese and the Europeans resisted the reflation line that (British Chancellor of the Exchequer) Healey and Blumenthal were pushing at the IMF meeting" he continued. "Now, Japan has to be made to surrender to the yen appreciation, to show that resistance is impossible. Plus, Japan will then have no choice but to ally with the U.S. to push reflation on all the other countries."

This banker indicated that the U.S. Treasury Department's decision on steel dumping was part of the same policy, and added that he didn't expect the Healey-Blumenthal economic reflation program to succeed globally for two or three years. Thus, as the foregoing indicated, these investment houses are, for the present, simply "destabilizing" Japan's economy to put its political leadership off blance, isolate Japan internationally, and forestall the coalescence of any coherent opposition.

Graph 1

Japan's Industrial Production Index
(1970 = 100)
(seasonally adjusted)



Note: *September & October are MITI Estimates
Source: Japanese Ministry of International Trade & Industry

A Failure of Will

This strategy has been largely successful in Japan, at least so far, in contrast to the same London-Lazard grouping's failure to cow West Germany and France. At each point that the Bank of Japan wanted to resist the yen appreciation, Premier Takeo Fukuda and his supporters advocated capitulation, mainly out of fear that resistance would provoke even harsher measures against the Japanese economy. At times Fukuda has even gone so far as to indicate in public that a yen appreciation might have beneficial effects against inflation. The press has repeatedly blasted Fukuda for such statements, since they only spur the yen's rise.

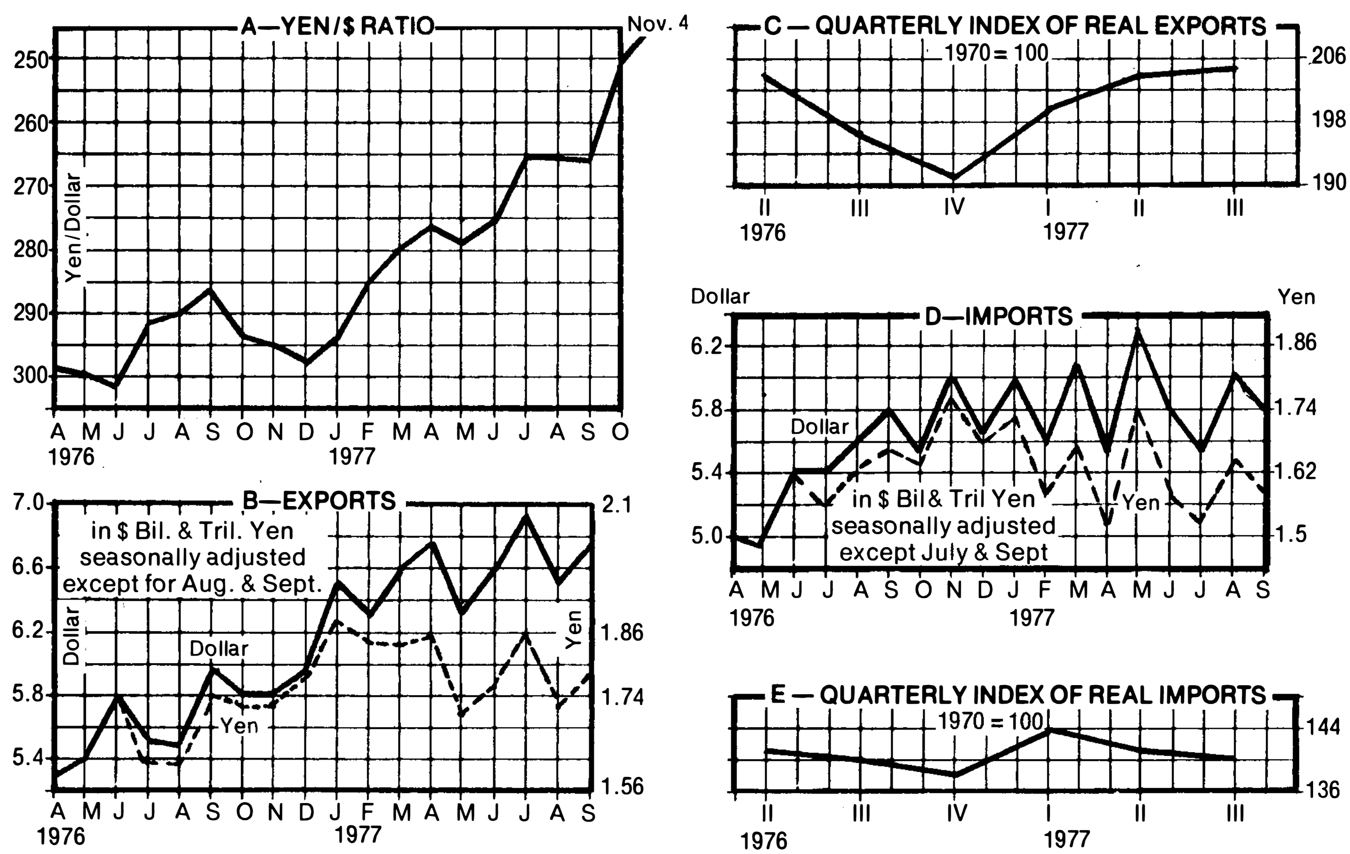
Moreover, the Bank of Japan's attempts at resistance have been hamstrung by a futile Maginot Line approach. It has tried to stop the rise through intervention at successively higher target rates. At each barrier the investment bankers' group has broken through with daily currency flows up to $750 million.

So far, most Japanese business has concentrated not on resistance, but on adjustment. Business leaders have already raised the call for an early repetition of the $7.5 billion stimulation program announced in September, whose effects have already been negated by the yen rise, as well as bailouts of injured industries.

Despite the current atmosphere of paralysis, Japan's businessmen know they will have to act; they cannot remain passive and let the economy be destroyed. The most advanced thinking among these circles is expressed by the "resource faction," whose views were recently expressed in a speech given by Liberal Democratic Party leader Yasuhiro Nakasone, a rumored candidate for Foreign Minister in a likely upcoming cabinet reshuffle. Nakasone deplored the current "drifting" of Japan's foreign policy, and proposed that Japan act to secure close ties to OPEC and to transform Southeast Asia into a region of "peace and prosperity" through international cooperation on development programs. Several days later, at a meeting with Australian businessmen, Tokyu Corporation chairman Noboro Gotoh, a Nakasone supporter, proposed the creation of an Asian Common Market, focused on the industrialization of the region and with Japan and Australia as its nuclei.

The key to Japan's future is whether the "resource faction" can link the broad center of Japanese business to its development program. The center group has no substantive objections to the program. In fact, two months ago an organization of the center group, Keizai Doyukai — the Japanese affiliate of the U.S. Committee for Economic Development — proposed a multibillion-dollar joint OPEC-Japan development fund for Southeast Asia. But as a Brookings Institution economist pointed out, Japanese business will never invest heavily in such a venture unless there is assurance of a stable world recovery to provide the markets for the products of such enterprises and to insure against default by the developing countries.

Graph 2
Japan's Trade Indicators



Source: Japanese Ministry of International Trade and Industry

At the present time, the Brookings economist underlined, Japan's private foreign investment is stagnating even through Japan is loaded with excess dollars, precisely because business is afraid to invest. Many firms are even abandoning existing ventures, with the wholesale flight from Brazil as only the most dramatic case. The program of Nakasone and Keizai Doyukai cannot succeed unless Japan obtains cooperation in the U.S. and Europe to secure genuine world recovery. Yet it was exactly on this point that Nakasone was most vague in his speech.

With the notable exception of its recent energy deals with the Soviet Union, Japan has failed to obtain significant allies for defense against the reflation forces, let alone for positive action, either in Europe or among circles in the U.S. opposed to the "Tory" policies of Blumenthal and his allies. As a result, business in Japan has remained in a paralysis of fear.

The investment house executive cited above commented, "Sure, they'll try to resist and gain allies, but they won't have time to do anything before the effects of the yen rise set in." For the present, Japan has been successfully kept off blance. This could change very quickly once business in and out of Japan realizes that something must be done, but for the moment Japan has been effectively isolated.

Time Running Out

Japanese business is increasingly aware that it has little time left to avert disaster. For months Japan has been perched on the brink of all-out recession. Estimated production levels for October are no higher than those of last January. This predicament is the result of the 11 percent appreciation of the yen from January through September. Exports, the lifeblood of the economy, have been stagnant in dollar terms at the $6.7 billion level since March. In yen terms — the terms that determine the financial viability of the export firms — exports have fallen. In real terms — the terms that determine exports' ability to stimulate the rest of the economy — exports in September were no higher than in March of 1976! (See *Graph 2 B* and *C*)

Since growth in exports has been Japan's sole source of production increases and financial stability since the 1974-75 recession, the collapse of exports was enough to threaten serious new economic troubles. Even before the October yen appreciation the export picture was getting worse. September contracts for trading firms which sell 60 percent of Japan's exports were down 5 percent from year-before figures in dollar terms. The new appreciation will sharply cut Japan's real exports, and a major bank reports that every export industry except auto will have to sell at a loss if the yen remains above 250. As a result, the illiquid corporations in Japan will be forced to institute cost-cutting measures such as capital investment cuts and inventory liquidation, undercutting the whole economy.

The Lazard-linked investment house official said he understood Japan's predicament perfectly. "The yen appreciation will throw them into recession, unless they launch an absolutely massive reflation program, perhaps two or three times the $7.5 billion they announced in September. They won't have any choice." This would mean "intolerable inflation," he said, and therefore the Japanese could have "no choice but to ally with the U.S. and force everyone else to reflate also. That is the only way they could avoid chaos." Recovery is still years away, he added, "and I must emphasize again that the motivation behind Blumenthal's actions is political, not economic."

Turning reality on its head, most newspaper reports have ignored the grim implications of Japan's production figures and instead emphasized the monumental Japanese trade surplus. This record surplus — it could reach $17 billion this year — is due not to exports, but to the steady fall in imports. (*Graph 2 D* and *E*). And imports, in turn, fell because of the stagnation in production — caused by the flatness of exports. In other words, Japan has such a large trade surplus because its exports are too low!

Friends and Enemies

Japan's future depends on whether it can secure international allies. Naturally, there is no real support in Japan for the immediate London-led campaign against the Japanese economy, but the same London and New York bankers do have powerful friends who support their long-range orientation: low growth and austerity. This attitude is exemplified by the Industrial Planning Council, headed by a long-time Fukuda ally, Takeshi Sakurada. In his capacity as head of the Employer's Federation, Sakurada warned that the yen appreciation was an even worse shock than was the 1973-74 oil crisis. Therefore, many firms would have to refuse wage increases this year, he predicted, and others would have to actually reduce wages. At stake is an immediate 10 percent cut in real wages.

Sakurada's group has strong influence over Fukuda, but Fukuda's own credibility is weak. Known as the "economic wizard" when he took office last December, he is now derided as the "god of poverty." It is expected that Fukuda will soon be forced to reshuffle his cabinet and bring his political opponents into powerful posts.

The opposite pole to the group represented by Sakurada is marked by Japan's recent breakthroughs in energy cooperation with the USSR. Japan will sell the Soviet Union four atomic power plants as part of a deal to be finalized Nov. 15 between the two countries, according to the Tokyo daily Mainichi, and the agreement includes a call for close collaboration on fusion power research. There is speculation that the deal will also clear the way for the Soviets to assist in enriching Japan's depleted nuclear fuels, an operation hitherto monopolized by the U.S.

The atomic energy agreement follows the announcement two weeks ago of a major oil strike off the Soviet Sakhalin islands, believed to be the largest single oil field in all of Asia. Its development could lead to a new source of fuel supplies for Japan, which is now virtually dependent on U.S.-controlled flows of Mideast oil. Involved in negotiations on developing the field are Japanese firms which figure as part of the "resource faction"; the United States' Gulf Oil is also a participant.

The rest of the international picture, however, remains dismal. The Bank of Japan had looked to West Germany and Switzerland for cooperation, and had leaked to the press that it had agreements for coordination among the central banks of the three countries against currency speculation. But approximately 10 days ago, reports appeared that the West Germans and Swiss had reneged on their agreement, and now it appears that West German and Swiss banks are among the biggest buyers of yen.

Many of the private banks in Japan hoped for political support from those American bankers who opposed the Blumentahl "toilet paper dollar" crowd in favor of Arthur Burns' attempts to defend the dollar, including the Rockefeller and Harriman interests as well as institutions like Citibank and Bank of America. But at least one Harriman spokesman, Robert Roosa of Brown Bros., Harriman's investment bank, indicated in an interview this week that the Harriman-Rockefeller interests have little positive to say beyond a narrow interest in defense of the dollar and sentiments against protectionism.

Others in Japan looked to the Southwest-based industrialist forces in this country led by men like John Connally and former deputy Defense Secretary William Clements. But although Connally and Clements themselves have consistently attacked protectionism and dollar depreciation, a sampling of Texas bankers and businessmen — Connally's base — interviewed by this reporter revealed that they had been suckered into at least lukewarm support of Blumenthal's protectionist line. A Texas-Japan meeting last month in Tokyo failed to reach any significant breakthroughs in cooperation.

Both the Harriman-Rockefeller types and U.S. industrialists will find very soon that they must shift into a far more active posture if they are not to follow Japan into London-engineered economic chaos. As of this writing, they have not yet done so.

—Richard Katz

China's Teng Seeks World 'United Front' Against Soviets

Teng Hsiao-ping, deputy premier of China and third-ranking member of the Peking Communist hierachy, took China's long-standing vendetta against the Soviet Union to a new level of intensity last week in an interview with Claude Roussel, chairman and managing director of the French wire service, Agence France-Presse. During the Oct. 21 interview, Teng broke all precedent with a call for a *worldwide* united front against the Soviet Union using economic warfare to destroy the Soviet economy, and attacked those nations which sell technology or food to the Soviets for "appeasement." (A transcript of portions of the interview which discuss the Soviets and other foreign policy issues appear below.)

CHINA

China has stepped up its diplomatic organizing for this "anti-Soviet" united front, as reflected by the spate of foreign dignitaries invited to Peking in the last two weeks. The list is headed by Paul T.K. Lin, professor at the center for East Asian Studies at McGill University in Toronto, Canada. Lin was once a secretary to Chou En-Lai and is a key private liaison between China, western Maoist groups, and western pro-China lobbies who have been using China as a bludgeon against the Soviets. Mr. Lin met Teng on Oct. 15. The day before, politburo member Chi Teng-kuei met with Evelyn de Rothschild, who is chairman of the board of the British magazine, *The Economist* and an important link to the City of London financial circles working with the likes of Mr. Lin to use China for their own purposes.

Other visitors during the last two weeks of October included General Stig Synnergren, Supreme Commander of the Swedish Armed Forces; Edward Heath, former Prime Minister of Britain; William Scranton, former U.S. ambassador to the UN; Brian Talboys, New Zealand's Minister of Foreign Affairs and Deputy Prime Minister; a delegation from the National Committee on U.S.-China relations, and several prominent private citizens and members of parliament from Australia and Britain. The Chinese aim in these visits is to drum up support for Teng's "united front." China was apparently successful with West Germany's Manfred Wörner, a Christian Socialist parliamentarian who returned from a visit in September sounding much like Teng himself. In a recent speech, "Manchurian candidate" Wörner recited, "We must cease pursuing the policy of bowing step by step to the big powers under the illusion that this will be conducive to transformation and peace. We must stop following the policy of promoting the buildup of Soviet power through financial technological assistance."

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The French wire service, Agence France-Presse, recently released an interview with China's Deputy Premier Teng Hsiao-ping. Here, excerpts from the Oct. 21 interview.

On world struggle against the Soviets: The global war plan cooked up by the Soviet Union must be destroyed. I hope that this effort will be made by the whole world — the Third World, the Second World and even including the First World, the United States. This is one of the ways to delay an inevitable world war. The war is inevitable because of Soviet-American rivalry although the principal danger is from the Soviet Union because of its