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Congress punts on the Volcker bailout issue

by Ronald Kokinda, Washington, D.C. correspondent

Something worse than the dog days descended upon Washington the fourth week in July. 1) Federal Reserve Chairman Paul Volcker announced to the Senate that he intends to bail out the offshore Eurodollar markets with American liquidity, if need be, while denying interest-rate relief to the domestic economy—and he went unchallenged in Congress. 2) The White House attempted to divert attention from the entire Volcker issue by puffing the ludicrous balanced-budget amendment proposal—even though the malignant size of the deficit is largely due to the burden of Volcker's rates on the Treasury. And 3) the Harrimanite wing of the Democratic Party leadership re-launched its proposals for top-down post-industrial rationalization and economic controls—while privately saying they welcome the continuation of Volcker's rates.

The Euromarket question

Not that Capitol Hill has been devoid of talk about financial and economic collapse. The talk is of two kinds. One is impotent, if sincere, wailing about the domestic effects of high interest rates. Despite the fact that Lyndon LaRouche's National Dmocratic Policy Committee has saturated Congress with material on the danger of a Euromarket crash and an inflationary U.S. backup for these bad offshore loans, the subject has not come into the open. Congressmen who were warned a year ago by the NDPC that the interest rates were wiping out industry have finally caught up with that reality, but seem utterly unequipped to deal with the danger of a Euromarket crash. The second kind of doom-mongering are warnings of a U.S. banking collapse that are designed to create the climate for Volcker to take whatever emergency action he chooses, above all bailing out the Eurodollar debt.

Before the Senate Banking Committee on July 20, ranking Democratic Senator Donald Riegle of Michigan addressed Volcker, who was testifying there: "We are in a jeopardy not seen since the 1930s. There have been quiet runs on financial institutions. A top banking officer told me that the U.S. economy is on the edge, and there is a 50 percent chance that we will go over."

Volcker replied that, while "I think the financial system is a strong one in this country," "the Federal Reserve is well aware of its responsibilities as lender of last resort and provider of liquidity to the economy if necessary."

If there were any illusions that Volcker intends to begin providing adequate credit for American industry and agriculture, it should have been dispelled when he stated that 1983 monetary targets would remain at this year's level, that he was pleased by the decline in U.S. real wages, and—on July 21 to the House Banking Committee—that the Federal Reserve would not intervene to save smaller banks like Penn Square (see article, page 12).

A parade of witnesses flanked Volcker to lay out the gory state of the economy due to high interest rates. The picture presented led Sen. Henry Jackson (D-Wash.) to comment that if things continue the way they are, "the next thing we'll have is a financial panic." A source close to Riegle confirmed that the panic talk was

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designed to create the conditions to enable Volcker, the man who has destroyed the economy, to dictate the emergency action, on the basis that "the President has no emergency powers" and that the "Congress will recess soon for the elections."

Being saddled with Volcker's high interest rates is recognized by many Republicans as a tremendous election-year liability, but even those most hostile to Volcker did not raise the issue of a bailout of the Eurodollar market. Rep. Stan Parris (R.-Va.) told Volcker on July 21 that "if the nation's economy is reduced to a pile of rubble the battle [against inflation] may be won but the war lost . . . if you are wrong in your policies you will have done a great and irreparable harm to the American economy . . . you may be remembered as the Benedict Arnold of monetary policy. . . ." President Reagan's close friend in the House, Rep. Tom Evans (R-Del.) made a rare appearance before the House Banking committee to tell Volcker that he had "avoided using you as a whipping boy, but I now think that your policies are too rigid." The best that Parris could suggest, however, was to refer to Arthur Burn's tenure at the Fed a "historical justification" for "loosening money supply without inflation."

The consistent theme among the Harriman-controlled Democratic Party leadership, a theme which was initiated by Sen. Ted Kennedy (D-Mass.), is that the high rates are just what the Reagan administration wants, that Volcker is only following administration wishes. Spokesmen for the administration have lent credibility to such charges. Hours after Volcker appeared before the Senate Banking committee, presidential press spokesman Larry Speakes told the press that "we want interest rates to come down, but we agree with the Fed's existing monetary targets." Murray Weidenbaum, as chairman of the President's Council on Economic Advisers, appeared before the Senate Banking committee the day after Volcker on July 22. As Sen. Paul Sarbanes (D-Md.) reported, "Weidenbaum made clear that the Fed was pursuing the policy that the administration wanted." It is possible, but not likely, that Weidenbaum's abrupt departure was related to his endorsement of Volcker.

Casting himself in the role of the Washington "outsider" attacking big government, the President was also taking the heat off of the Fed by addressing a top-down organized rally on the Capitol steps July 20 for a Constitutional amendment for a balanced federal budget. *EIR* has heard for the last five months from Volcker supporters on how the balanced budget campaign would get the Fed off the hook. The White House views it as an easy means of political gains in popularity, although it would be an unconstitutional farce at best and a terrible blow against defense, Social Security, infrastructure, and other necessities at worst.

As the Republicans and the White House reduced themselves to the appearance of total complicity with the Fed, the real Democratic gameplan was summarized once more by a staffer on the House Banking Committee. "The last thing we want is for the Fed to change its monetary policy," the staffer said. Volcker has done a very good job on the economy. He's done a good job bringing down inflation, and a very good job bringing down wages. We don't think credit should be growing any faster," he said, arguing that all that is needed is a "limited bailout" of Eurodollar banks, not a general increase of credit to the economy. The aide further confirmed that "the Democratic leadership is not interested in any change of Fed policy and if Reagan attacks the Fed, we'll defend the Fed. . . . Reagan knows that we will do this, and that is why he has not come out openly against Volcker."

While the Democratic leadership focus has been on the panic, a drumbeat continues for the Democratic National Committee's program of credit controls, wage and price controls, and a surrender of the U.S. economy to the International Monetary Fund. Hearings held in July on national urban policy in the congressional Joint Economic Committee organized by Rep. Henry Reuss (D-Wis.) laid out the alternative. Felix Rohatyn, author of New York's Big MAC, demanded of Congress that a Reconstruction Finance Corporation be set up to bail out the large banks "whose fragility is cause for serious concern." Sen. Daniel Moynihan (D-N.Y.), an early advocate of the "benign neglect" approach to minorities, urged that some financial institution was needed to ease the formerly industrialized, formerly urban centers into the post-industrial society. "The great manufacturing cities that grew up in the 19th century had entered a period of sharp decline for the simple reason that the economic functions they once served—especially those associated with density—are no longer decisive. The cities would no longer serve the economic function they once had done, and there would be much social disruption." Another witness Reuss brought before the committee was Chase Manhattan Bank's Philip Braverman, who was even more explicit: "A national financial entity may be appropriate to provide assistance to the cities willing to make hard sacrifices. The IMF provides such assistance to nations; we should be prepared to do no less for our own cities."

Volcker openly affirmed his agreement with Moynihan in a response to Rep. Stan Lundine (D-N.Y.) at the House Banking Committee hearing. Lundine warned Volcker that "the future of American industry is at stake. . . ." Volcker's reply: "Our manufacturing base has been declining for a period of time. This is becoming a less important section of our economy—which may be a reflection of a trend toward a post-industrial society." That statement went unchallenged by the committee.