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INTERNATIONAL CREDIT

'The IMF can't impose conditionalities'

Two senior U.S. policymakers gave their views this week on the dim prospects for the International Monetary Fund and various possibilities for the European Monetary Fund.

From an EIR interview with a ranking advisor to the U.S. Treasury, Sept. 13:

Q: *French Bank Paribas has spoken of possibly extending a gold-backed ECU as a currency linking up Europe with the Middle East and the northern tier of Africa by financing and becoming the settlement currency for trade.*
A: That can't happen. Listen, I've talked to top European officials who at a top-level monetary meeting recently told the French that they will not tolerate the French using a gold-backed ECU [European Currency Unit] to replace the dollar and Special Drawing Rights. Look, the EMS is progressing too rapidly to step 2 or step 3 and it shouldn't be going beyond step 1.

Not only that, the finance ministers of the Group of 77 [the Third World members of the IMF—ed] have a special proposal that calls for a new special facility of easy-term credit on easy conditionality terms. This fund will totally lessen the IMF's ability to impose conditionalities. How can the IMF approve this fund? Very few people are borrowing from the IMF tranches and almost no one has borrowed from the special 10 billion dollar Witteveen Fund. So we can't issue a new fund.

Q: *What will you do?*
A: I would recommend that the IMF put together a study group that recommends that consideration of the new fund be put off until the spring, and not start until the other funds have been used.

Q: *What will the Third World do if that proposal is made?*
A: They'll do a lot of militant speechifying.

Q: *What will be the agenda of the Oct. 2 IMF meeting?*
A: Well, I think there will be first, the world economic outlook; second, demand for this new Third World special facility; third, the U.S. Congress' unwillingness to finance the World Bank without heavy strings at-

DOMESTIC CREDIT

Will history repeat itself? Fed plans another depression

It was the fall of 1929. For months the London *Economist* and the *New York Times* had been "predicting" a stock market panic. Benjamin Strong, president of the New York Fed, moved precipitously in coordination with Bank of England Governor Montague Norman to jack up U.S. interest rates. With this abrupt reversal of the previous policy of easy money and low margin requirements, which had been fueling the rampant stock market speculation, the crash was on.

As the nation's financial newspapers commemorate the fiftieth anniversary of the crash of '29, there is never a hint that the crash was deliberately provoked, not least to torpedo expanded trade with the young Soviet republic (Henry Ford's idea) and industrialization of the colonial world. Nor is the certainty mentioned that revival of these policies would have ended the ensuing Great Depression.

The successors of Strong and Norman are again deliberately attempting to provoke a world depression beginning in the U.S. For the last week, the *New York Times* has been running scare stories about the building level of business inventories in the U.S., urging corporations to cut production and lay off workers now, supposedly to avoid a worse economic crisis later. We quote from the *Times* of Sept. 10: "The concern is that, as in 1974, companies will wait too long before reducing their orders. Then, when they finally do turn off the tap, the shock to the economy would be widespread as production lines were idled and workers were thrown into unemployment."

But despite the large 1.9 percent rise in overall business inventories in July and the probability that there was further involuntary accumulation in August, the carefully watched inventory-to-sales ratios are still low by 1974-75 standards. According to the Commerce Department, in July total business inventories stood at a seasonally adjusted 1.44 of a month's sales, up from 1.43 in June and 1.4 in May. The ratio of stocks to sales is higher at the manufacturing and re-

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tached, and fourth, the SDR substitution account.

Q: *What will be the fate of the SDR substitution account?*
A: Well, if the French block it at the upcoming G-5 meeting on Sept. 16, then there's no way it can be referred to the IMF Interim Committee.

A financial journalist provided the following Sept. 13 interview with Harold Van Cleveland, senior vice president of Citibank and an active Council on Foreign Relations members:

A: Now let's see, you're saying that the EMF would issue ECU bonds to foreign monetary authorities and then use the funds to issue ECU credits to third countries. Yes, that could work.

Q: *What do you think the U.S. can do about it?*
A: I wrote an article in *Foreign Affairs* which has just come out on the EMS. What I said there is that our problem of stagflation is caused by bad money management and that what we need to solve this is a global system like the EMS.

Q: *That's different from what Treasury is saying. They're very upset that the EMS could develop into a rival to the IMF. What they're proposing instead is the SDR substitution account and increasing the power of the IMF so it can intervene in countries' domestic economies.*
A: That's chimerical. The IMF can't intervene in industrialized countries, particularly when it's the U.S. which is the real source of the problem. It's possible you could put an enlarged EMS under the rubric of the IMF. But to make the IMF an independent center of authority—it just doesn't work. The substitution account is simply irrelevant, because it ignores the problem of our bad management.

Q: *Well, what are you proposing that we do about the dollar?*
A: Get the U.S. inflation rate down to 3 percent. This can only be done when the Fed and the administration give first priority over a period of several years to restrictive money growth.

Q: *But the Europeans want to expand by lending to the developing countries to finance their capital goods exports.*
A: There are limits to how much they can lend to these countries. The European economies are too large, it won't make enough of a difference...

Q: *How long do you think this period of tight money will have to last?*
A: Five years.

—Richard Freeman

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tail levels. However, when the 1974-75 recession "officially" got underway in the first quarter of 1974, the overall ratio was 1.57, and it peaked to 1.71 in the first quarter of 1975.

Government analysts are warning that any further drop off in retail sales at this time will lead to a dangerous backing up of inventories and a major liquidation of stocks by the nation's consumer-oriented businesses in short order. John Heimann, Comptroller of the Currency, has just set the stage for such a scenario by taking steps to pop the still-expanding consumer credit bubble. The former partner of Warburg Pincus disclosed in a speech Sept. 11 that he had written a letter to all nationally chartered banks, warning them against the overextension of consumer credit. The letter, which the *New York Times* obtained from Heimann and quoted as part of its campaign to start a depression, apparently focuses on the extension of revolving credit lines by the banks and the providing of multiple credit lines to individual borrowers through credit cards. Both practices are post-1975 innovations, which made possible the "consumer-based recovery" in the first place. The Heimann letter comes at a point when consumer credit expansion is already slowing. Earlier last week the Federal Reserve had reported that consumer credit grew by $2.44 billion in July, compared with $2.56 billion in June and $3.73 billion in May.

The big fear in the corporate sector is that Fed chairman Volcker is about to crack down on *credit availability*. During the month in which he has occupied the Fed chairmanship, Volcker has already succeeded in touching off a spiral in short-term interest rates. As of last week the yield on three-month Treasury bills was 155 basis points higher than the yield on thirty-year government bonds. This unusual reversal in the "yield curve" is the result of the Fed's continuing efforts to arrest money supply growth by yanking up the Federal funds rate, the trend-setting overnight interbank rate.

As we go to press, the record 13 percent prime rate established on Sept. 12 by Chase Manhattan Bank, Mr. Volcker's former employer, is catching on at banks across the nation. The pressure on the prime rate is coming from two sources: the escalating rise in the banks' cost of funds, and heavy demand for short-term financing from businesses. Over the last two months, short-term business loan demand has been growing at a 30 percent annual rate, as the cost of financing building inventories rises and corporate liquidity dries up. From all appearances, Volcker is intent on deliberately cutting off credit to U.S. business at the point when it needs it the most, and trying to make history repeat itself.

—Lydia Schulman