Business Briefs

Banking

"Equality of reserves

"Is it any wonder that a mounting number of banks are dropping out of the Federal Reserve System every year?" a regional banker commented in response to Fed Chairman Volcker's recent warning about the accelerting decline in Federal Reserve membership. "Our bank has had to pay on average 18 to 20 percent for Fed funds [overnight interbank loans] since October, on top of the financial burden of keeping noninterest-bearing reserves on deposit with the Fed. Frankly, the Fed has given U.S. regional banks every incentive to *get out* of the Fed system this year."

A record of 69 banks with a total of about $7 billion in deposits served notice they they were withdrawing from the Fed in the final quarter of 1979 and the beginning of this year, Fed Chairman Volcker noted in testimony before the Senate Banking Committee Feb. 4. "The loss of deposits in this short period exceeds that of any full year," Volcker said. "It is my judgement and that of many others that in the absence of legislative action, the stream of member banks withdrawing will reach flood proportions." In mid-1978 there were 5,000 to 6,000 Fed members.

The reasons for their flight are simply that the Federal Reserve's "tight money" policies have so increased the cost of doing business for banks that they are seeking to escape the Fed's reserve requirements.

Volcker and Treasury Secretary Miller, who testified before the Senate Banking Committee the next day, both favor a bill on Fed membership/reserve requirement that would for the first time in history force all despository institutins to hold reserves at the Fed. The sweetener on the bill, which was passed by the House last year, is that it would lower current reserve requirements, while making them mandatory throughout the banking system: it would establish "equality" of reserve requirements.

Miller testified that he does not favor another version of the bill being considered by the Senate committee that would encourage Fed membership by making the Fed pay minimum interest on reserves deposited with them in addition to lowering reserve requirements across the board. Both officials noted that the other Senate version would cost the Treasury $579 million yearly in lost revenues, while the bill they favor would cost the Treasury about $74 million in yearly revenue losses. The losses would stem from the reduction in the amount of interest-free reserves available to the Treasury for investment in interest-bearing securities.

International Credit

Do resolutions have teeth?

At the European Community's Council of Ministers meeting in Brussels on Feb. 5, the foreign ministers all agreed that their member countries would stop granting the U.S.S.R. favored credit terms in protest over Soviet actions in Afghanistan. This presumably would hit the high volume of loans made by the state agencies of France, West Germany and Italy through their equivalent of the U.S. Export-Import Bank. Currently favored credit terms to the U.S.S.R. are defined as any loans made at below a 7.5 rate of interest.

However, on a closer examination, many analysts have found that the resolution is not as stringent as it may appear. First, an interest rate minimum charge of 7.5 percent, under today's inflationary and high interest rate conditions is hardly a penalty. U.S. interest rates are 15 percent and above. It is assumed the Soviets are already being charged more than 7.5 percent in trade credits extended by the West. Secondly, and of more substance, is the fact that the governments of France, West Germany and Italy are still continuing strong trade with the Soviet Union. Three weeks ago, Bertold Beitz of Krupp Gmbh concluded an $11.6 billion oil and gas exploration and transmission deal in Moscow.

Moreover, the continental Europeans, as opposed to the British and the U.S., have refused to cut off grain shipments and high-technology goods. The Feb. 6 *Financial Times* editorialized on the action by the EC foreign ministers in removing favored credit terms with the Soviets: "It is beginning to look as if the alliance is able to swing in harmony, if not in unison." But, adds the *Financial Times*, "the loose ends have to be tightened," including high-technology goods and agricultural sanctions which the Europeans have refused to take.

Gold

Monetary conference treats role of EMS, gold

A conference sponsored by the New York-based Securities Goup and its leader Eugene Birnbaum, that called together several leading monetary experts to in effect discuss the "failure of the European Monetary System" Feb. 3, ended up instead debating what role gold will play in the world monetary system.

Rinaldo Ossola, former head of the Bank of Italy and soon to be chairman of Banco di Napoli, was the featured speaker. Ossola stated, according to the Feb. 5 *Journal of Commerce*, that "the system's margins are too narrow, the highly complex divergence indicator isn't of any value, the credit system does not permit the evolution of the European currency unit, the ECU, and Britain is not participating." Ossola also called for a link between the dollar and EMS.

The one feature of the EMS that he claimed to like was the fact that the EMS was capable of imposing "some form of regional surveillance, supplementing the work of the International Monetary Fund."

Yet, very soon the conference shifted from technical and other disagreements with the EMS to what role gold will play in the emerging reorganization of the world monetary system. Most of the participants were very aware of the re-

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ports, leaked from the Elysee Palace residence of the French President last week, that Giscard plans to unveil phase II of the EMS, based on a total monetization of gold in Venice this spring. Such antigold protagonists as Robert Mundell of Columbia University say that the role for gold is unthinkable and would make the world hostage to South Africa and the Soviet Union.

But most others at the conference recognized that Mundell's response was a very ineffective counter to Giscard's gold option. Ossola proposed that gold be used in the EMS but that it could also be used as the back-up for the International Monetary Fund's funny-money Special Drawing Rights (SDR) substitution account. Gold will never be the central standard for the world's monetary system, Ossola insisted. Ossola's proposed use of gold-backing for the SDR issuance sounded remarkably like the proposal that came that same day from the IMF.

Janos Fekete, governor of the Bank of Hungary, and a supporter of the City of London proposal to divide the world into competing currency and trade zones, also urged the conference to create an SDR monetary-type asset that would have implicit backing of gold. By this is meant that gold will determine some ratio of SDR use, but not be convertible into the world's principal currency, the dollar.

Many of the participants at the Securities Group conference, which included Federal Reserve Board member Henry Wallich took a far less anti-EMS view than Ossola, realizing that the EMS is a fact of life and that it might be more "profitable" to work inside the EMS than to criticize from the sidelines.

Trade

Protectionist War Looms

European industrial sources are saying that they fear a protectionist war is erupting between the U.S. and Europe that will have a disastrous effect on both parties and further widen the gap between the U.S. and continental Europe.

In Brussels Feb. 6 at the EEC Council of Ministers Meeting, the British government claimed that the U.S. is flooding cheap man-made fibers into Great Britain, ruining the British market. The British spokesman then went on to say that Britain will most likely invoke Article 19 of the General Agreement on Tariffs and Trade against the United States. According to the Feb. 6 *Financial Times*, "In spite of a warning by Herr Wilhelm Haf Terkamp, the EEC External Trade Commissioner, that such a move could unleash a damaging trade war between the EEC and the U.S., there were strong indications here that Mr. John Hott, the British Trade Secretary, will inform the House of Commons that special trade measures are to be adopted." This could amount to U.K. imposed quotas that will reduce the volume of U.S. fiber goods by 18 to 20 percent.

On the other hand, on Feb. 4, Lewis Foy, chairman of the Bethlehem Steel Corporation and head of the American Iron and Steel Institute, was handing reporters in Washington D.C. a 90-page report entitled, "Steel at the Crossroads" which demands tougher action by the U.S. government against what the steel industry charges is dumping.

The report proposes changes in the steel trigger price mechanism administered by the U.S. government which is supposed to stop dumping. Specifically, the report asks that the government raise the "minimum price" below which it is illegal for the Europeans to sell steel in the U.S. It also asks that the various specialty steels be included under the trigger mechanism umbrella.

Yet, any economists with a sharp political eye recognize more than simply a trade war brewing, as disastrous as that would be in itself under depression conditions. Of equal significance is the threat of what a trade war may do to shift the world balance of power.

In a lead editorial, "Steel's Washington Hostage," the Feb. 5 *Journal of Commerce* warns that this trade war posture on steel by the U.S. against the Europeans could be very dangerous.

Briefly

● **CONTENDERS** for the job of Undersecretary of Treasury, the post being vacated by Anthony Solomon, have all been panned by leading pundits in Washington. Three of those contenders, Richard Copper Under-Secretary of State for Economic Affairs; Robert Hormat, a state Department official; C. Fred Bergston, Assistant Secretary of Treasury for International Affairs have all been considered "top soft." "The Europeans will push them around like crazy," said one Washington insider, referring to growing differences between Washington and continental European nations over monetary policy and the dollar crisis.

● **REP. BENJAMIN ROSENTHAL** (D-N.Y.), a ranking member of the House Operations Committee issued a press release Feb. 3 announcing his objection to the Federal Reserve's approval of the Hong Kong and Shanghai Bank take-over of the Marine Midland Bank, the U.S.'s thirteenth largest.
Rosenthal states that HongShang, as both a bank and trading company, violates the terms of U.S. banking law which only permits banks to acquire other banks. The Federal Reserve ruled Rosenthal's accurate objection as insufficient to stop the HongShang takeover.

● **DONALD RUMSFELD,** president of O.D. Searle Drug Company is reported planning to leave that company soon and has already delegated a successor. Rumsfeld, who was President Ford's Secretary of Defense is returning to political life.