

A hard landing onto a gold monetary base?

by Laurent Murawiec, European Economics Editor

That the U.S. and international capital markets face a crisis in the weeks and months ahead has virtually ceased to be disputed. What were warnings a few weeks ago have now turned into a near debacle, whether one looks at the nosedive made by the Dow Jones index, which stands close to 200 points under its high of the early months of the year, or the beatings repeatedly taken by the bond markets.

Internationally, the anticipated debt crises are bursting out right on schedule; Romania joins Poland among the ranks of the financially ailing East bloc nations; Costa Rica declares a debt moratorium; Bolivia sends telexes informing its creditor banks that it will not honor its Oct. 31 commitments. Additionally, while the Reagan administration is bogged down in sorting out the fiasco of the budget deficit, the Federal Reserve and Paul Volcker are announcing further tightening of the monetary policy, with the stated intent of sending cities and states, as well as corporate borrowers, out of the market and into bankruptcy.

The fact that the Treasury will have to float an inordinately large \$33 billion in debt in the fourth quarter of this year (while \$18 billion in corporate bonds is trying to appear on the market at the first signal) will further erode whatever remained of what Europeans called "The Reagan Effect" before and after the Jan. 20 inauguration, the state of euphoric "confidence" that continued through the passage of the tax bill.

The Reagan administration is utterly unprepared for the kind of emergency it will shortly face. The timid protest against the Fed's astronomic interest rates which President Reagan made Aug. 28 during a rare instance

in which he was not followed by doctrinal bodyguards, was quickly supplanted by an avalanche of statements from the Treasury and other members of the executive: "The Fed is absolutely correct in tightening and tightening further. We and they are on the same track with the same objectives and the same methods," a very senior Treasury official told *EIR*.

What makes this administration so singularly unprepared to deal with the imminent danger of a market crisis is the magical belief expressed by both its "supply-side" and "Friedman monetarist" components that the continuously high interest rates are only the result of "bad financial circumstances based on the fact that the markets have not convinced themselves that the Fed will stick to its guns." The Treasury source explained, "The markets still think that we will pressure Volcker—which we will not. If only Volcker repeats that he will stay firm often enough, the markets will understand." As the deepening problems on the markets compound the bankruptcies prepared by Volcker's interest-rate policy—the Fed candidly asserts that it is doing contingency planning for large-scale bankruptcies in housing construction, the airlines, and the S&Ls—the aura of confidence that has been painted around the President's head will vanish overnight—and with it, any stability on the markets.

Old sharks patiently wait

The doctrinaires that surround Ronald Reagan may be shell-shocked by the outbreak of the crisis, but some older hands that surround him, at a certain distance from the mess being created, are not so naive. The "old

boys" from the Nixon and Ford times—former Fed Governor Arthur Burns, former Treasury Secretary George Shultz, former head of the Council of Economic Advisers Alan Greenspan, whom high-level sources at the International Monetary Fund describe as feeding the President with the conceptions he then applies to immediate decision-taking—are not surprised.

In fact, not only did they predict the crisis six months ago, *they started it*. It was this group which warned the President in January that neither the Bank for International Settlements of Basel, Switzerland, nor the network of the leading central banks clustered around it, the Bank of England, the Swiss and Dutch national banks, and so forth, would tolerate Reagan action against Paul Volcker and his interest-rate policy.

When Reagan capitulated to the blackmail of a dollar crisis, Burns et al. started to openly predict that the "supply-side" panacea would be dropped after a short period—time for the tax bill to be passed, for massive, deflationary budget cuts to be implemented, and time for the administration to have cut itself off from its disgruntled constituencies.

What these self-styled "cooler heads" contemptuously explain about the administration can be summed up in comments received by *EIR* at the IMF. "This boy Stockman is profoundly insane. . . . The NSC does not know anything about economics. . . . Those people just do not know anything."

What they propose is deep, deep cuts in the budget—Chase Econometrics is now predicting that the deficit will reach \$100 billion not only in fiscal year 1981, but *every year* of this administration—and, to start with, deep cuts in the defense budget. They propose to let "just a few banks including big ones go under in a carefully limited banking crisis—like Herstatt [the German bank that collapsed in 1974], which did not do any harm, to the contrary, since it's restored discipline to the banking world," as a senior U.S. source at the IMF told *EIR*. They predict—and in fact *propose*—"a rapid unraveling of the economy" and "a situation where people will be out of a job for a long period," while Paul Volcker, in his own testimony, wants wages to be slashed.

Last, they propose to let the Third World "eat cake." "The whole question at [the North-South summit in] Cancún is money—and we're not going to give any to the Third World, that's it. A one-way transfer of resources to the Third World is a non-start as far as we are concerned," a diplomat close to Caspar Weinberger and the old boys stated. It is quite likely as a result that a large number of Third World nations will face, as soon as the third and fourth quarters of this year, the immediate threat of open default. "When the bankruptcies come, and U.S. and European banks are in dire straits because they are overextended, then the central

banks will be able to step in and take the whole matter in their own hands, failed borrowers and overextended creditors alike," the diplomat said.

A guarantee of last resort: gold

As this journal has been pointing out for the last five years, the outbreak of a generalized monetary and financial crisis demands that gold be used in some form to restabilize the system. That idea has now gained fresh credence, as the crisis approaches.

An extraordinary barrage of press articles has been paving the way for something to happen on that account. Editorials in the *Wall Street Journal*, radio debates, pieces in *Business Week*, the *Washington Post*, the *New York Times* have recently accustomed the general public to this idea that something ought to be done involving gold to solve the intractable budget problem and that of inflation.

A similar exercise is being conducted at higher levels, for the benefit of the credulous members of the administration and Congress, under the name of the President's Special Commission on Gold.

An apt definition of both advertisement campaigns was recently given by supply-side gold advocate Jude Wanniski, who explained that it was principally "filling in the stadium before the action begins."

Discussions such as that which the *Journal of Commerce* indulged in—should the gold cover of the money supply be set at 60 percent or 100 percent? should dollars be gold convertible, or only inside the United States and not to foreign dollar holders?—are in fact immaterial. The real debate is whether gold will be used as a method for smoothing out the dangers inherent in a deflationary collapse of the economy, and managing the crisis to that very purpose, or as a means of generating credit for productive investment?

It is extremely significant in this context that one spokesman for the old boys, Alan Greenspan, should have joined the ranks of the advocates of a return of the dollar to gold, in an Aug. 31 editorial-page article in the *Wall Street Journal*. Contrary to the doctrinaire propaganda about a 19th-century gold standard that has appeared in great quantities these last weeks, Greenspan's proposal to gradually reintroduce monetary gold in the dollar system has technical competence and legitimacy: Greenspan proposed to issue gold-backed and gold-pegged Treasury debt, with a 2 percent interest rate, and both interest and principal payable optionally in gold.

Greenspan calculates that compared to presently floated Treasury debt, which carries interest of close to 17 percent, his gold solution would entail an annual savings of \$1.5 billion for \$10 billion of debt, which would further help reduce budget deficits as well as inflation.

The snag in the Greenspan proposal is that it is entirely geared to manage what is accepted and prepared as a vicious deflation of the economy: he specifies that an appropriate "environment" should be constructed to support the gold option, namely, a tight monetary policy and fiscal policy. Greenspan is offering nothing else than the worst aspects of the current situation, save more of the same austerity, which would be fatal to further stretches of U.S. industry, farms, and financial institutions, as well as to world trade and the financing of the oil- and recession-induced Third World deficits.

What is being proposed is a fine-tuning of crisis management with the aid of gold. Greenspan and his sponsors are not interested in generating more and cheaper credit for the productive sectors of the economy. Moreover, this version of a gold standard, coupled with austerity, would prove totally incapable of wiping out the large budget deficits incurred at present; continuing deficits would simply deliver the gold stocks of the United States to holders of U.S. Treasury debt.

Expectations of crisis are so widespread that very large-scale movements have been observed on and off the international gold markets. As *EIR*'s gold column has stressed in the past months, the *fondi* of wealthy European oligarchical families have been grabbing any gold assets available, as the prices were plunging, to position themselves in the one asset that will survive the shakeup which has already begun. More than 150 tons of gold assets have been liquidated by Third World holders since the year began, and acquired by the *fondi*. The astute Japanese have acquired no less than 88 tons in the last seven months.

Gold and an 'independent Europe'

As preparations accelerate to organize and control the crisis in the United States, and make U.S. gold stocks available to foreign-dollar debt holders, a European counterpart has surfaced which originates in the same circles.

As the notorious Siena Group of monetary experts owned by the *fondi*'s oldest bank, the Monte dei Paschi di Siena, convenes the first week in September to discuss gold, the new Socialist finance minister of France, Jacques Delors, has launched a propaganda campaign for setting up among European Community (EC) member countries what he called "a dual system of interest rates" or a "European interest-rate snake" aimed at "decoupling European rates from those in the dollar area." Delors specified that he wanted to disjoint "external" interest rates—such as those paid on deposits of Arab petrodollars—from domestic rates, which would be allowed to float as low as local conditions would afford. Delors additionally proposed to combine this new "snake" with "a European currency based on the European Monetary System, running parallel to the

dollar but competing with the dollar." In his view, that new EMS-based currency would become the reserve asset held by central banks—within Europe and without.

The influential British Conservative European Parliamentarian Sir Frederic Catherwood, formerly head of the British Board of Trade and now leader of the external economic affairs committee of Strasbourg's European Parliament, proposed simultaneously that Britain at last fully enter the EMS, in the framework of a plan to be voted by the European Parliament to propose a Euro-Arab "treaty" including the issuance of long-term oil-price-indexed bonds by the EC to guarantee the income of oil producers, who in return would stabilize the price of oil and deliver up to \$20 billion a year to the EC.

Taken together, Delors's and Catherwood's ideas are reformulating a proposal issued last March in Trieste by Siena Group éminence grise Robert Triffin and a top EC bureaucrat, Italian nobleman Tommaso Padoa-Schioppa, at a secretive monetary conference organized by the "*fondi* of all *fondi*," the powerful Assicurazioni Generali di Venezia. Their idea—which is now acquiring dangerously real forms—was to set up two competing monetary blocs, the dollar bloc and an EMS bloc (with a probable yen bloc besides), the latter organized around the European Currency Unit (ECU); the two blocs should float against each other with credit and monetary policies inside each bloc centrally regulated and controlled by means of a gold cover for the money supply.

Whoever holds the gold in such a configuration would be able to rig relations between the two blocs—and who controls the key margins of gold at present are the *fondi* that have bought so much metal over the recent period. "Private-sector" raw-materials corporations generally headquartered in the British Commonwealth would exert unchallengeable control over a world of monetary zones, with a European central bank dictating the terms of monetary deflation to the EMS member-countries, just as the gold mechanism would be used in the United States by the Federal Reserve.

The alliance of Lord Carrington's government (it is not clear at this point whether Margaret Thatcher will long be retained even in the limited function of overseer of the "great experiment" in monetarism at home that she presently fulfills) with the Socialist government of François Mitterrand, and other Socialist International forces, has already shaped an alliance of the "old world imperialisms" around the British Commonwealth; the emergence of the gold option signals that the policy of an "independent Europe" playing the role of a third force between the superpowers—the policy Carrington is deploying all his efforts for—could now take monetary form.