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EIR: But Volcker denounced Reagan's tax cuts last week.

A: Volcker wants the individual tax cuts rescinded or postponed, and all the loopholes closed.

EIR: Aren't you worried that foreign central banks sold $800 million in U.S. Treasury bills last week?

A: They're not dumping, net. The French sold a lot of short-term Treasury bills to support the French franc, which they did in dollars. They sold a lot more than $800 million, that's just the net. They did over $3 to $4 billion in total intervention when the EMS was re-aligned. But they sold a lot of the Treasuries to the Kuwaitis and the Saudis—the Arabs are buying plenty. Short-term U.S. Treasury rates have come down in spite of what the French did, because there is a big capital inflow, net. Kuwaitis are buying up Los Angeles real estate.

Sadat's assassination won't hurt the dollar, it just makes the U.S. and Treasury bills a safe haven from Mideast instability. . . . We can get along without Mideast oil. No matter how destabilized it gets.

There's now been reached an upper limit to energy prices, where demand is fully responsive to price rises. Yamani is right about that. We will just cut our imports more. The U.S. is the best positioned of any industrial economy. This works in favor of the dollar, and the British pound. The U.S. will simply buy less than everyone else, and Europe and the Third World will suffer the most. And Japan.

U.S. Economy

Industrial chain reaction, not 'fine-tuning'

by Richard Freeman

Federal Reserve Board Chairman Paul Volcker's underlings claim that he can finely tune his control over U.S. money supply and interest-rate levels over the next several months so that he can gently ride the U.S. economy down into full recession, but avoid a sharp industrial crash. The latest steel operating-capacity figures disclose that the economy is not going to be so tidily controlled.

This March, steel operating rates were up to 87 percent, as steel was produced at near-capacity levels for rapid auto output. Those cars were soon to sit unsold on auto dealers' lots; once the downturn in auto sales caught up with production schedules, auto companies were forced to cut back production.

As a result, the steel industry produced at only 70.8 percent of capacity for the week ending Oct. 9. The fact that steel operating capacity had fallen 1.6 percentage points from the previous reporting week indicates how fast the industry is unravelling. U.S. Steel announced Oct. 1 that it will close down one of two remaining blast furnaces and two open hearth steel-making furnaces at its Fairless, Pennsylvania works, and will lay off 850 workers.

Developments in other industries show that unemployment—which reached nearly 8 million in September—will continue to increase. The construction industry is indicative. Employment there, which had shown some growth in the later part of 1980 and early months of 1981, fell by 20,000 in September; it has declined by 165,000 since April. The number of construction jobs in September actually tumbled below the July 1980 recession trough level. And the latest report for the month of August, which shows housing construction down to an annualized 937,000 units, 50 percent below normal levels and falling fast, means that construction employment is in for a further big tumble.

Chain-reaction effect

By slashing hard into basic sectors of the economy, Volcker necessarily cuts the props out from other sectors. The fall in the housing and general construction sector has had terrible repercussions for the forestry and lumber industry. Forest company output will be down 10 to 15 percent this year.

The auto industry exemplifies the chain reaction, as indicated above. The Big Three auto producers announced Oct. 1 that the production schedule of cars for the fourth quarter of this year, at 1,544,000, is down 8 percent from last year and will be the lowest level of output since the fourth quarter of 1970, when an autoworkers strike against General Motors, the nation's largest auto producer, wiped out most of GM's production. The cutback in auto production will not only lead to a new wave of layoffs—in an industry with more than 175,000 workers already on indefinite layoff—but will also trigger layoffs in industries that ship a good amount of their output to auto. This is the case in steel, as already documented.

It is also true of aluminum, where orders for the first two weeks of September were down 17 percent from last year's levels. The aluminum industry, of course, also ships to the aerospace and consumer durables sectors, the latter of which is not doing well either. Aluminum

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operating rates are rapidly pushing below 80 percent, and the announcement Oct. 9 by the number-three aluminum producer, Kaiser Aluminum & Chemical Corporation, that its third-quarter earnings fell a stunning 75 percent, lends credence to the Sept. 30 assertion by one Wall Street analyst that "high interest rates will probably choke the sector" further, and that the profits of some aluminum companies will be down as much as 30 to 50 percent below 1980's weak levels.

Two choices

Paul Volcker's actions remind one of the TV repairman who announces, "Don't worry, I'll have this baby working in a jiffy," and then proceeds to take a sledgehammer out of his repairman's kit and smash the set to pieces.

This is how delicately the loutish Volcker is "fine-tuning" the economy. Remarks by American Treasury Secretary Donald Regan on behalf of the President to the effect that Volcker is "perhaps undershooting" monetary targets reflected a glimmer of recognition on the part of the White House that something is going drastically wrong—but only a bare glimmer of recognition.

In March 1980, Volcker imposed lending limits and extra reserve requirements on all banks, as well as raising the discount rate by three extra percentage points for all money center banks with more than $500 million in assets.

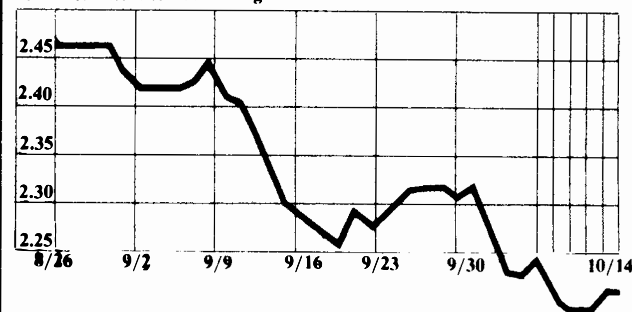
Volcker proceeded to elaborate that his policy was not meant to force a contraction in auto loans or home mortgage lending. Needless to say, these were the first two sectors that got crunched. By May of 1980, production was down 5 percent, and Jimmy Carter, watching his chances for re-election evaporate as tears streamed down his eyes, telephoned Volcker and told him "ease up." The economy managed to climb by December 1980 to a level below its 1979 production levels, and then clung to this depressed December plateau for the next several months. When, by summer 1981, the economy had not turned downward again, several economists proclaimed that the U.S. economy is "impervious" to high interest rates.

Of course, the economy cannot "adapt" to high interest rates, even if they were "only 10 or 12 percent." An economy cannot bear a rate of interest that drives the cost of funds higher than the *rate of real profit* that can be generated by industrial firms. Interest payments of 17 to 20 percent can be paid from only one of two sources: from real industrial expansion and the resulting profits, or from the destruction of the underpinnings of industrial and agricultural capacity.

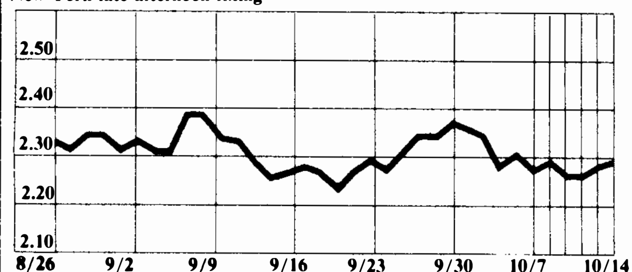
These are the only two choices; there is no third way. There is no evidence that President Reagan understands this point.

Currency Rates

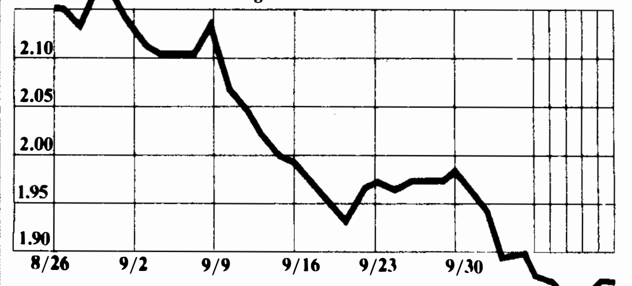
The dollar in deutschemarks
New York late afternoon fixing



The dollar in yen
New York late afternoon fixing



The dollar in Swiss francs
New York late afternoon fixing



The British pound in dollars
New York late afternoon fixing