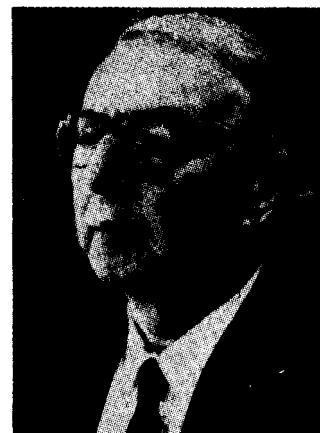


The Zijlstra-Mundell plan for BIS credit restriction

by Kathy Burdman



Jelle Zijlstra

Addressing the annual meeting of the Per Jacobsson Foundation of the International Monetary Fund on Sept. 29, Bank for International Settlements Jelle Zijlstra outlined the official BIS central bankers' proposal for a return to gold. It is based on a sophisticated plan, not for an overtly deflationary British system, but for a return to a "neo-Bretton Woods" gold/dollar exchange standard, at least in its first phase.

While the BIS plan might seem to be a reasonable version of a reinvigorated dollar-centered monetary system with gold backing, the intent is otherwise. Zijlstra proposes to enforce nations' adherence to the new gold standard through *supranational* control at the BIS and the OECD over national credit issuance and budget policy. He specifically called for nations to impose credit controls, and if necessary, incomes policies.

The day following Zijlstra's speech, Robert Mundell, chairman of the Italian Siena Group and stepfather of supply-side economics, issued a remarkably similar proposal on the editorial page of the *Wall Street Journal*. Although Mundell told *EIR* in an Oct. 1 interview with Kathy Burdman that he hadn't personally consulted with Zijlstra, the Siena circle has long worked directly with BIS Director of Economics Alexandre Lamfalussy; and Professor Mundell characterized the two plans as "identical."

The Mundell plan, or BIS plan for short, is the only proposal on the table other than that of *EIR* founder Lyndon LaRouche's which proceeds from the international need to *remonetize gold as a medium of exchange between, primarily, governments*. Both propose that the Bretton Woods system of gold valuation be reinstated, in which central banks would convoke an international monetary conference to attempt to establish an official central bank gold price in the region of \$300-\$600 per ounce. Under the BIS plan, the dollar would remain a reserve asset of all participating nations, and the central banks would undertake to jointly use their reserves

among central banks, to maintain the agreed-upon official gold price backing the dollar. The BIS plan would not involve a formal gold peg at first.

Under the initial phases of the BIS plan, only central banks would have access to each other's gold reserves, and there would be little danger of a run on American gold reserves by central banks. Neither foreign nor American private dollar holders would have the right to demand U.S. gold assets. There would be no U.S. domestic "gold peg." The private gold market would be allowed to continue on its own, alongside the new central bank official gold market, which would be insulated from the private gold price. Professor Mundell refers to this as the "first or transition phase" of his program.

This system, as far as it goes, is inferior to the LaRouche proposal, in that it provides for no new credit generation from the remonetized official gold reserves. However, it is a perfectly sound gold/dollar system; and if all nations pursued domestic policies of credit expansion for high-technology investment in capital goods and exports to the developing sector, it could support acceptable growth in world trade.

Mundell told *EIR* he wants a "second" phase to the BIS plan which would do the opposite. The BIS proposes instead to slash world credit creation, first by clamping drastic central bank controls on the Eurodollar markets, and then imposing equally drastic supranational control over domestic credit policies in the West. Through these "transitional" measures, the central banks would seek to reduce credit supply throughout the world to the point where the official central-bank gold price could be brought into "synchronization" with the private-market gold price. That is, a fully convertible British 19th-century gold system would be eventually restored.

Mr. Zijlstra does not elaborate this, but announced that the new central bank gold system is to be "managed" through supranational agreements to impose "multilateral" economic policies upon sovereign members' econ-

omies. Among the programs suggested by the BIS were credit controls and whatever other policies deemed necessary to reduce incomes and inflation to internationally established levels. In the past, the BIS has demanded in particular huge budget cuts in the United States and Europe.

Even if the BIS is not contemplating any early move to full gold convertibility, this program would be deflationary enough to ensure an international depression—not to mention trampling on the national sovereignty of the United States. Professor Mundell, however, argued to *EIR* that the central-bank negotiations on the official gold price should lead to “negotiations on how to impose discipline on international monetary creation so as to eventually bring the private market gold price into line with the official price.”

First, Mundell noted, “is the Eurodollar market, which has \$1.2 trillion in stateless money and which must be reduced to manageable size.” He advised that the central banks would negotiate restrictions on the Eurodollar market, such as reserve requirements and outright Euromarket credit controls, so as to reduce international liquidity there, in particular reducing loans to the Third World. This was precisely the subject of a BIS meeting in Washington of the International Conference of Banking Supervisors during the last week in September. There, U.S. Federal Reserve Governor Henry Wallich and Bank of England Director of Bank Regulation Peter Cooke made extensive statements urging central banks to negotiate mechanisms in order to reduce the level of credit in the Euromarkets and bring them under close BIS control.

Simultaneously, Mundell told *EIR*, central banks are to negotiate supranational “stabilization policies” for their domestic economies. Each central bank and finance ministry is to join in what Mundell’s 11-point plan calls “multilateral surveillance of the balances of payments problems and exchange rate policies of major countries . . . along with multilateral discussion of anti-inflation policies and unemployment-stagnation problems.”

Such policies would be aimed at greatly restricting credit to industry within each economy, such as “incomes policies . . . and budgetary surpluses” in inflationary periods like the present one, Mundell writes.

Eventually, he said, “we will drain enough inflationary liquidity from the system to return to the world as it was when the British ran the banking system in the late 19th century. Gold will be fully pegged, and we will be able to reform the central banks so as to remove discretionary creation of credit by the monetary authorities. We can use the central bank discount rate then as a penalty rate, as the Bank of England did, and as Lewis Lehrman has proposed. The only difference between my plan and Lew’s is that I propose taking a slower route to the same ends.”

Mundell: ‘Surveillance’

From Prof. Robert Mundell’s commentary in the Sept. 30 Wall Street Journal, titled “Gold Would Serve into the 21st Century”:

The basic ingredients of a restored *Equilibrium Atlanticum-Pacificum* would involve the following elements:

1. Stabilization of the dollar price of gold, probably in the \$300-\$650 range, to be determined by the U.S. in consultation with its allies.

2. Issuance of a gold coinage (various fractions of an ounce) with a face value equal to the stabilized gold parity.

3. Stabilization of other currencies—particularly the DM to the dollar in the DM1.80 to DM2.20 range.

4. Attention to the gold “discipline” by the U.S. such that the U.S. money base is allowed to increase or decrease with gold purchases and sales.

5. Attention to the balance-of-payments discipline by the non gold-pegging countries such that the national money base rises or falls with increases and decreases in holdings of gold and foreign exchange.

6. Co-ordination of interest rates to prevent excessive disparities from developing between money market centers and gales of hot money disrupting confidence and purchasing power parity relationships of exchange rates and price levels.

7. *Multilateral surveillance of the balances of payments problems and exchange rate policies of the major countries within an OECD-OPEC institutional framework, along with multilateral discussion of anti-inflation policies and unemployment-stagnation problems.*

8. Programmed adjustment of dollar-gold portfolios of major reserve holders to encourage more expansive or restrictive monetary policies in the center reserve country or countries (initially the U.S.).

9. *General budgetary policies and if necessary, incomes policies, should be employed to mitigate the business fluctuation, with tax cuts and extra government expenditures to stimulate aggregate demand, and reduce unemployment during recessions, and budgetary surpluses to restrain aggregate spending in periods of inflationary boom.*

10. Reform of tax rates and structure in the U.S. and other countries to enhance incentives for more employment saving, productivity and growth of potential output, to offset distortions arbitrarily produced by past and anticipated inflation; replacement of the income tax by a 20 percent value added tax should be considered.

11. Balance of government budgets over the cycle at levels of deficits necessary to keep debt ratios at realistic proportion to GNP, thus making central bank finance of the government-sector deficits unnecessary.