of food price increase, the resurgence of food prices threatens to bring the economy right back up to the inflation levels that caused near financial panic.

Most threatening, however, is the foreign side of the securities markets. It has been clear for some months that the rest of the industrial world viewed the electoral choice of Carter, Reagan and Anderson as the worst disaster that had befallen the Atlantic Alliance in the decade.

There is no confidence whatsoever in either the Carter or Reagan economic strategies, for one overriding reason: both approaches are founded on a Malthusian attitude toward the developing sector. Europe believes, and its leaders have stated publicly at every available pretext, that the industrialization of the developing sector is not merely the key to the industrial world's future economic growth, but a precondition for world security. Combined with European judgment of the quality of American economic management, justified foreign repugnance toward the American government's Malthusianism has brought confidence in the United States to a postwar low.

Fed to crunch again?

Various European institutions (see Foreign Exchange) are poised to act on the conviction that the United States headed towards the sinkhole, liquidating large volumes of fixed-income dollar securities. This is not merely a short-side play on the market, but a decision to reduce exposure for the indefinite future. The results for the dollar and American interests rates are potentially disastrous.

The probable response of the Federal Reserve to all this will be to further tighten the monetary situation, partly to draw short-term funds back into the United States, partly to further reduce American consumption. This will only worsen the vicious circle that brought us here in the first place.

Little noticed in the American press, but splashed over the front page of the London *Financial Times* Aug. 11, was a report issued by Sen. William Proxmire's Senate Banking Committee. The Proxmire report 1) commended Volcker for his policy actions thus far, and 2) demanded stricter monetary targets to be set for the next several years. This is a page from the book of Reagan campaign guru Milton Friedman, from the pen of one of the most liberal Democratic senators. With this political encouragement there is not much room for Volcker to choose courses alternate to the one he apparently prefers.

With these pitfalls in view, we consider our econometric forecast a *best-case scenario*, because credit market disruptions could make matters a great deal worse very quickly.

Who's behind the world oil glut?

by Judith Wyer

Following the December 1979 OPEC cartel price-setting meeting, Saudi Arabian Oil Minister Ahmed Zaki Yamani vowed that his country would reverse the tide of anarchic oil price increases by flooding the world markets with Saudi crude and outstripping demand. Eight months later, the Saudis have succeeded in this objective.

"There's an unbelievable oversupply of oil out there," observed a Wall Street oil analyst, "and yet the Saudis just keep pumping their 9.5 million barrels a day of crude. . . . The basements of the corporate headquarters of the major oil companies must be full of crude now, I don't know where else they could put the stuff."

Saudi Arabia's record-high production level, coupled with a marked decline in world consumption, has forced a number of OPEC price hawks, most notably Iran, to begin to shave their prices. In the industrialized countries refiners have imposed cuts in the market price of petroleum products, including gasoline during the summer months when gasoline is normally in peak demand.

Riyadh's goal is to force the pricing militants in OPEC to reunify the OPEC price at the upcoming heads of state OPEC summit in Baghdad in November. This will require a number of OPEC producers to lower the price tag for their crude, which goes as high as $37 a barrel, down to the Saudi benchmark price, now at $28 a barrel.

Riyadh hopes to then force the cartel to accept a plan worked out by the Long Range Planning Committee headed by Yamani to stabilize world oil prices by imposing small quarterly oil price adjustments pegged to the rate of world inflation.

Last week, Saudi Arabian Foreign Minister Saud al Faisal gave a press statement affirming that Saudi Arabia would continue its present oil producing and price policy through 1980. A well-informed Mideast observer remarked that the Saudis are "regaining the upper hand in OPEC and they are going to play very nasty to renew pricing discipline."

Saudi Arabia is not acting independently in this effort but has the support of the nations of Western

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Europe which, along with Riyadh, is fearful that continued price hikes will put such strain on the poorest developing nations that default on their debts could blow out the monetary system.

The European angle

The building Euro-Arab cooperation being led by the governments of France and West Germany on the one hand, and Saudi Arabia and Iraq on the other, aims to consolidate Phase II of the European Monetary System. The purpose of the EMS is to provide new economic support for the developing nations without the backbreaking conditionalities that accompanied International Monetary Fund aid.

Recent developments indicate that even London, which has been opposed to the EMS, is now making a bid to jump on the Euro-Arab bandwagon. London intends to get in on the economic gains which the Euro-Arab axis is offering through the recycling of petrodollars and new development contracts.

One indication of this has come in the form of hints from Britain that oil prices must be subject to international discipline. A Lloyds Bank report published in the July 20 issue of the London *Telegraph* called for world oil prices to drop to the level of Saudi Arabia. About that time certain North Sea oil transactions began to register a drop in value. The Aug. 12 *Financial Times* reports that the North Sea producers may soon lower contract prices. One key indication is the slashing of North Sea crude prices on the spot market to as much as $3 below the official $36.25 price. It is reported that a number of refiners that take North Sea crude are arguing that the British National Oil Company should be the first Western company to trim contract prices.

Rotterdam spot market 'in the red'

Unlike this time last year when the speculative oil spot market was booming to prices as high as $50 a barrel and setting the pace for OPEC prices, the spot market prices now are below long-term contract level. North African crude, the most expensive in OPEC, has gone for as much as $4 below contract level on the European spot market, prompting both Algeria and Libya, traditional pricing hardliners, to lop off expensive premiums on contracted oil. Saudi Arabian light crude, one of the highest-demand crudes in the world. is fetching $32 a barrel, a marked drop from spot values even two months ago.

A Wall Street oil analyst noted that for the first time in a long time, the Rotterdam spot market is "in the red." The Aug. 13 *New York Times* reports that Shell Oil Company is now subsidizing some of its distributors that have been negatively affected by the sagging spot prices.

Across Europe the price of gasoline is also dropping. Recently, the Netherlands, whose government controls gas prices cut 20 cents a gallon off retail gas prices. In West Germany, the major oil companies have reduced gas prices by 10 cents a gallon.

The U.S. is presently experiencing the worst decline in uncontrolled petroleum prices since the mid-1960s. This is not only a reflection of the worldwide glut, but also a record postwar decline in consumption, the product of the economic austerity programs of the Carter administration. Gasoline consumption is down a full 8 percent over the first six months of 1979. A number of U.S. producers are cutting prices. Standard of Ohio reduced 250,000 barrels a day of North Slope crude by a full $4 a barrel last month.

An executive with Morgan Guaranty has begun to campaign for a policy of international discipline with respect to oil pricing policy, and has called for no more than a 3 percent price hike per year for fear that anything more extreme will bankrupt the developing nations and bring down the monetary system. Morgan Guaranty has until now been a staunch advocate of high oil prices to make exotic alternative energy sources, such as gasohol and synfuel "economic." The Lloyds Bank report similarly chastised those pushing high prices as endeavoring to make synfuels affordable.

Saudi Arabia's record-high production level is designed to curb the price hawks and keep the world credit markets from a blowout. Even North Sea prices may come down. Another factor is the Carter administration's overkill against oil demand.

Perhaps these sentiments reflect a turn of thinking in Anglo-American financial circles who now see that exorbitant fuel costs plus backbreaking austerity could undermine the Bretton Woods system. It is these London centered financiers that are now flirting with the EMS.

Recent public statements from British Foreign Minister Lord Carrington and Lord Kalder, both speaking in Latin America, on the need to the loosen IMF conditionalities and find new ways of recycling petrodollars would indicate they have no other alternative.