Click here for Full Issue of EIR Volume 7, Number 9, March 4, 1980

Carter's deflationary economics:

A new fascist world order

by David Goldman

What is wrongly deemphasized in virtually all domestic coverage of the inflationary "explosion" in the United States, using the term of a senior administration official, are the tremendous international repercussions of the Federal Reserve's actions of the past week. These repercussions include:

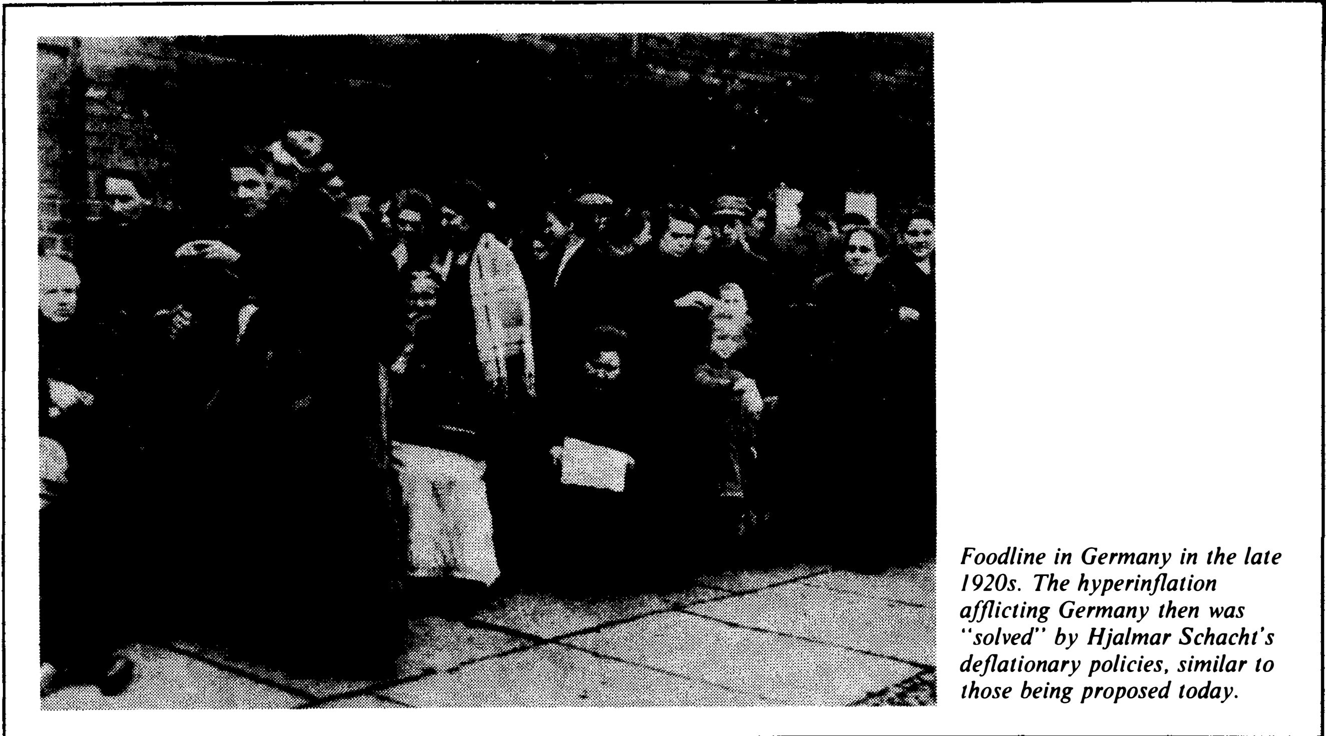
- The extreme additional burden the new level of interest rates places on Third World debtors;
- The near impossibility of maintaining a stable dollar under present conditions; and
- The precarious position of $150 billion in official dollar balances held by Western Europe and Japan.

Although Volcker, answering questions at his Feb. 20 testimony before the House Banking and Currency Committee, promised "horrendous" rates of inerests if necessary, even a 16.5 or 17 percent prime rate does not measure up against 19 percent per annum wholesale price inflation. "Real" interest rates, sufficient to persuade corporations and households to stop going into debt to acquire appreciating goods with depreciating dollars, mean rates in excess of 20 percent—Brazilian-style monetary policy. Under these circumstances, it is absurd to discuss slow monetary restraint as a means of cooling inflation, as Volcker did in his Feb. 20 testimony.

The Federal Reserve's intention, on the contrary, is to "break the back" of the American economy, as one senior Treasury source put it, producing sufficient chaos and retrenchment to permit the elimination of large portions of the civilian budget, the imposition of credit, wage, and price controls, a gasoline tax, and similar measures. The combination of these measures would substantially reduce American living standards and restrict industrial investment to whatever can be financed out of military or energy-financing porkbarrels. Strictly speaking, the United States would become a Schachtian economy on the precise model of Germany, 1936.

Volcker would then have the same foreign-side problem that Nazi Fin-

© 1980 EIR News Service Inc. All Rights Reserved. Reproduction in whole or in part without permission strictly prohibited.



Foodline in Germany in the late 1920s. The hyperinflation afflicting Germany then was "solved" by Hjalmar Schacht's deflationary policies, similar to those being proposed today.

ance Minister Hjalmar Schacht had with the additional problem of maintaining a domestic credit system grounded in the dollar's reserve-currency role. Henry Kaufman of Salomon Brothers, who proposed exchange controls on the dollar in a Feb. 21 speech, followed this logic to its obvious conclusion.

So, Volcker's measures must be seen in the context of a global political strategy to break all international resistance to Schachtian economics. The key point is the power-consolidation of Sir Keith Joseph and Chancellor of the Exchequer Sir Geoffrey Howe, the arch-hawks on both austerity and strategic confrontation with the Soviet Union. The decision has been made to put the American economy under military wraps, and permit the worst consequences to go through both at home and, equally critically, in the Eurodollar market.

There is virtual panic among sections of the international banking community over the consequences of this deflation, which, among other things, would make the refinancing of $40 billion in Third World interest payments alone during 1980 impossible. In a speech Feb. 27, Chase Manhattan Bank chairman David Rockefeller warned that default of leading Third World debtors was a real possibility. He pleaded for an increase in resources to the International Monetary Fund. World Bank President Robert McNamara, the leading light of the Brandt Commission, is pleading for an extraordinary World Bank role in balance of payments lending, to prevent such defaults from taking place.

Former British Prime Minister Edward Heath summarized this viewpoint in a long *London Times* article Feb. 26, begging for a rise in World Bank and International Monetary Fund resources, warning: "It is all too easy to see the difficulties. The alternative is for the world to go sliding deeper and deeper into recession, affecting both North and South, and for the South to become so frustrated by its impotence that it puts pressure on OPEC to use oil again as a political weapon, so denying the North the energy it needs."

However, Heath was the factional loser in the played-out British internal fight. Opposite his article was the triumphant proclamation in the *Times* editorial column of the success of the deflation policy.

The other problem that Sir Keith and his friends have shut out of consideration is the unwillingness of Western Europe to accept a collapse of the world economy. France has already proposed the circulation of gold as a central bank reserve medium, and won agreement for this policy among central bankers at the February meeting of the Bank for International Settlements in Basle. France and West Germany, who have given no ground to either the monetary or strategic policy of the Margaret Thatcher government, have the option to activate the advanced features of the European Monetary System at virtually any moment.

Where the American economy itself is concerned, the Federal Reserve and the administration ultimately expect the centralization of world liquidity through the

International Monetary Fund will provide *both* the source of funds for and the means of disciplining the federal budget. Since the proposed IMF Substitution Account, which the Group of 30 expects to be approved this year, will invest some tens of billions of dollars in American Treasury securities, its leverage over American economic policy will be enormous. At the same time, by providing the equivalent of an exchange rate guarantee for dollar holders, the Substitution Account will solve the basic dilemma of the American "Schachtians": how to run an essentially hyperinflationary monetary policy to finance a defense and energy-autarky program in the United States, and maintain the integrity of a federal debt which depends heavily on the willingness of foreigners to hold dollars as a matter of Atlantic Alliance loyalty.

London Times demands worldwide deflation

In a Feb. 26 editorial that bears the unmistakeable thumbprint of editor-in-chief William Rees-Mogg, the *London Times* proposed a global deflation whose consequences are almost gaugeless. The editorial, entitled, "The Road to Hyper-Inflation is Paved with Good Intentions," celebrates the factional victory of the hardline "Friedmanites" in the British Tory government, under the leadership of Industry Minister Sir Keith Joseph. The uncharacteristic public fight inside the British cabinet over the past two weeks, between surrogates for former Prime Minister Edward Heath and Sir Keith Joseph was represented as a difference over monetary policy and handling of the British Steel strike. In reality, the dispute was a sorting-out at the top level of policy-making in the Anglo-American leadership. The decision for deflation has been made on both sides of the Atlantic.

Rees-Mogg's editorial, penned a few days before his month-long tour of the United States, should be read as a ukase in force on both sides of the Atlantic, emphatically at the U.S. Federal Reserve. The sudden spate of editorial support for the identical policy, including the *New York Times'* sudden conversion Feb. 28 to support for a balanced budget, indicates how fast the American side of the Anglo-American machine came on board.

Rees-Mogg asks opponents of deflation:

> Do they want a higher public sector borrowing requirement? If so, are they going to finance it by higher interest rates or by higher inflation? Do they want public expenditures to be maintained or cut? If cut, where else would they cut it? If maintained, how will they pay for it? Do they want higher taxes? On income, or expenditure? There are no soft options in public expenditure; either the Government cut expenditure, or they accept a higher borrowing requirement or higher taxes, or they will cause even higher inflation. Some increases in taxation are already inevitable. ...
>
> The (British) Government is committed to a long and painful attempt to reduce inflation by fiscal and monetary means. They have been in power for nine months, far too short a time for success. Can it be right to relax the attempt and return to more inflationary policies, in order to ease the pain, when inflation is still moving toward 20 percent? Faster money growth would not reduce unemployment; its only enduring result is higher inflation.

The fact that American and British interest rates and inflation rates are now within ½ percent of each other should eliminate doubt that Rees-Mogg is only talking about the United Kingdom. Additionally, the appearance of American monetarist guru Milton Friedman at 10 Downing Street, and the remake of Friedman's American television broadcast series in Britain, raises another question. Friedman and his spokesman, former Treasury Secretary William E. Simon, have emerged as the leadership of the Reagan campaign. Simon and Friedman, through the American Heritage Foundation and other channels, are plugged directly into Sir Keith Joseph's operation in England. Can the Reagan campaign be used to leverage the United States into the type of deflation Rees-Mogg is proposing?

Although Fed Chairman Paul Volcker has not yet pulled the switch in the way Rees-Mogg proposes, and has opposed credit controls in recent congressional testimony, there is little doubt that he will move in that direction. Under 1969 legislation, the White House and the Fed can act unilaterally in this respect.

The budgetary side of the deflation operation is already underway. The Office of Management and Budget has already been instructed to resubmit administration budget proposals with a deadline of two weeks from now, eliminating virtually all inflation adjustments in federal income support programs. Among other things, that guarantees the slow starvation of some several hundred thousand senior citizens.

Volcker has artfully held back, warning against "impetuous action," while the bond market has disintegrated, and a crescendo in the financial press—amplifying Rees-Mogg's proposal—has created the conditions under which even congressional "liberals" have agreed to chop up the budget, and accept total monetary stringency by the Federal Reserve.