Miller, Blumenthal Set To Put NYC Through The Wringer

New York City continued its agonizing plunge toward social and political chaos last week, as the Senate Banking Committee finally began hearings on the proposed $2 billion austerity-based federal loan guarantee package. By week's end, the city was still tottering on the edge of a manipulated bankruptcy, while the nation was treated to a display of "austerity" politics.

Sources in the banking community and Sen. William Proxmire's office report that a consensus now exists between Proxmire, Federal Reserve Chairman Miller,

BUSINESS OUTLOOK

Treasury Secretary Blumenthal, London-linked merchant banking interests and their spokesman, Municipal Assistance Corporation chairman Felix Rohatyn, and the stupid leadership of the nation's commercial banks that New York City is to be made into "an example of fiscal responsibility."

The city is to be forced to undergo even more severe service cuts, layoffs, and so on, than outlined in Mayor Ed Koch's "austerity budget." New York's future is being compared openly to that of a Third World country placed under an International Monetary Fund dictatorship. Such sources fully expect riots and civil disturbances and are prepared, in the words of one Senate aide, to "crush all opposition with full force" — even if it means the use of National Guard troops.

Proxmire and others are already pointing to the so-called tax revolt as "evidence" of a "national mandate" for austerity in New York City. Whatever it takes, said a Senate aide, "New York will be forced to live within its means . . . so will everyone else. . . ."

While the threat of an immediate bankruptcy eased somewhat this week, our sources report that it is still very much a live option. Miller, Blumenthal, and Rohatyn can pull the plug on the outstanding $14 billion in city, state, and MAC debt at almost any time — regardless of whether the Congress passes an aid program. This fact is being used to blackmail the banks into "going all the way" on the genocidal austerity drive.

But, as one Washington-based, London-linked reporter indicated, a bankruptcy is a political question which would "shake the country from top to bottom." Sources at leading think tanks involved in contingency planning for a city crisis, report that it is well known that a city bankruptcy would "nail the lid on President Carter's political coffin and likely drive him from office."

Despite their public protestations to the contrary, knowledgeable banking community insiders report that Miller, Blumenthal, Proxmire, and Rohatyn favor a bankruptcy — provided they can find somebody to blame it on. The city unions, and the police union in particular, shape up as the likely candidates for "chief patsies."

Austerity Pact

"We in New York know the meaning of the word austerity," Mayor Koch bragged at the first day's hearings of Proxmire's banking committee. Only the night before, he had concluded what one trade union official termed "the worst major trade union contract in recent history." The agreement, which has yet to be ratified by 250,000 union members, would give city workers a little more than 5 percent in wage increases over its two-year life.

"We have gotten our workers to take a real cut in their incomes," said Koch. Not good enough, said Proxmire. "Under normal conditions I might say that this is a good contract. But the city's situation is not normal . . . services must be cut more and workers will have to suffer. . . . That is the way things are. . . ."

Koch and Rohatyn have reportedly told Proxmire that they are prepared to implement what is termed a worst-case scenario for major budget cuts, regardless of whether they receive any federal aid. The plans — which have yet to be made fully public — call for more than 20,000 additional layoffs beyond the 20,000 specified in the so-called city four-year plan (the city has laid off more than 60,000 workers since 1975), drastic cutbacks in the municipal, hospital, and university systems, and school closings. Proxmire believes that the plans, which would devastate existing city services, will amount to a budget cut of more than $1 billion. MAC's Rohatyn reportedly agrees.

"The City is already in effective receivership," Koch told the committee, "We tolerate it because, I as Mayor am willing to do what a receiver like the Emergency Financial Control Board (the city's austerity monitor — ed.) demands before it orders us to do it. . . . I fully agree with all budget cuts. . . ."

Useless Deal

Proxmire, (who has been assigned the hatchet man role in New York's fiscal drama), peppered Koch, Blumenthal, Rohatyn and New York Governor Hugh Carey with a combination of questions and facts designed to cast aspersion on the proposed city loan guarantee package. This suits Rohatyn and Blumenthal fine — they are reportedly using Proxmire as a foil to gain commitments to purchase hundreds of millions in additional

MAC paper through the banks and the union pension funds. The Wisconsin Democrat is prepared to roast banking community representatives when they testify this week, sources report. Koch has also found Proxmire useful. Aides to the Mayor report that it was Proxmire's threat to cancel the hearings unless a contract agreement was reached that helped push union leaders behind the austerity pact.

Despite his previous statements that New York should receive no aid, Proxmire is reportedly going to support a renewal of the present seasonal loan package on a diminished scale. One source reports that this move might succeed in delaying passage of any aid package — thereby pushing the city closer to bankruptcy, It is widely acknowledged that if, after the current loan program expires, nothing is done by June 30, the city could stumble along until mid-July, and then go into bankruptcy.

More importantly, knowledgeable political sources regard all proposed "loan programs" as ultimately unworkable since they are hooked into an austerity program that will further destroy the city's tax and credit base. At best bankruptcy would be delayed. "What kind of recovery plan leaves the city looking like ground zero at Hiroshima," a corporate leader in the midwest stated.

Unfortunately, most corporate business and labor leaders are falling for the "let's cure New York by austerity" line — as they are falling for Miller's anti-inflation programs.

Walking Into A Trap

While Proxmire, Rohatyn, et al. conducted their farce in Washington, the police and fire unions started walking into Rohatyn's bankruptcy trap. Both unions immediately announced that they would not sign the "pattern wage" agreement. They then proceeded in effect to say "screw everybody else, give us our wages." Both unions are thus isolated, as Koch prepares to push them out on strike.

Both unions refused the purchase of MAC bonds to help the city get through the month of June; the other unions anted up their $350 million the day after the contract was announced.

A spokesman for the Mayor's office announced that "Ed Koch is fully prepared to do what is necessary to make sure that the fire and police unions get not one cent more than anyone else. . . ." They are demanding roughly 30 percent in wage increases.

"The cops may finally pull the plug on the whole thing," said one banking source. "It would sure be a convenient excuse. . . ."

. . . Even If It Takes Tanks And National Guard In The Streets . . .

An aide to a prominent Midwest Senator had the following to say about New York:

. . . The key thing about the New York situation is austerity. Any way you cut it, the city is going to have to cut almost a billion dollars more than it says from its budget over the next two years or it won't be balanced. It's unpleasant, but that money is going to have to come from the hides of workers and city residents through service cuts . . . it's going to be painful, but they should have realized this years ago when they were living high off the hog . . .

You are going to have to cut from everything, but the ghetto and poor are going to be hurt worse . . . they depend more on city services. There will no doubt be some riots. They will have to be crushed. There is no way around it, even if it takes tanks and national guard in the street, then so be it. New York is going to have to be made to live within its means. . . .

N.Y.C. Default Could Bring Down U.S.

In light of current proposals for handling New York City's financial crisis, a Twentieth Century Fund expert on New York City portrayed that city's predicament as a perpetual crisis situation.

Q: Do you see the banks as having to absorb much more city paper or MAC bonds?

A: Definitely, although from the banks' standpoint it's not sensible to absorb more, but they'll just have to take in at least a couple of billion more.

Q: But that will put their holding of city paper in excess of their total equity capital, won't it, and make any default hit them very hard?

A: I know , but they have no choice.

Q: What about layoffs?

A: There will be layoffs, but they will be moderate — in the order of 20,000 or so (10 percent of the workforce — ed.)

The budget deficit may not be as much as you say, and the hope is to get larger federal monies and state funds, and perhaps greater local revenues. It is doubtful whether this will happen, but Koch will try to avoid layoffs.

Q: Given that the situation for some time will probably remain the same, with the city crisis capable of erupting any time and causing default; first, do you see bankruptcy as an increasing possibility, and secondly, do you see a bankruptcy as possibly being the straw that breaks the Administration's back and results in Carter's Waterloo, or Watergate?

A: You're right about default, that could indeed happen despite everyone's best intention, but I'm not sure it would bring down Carter. It would have tremendous international ramifications as to the confidence they would have in America and the White House, and it could indeed make Carter look very bad, and jeopardize the 1980 election, or even nomination, for him. It is possible that the Federal government will go out of control if New York goes down the tubes.

Massive Layoffs A Must

A source at the Russell Sage Foundation foresees massive layoffs and increasing debt absorption by New York banks:

Q: One person I recently spoke with indicated that he thought there will be only moderate layoffs, in the order of 20,000. What do you think?
A: There will have to be very heavy layoffs, I don't know exactly who or from what areas, but it has to be large. The budget is going to be completely out of whack with the wage settlements. Koch had projected that the budget would be $1 billion in deficit by 1981, and that assumed no wage increases; more federal, state, and local revenues; and an expanding economy. We are sure to have a recession this year or next, federal and state money will not be forthcoming, and corporations are liable to start running from the city. In addition, the current budget is probably going to be a billion or a billion and a half out of kilter just on these wage settlements, and Koch hasn't even figured the police and firemen — that'll bring the total wage settlement to $1.5 billion or so. The only way the city can get out of this is either by a debt forgiveness by creditors or a 25-year stretch-out — neither of which are going to happen.

Q: How do you think Koch will deal with the police and fire unions?
A: Almost for sure he'll take a strike. Once he gets things squared away with the feds, whatever it is, he doesn't have to settle right away with anyone else. There may be a lot of chaos, but he can — and has to, to keep things intact with the other unions — stand firm.

Q: Do you think the banks will have to absorb city and MAC paper?
A: They will absorb at least $2 billion, there's no way around this. Sure, it'll endanger their equity, but it has to be done, and they'll feel the heat. They can't let the city go down and they know it.

Is Schmidt Readying Gold Option For July Summit?

FOREIGN EXCHANGE

Chancellor Helmut Schmidt has now taken active charge of West German strategy for the July 6-7 economic conference of Western heads of state in Bonn. According to preliminarily confirmed reports in the daily *Frankfurter Allgemeine Zeitung* June 8, Schmidt has frozen out both central bank officials and finance ministry civil servants from monetary policymaking, and put together a private task force of trusted associates under his own guidance.

Both the *Frankfurter Allgemeine Zeitung* and other West German sources say that "reflation" is ruled out; a reserve role for the deutschmark to partially supplant the dollar is ruled out; and an expansion of West German-led joint-float currency "snake" is ruled out.

Schmidt's *positive* proposals remain to be specified. But two principal directions became clearer during the week of June 2-9. First, on trade: according to Economics Undersecretary Rohwedder, the Chancellor will press at the summit for the establishment of an international consultative forum for sustaining and expanding world trade, and urge that the Geneva talks on the General Trade and Tariff Agreement (GATT) must reach a prompt, growth-oriented conclusion.

Since Schmidt's multibillion-dollar 25-year trade and investment accord with the USSR gives the most concrete notion of what Schmidt means by "sustaining and expanding trade," this proposal seems to betoken a forward policy push beyond the complaints against European protectionist tendencies that have dominated West German statements. Rohwedder added in his June 2 speech that Schmidt had discussed the trade question with President Carter at the recent NATO meeting in Washington.

The second, still shadowy direction of positive initiative is currency policy. If Schmidt rules out the various London proposals for dollar demotion and the creation of anti-U.S. currency blocs, what does he suggest be done about dollar instability? It should be recalled that the Schmidt's talk with French President Valéry Giscard d'Estaing in April were reliably reported to include serious deliberation on the possibility of restoring some sort of gold backing for the dollar-reserve system. The *Frankfurter Allgemeine Zeitung's* June 8 report of the new Schmidt strategy explicitly refers to this option.

In the face of resistance to a restored role for gold from at least one group at the West German Bundesbank, the central bank, it was Schmidt who said at the time of his discussions with Giscard that his chief disappointment in the Nixon Administration was in its decision to sever gold from the dollar.

The gold question has resurfaced elsewhere. At a June 5 Conference Board gathering, former Federal Reserve foreign-exchange vice-president Charles Coombs, a veteran of the pre-August 1971 dollar blow-outs, proposed U.S. gold sales to the Swiss and West German central banks, a proposal originally made at the end of 1977 by Swiss central bank chief Fritz Leutwiler.

The "swaps" idea is regarded by both its advocates and opponents as a foot-in-the-door for remonetization of gold; it was rejected as such in so many words by Treasury Undersecretary C. Fred Bergsten at his June 5 press conference, when the West German press corps slyly baited him by raising the possibility.

Most significant is the recent public support for a gold-