Bundesbank sends an interest rate message

by Chris White

On Oct. 5, the Central Council of West Germany's central bank, the Bundesbank, increased its primary lending rates—the discount rate and the Lombard rate—by 1% each. Contrary to the insane insistence in U.S. political and financial circles that the interest rate increases were "a purely technical adjustment," intended to curb resurgent inflation inside the Federal Republic, the opposite is the case. The increase, to the highest levels since 1982, was done neither for technical reasons, nor for any internal reason. Anyone who says that, simply proves that along with approximately 70% of the U.S. population, they are out of the real world, or that such idiocy, for career management or other bureaucratic reasons, is what they have to be overheard saying at the moment.

The Bundesbank's Central Council members did have a choice. The choice was between raising the Lombard and discount rates by one-half of a percentage point—in which case the action could perhaps have been ascribed to the "technical adjustment" the Americans insist it to have been—and the increase adopted of a full percentage point. The latter was chosen, and it was chosen for purely political reasons.

First and foremost, the political reasons involved include the intent to send a message to those who run things in the United States that enough is enough. Through the Bundesbank, effectively the central bank for continental Europe as a whole, leading European circles are letting it be known that, in their view, those who run things inside the United States are not competent to hold the monetary and economic system together. The interest rate increase is the first assertion that key U.S. allies are losing confidence in the moral and intellectual capacity of the U.S. leadership to govern.

That the message was sent on behalf of continental Europe as a whole is easily shown. Within minutes, the central banks of England and France had followed suit. By the next day, the entire credit system of Western Europe had been realigned around the Bundesbank's new base rates. London, where the base lending rate is now at 15%, did not go along so willingly, but was compelled. Sour grapes from that quarter were not kept secret. London's *Financial Times* complained editorially that same morning that it has become redundant to continue discussing when Europe will have its own central bank. That bank already exists, to the dismay of the newspaper's editors, and it is West Germany's Bundesbank.

That the Bundesbank's choice of the full percent increase was intended to deliver a shock, was rapidly corroborated by high-level sources in different European financial centers. Delegations returning from the annual conference of the International Monetary Fund and World Bank, held in Washington over the weekend of Sept. 16, had returned with evaluations about what is going on in the United States, identical to those reported by similar such circles in June of this year. "My colleagues simply could not understand the mood of complacency and euphoria over there. All you hear in Washington is 'America's on top, everything is fine, the free market is sweeping the world, there's nothing to worry about.' My colleagues were stunned speechless by this. They could never discuss real problems in Washington," was the report of one.

A deflationary collapse

On Sept. 15, when the market in sub-investment-grade securities collapsed, in the wake of the default of Robert Campeau, the Canadian front-man who had borrowed to buy out the Allied and Federated department store chains, the United States entered into a spiral of deflationary collapse. The collapse dooms the U.S. economy to a new depression, at a pace determined by the rate of acceleration of the deflationary spiral, and by the diffusion of the shocks that will accompany that acceleration. The junk bond market was the first casualty of the end-of-third-quarter settlement process. There may well be more to follow, if not this autumn, then certainly by next spring.

This was the view circulated by jailed U.S. political leader and physical economist Lyndon LaRouche on Sept. 18. The Bundesbank's action is a signal from Europe that under present U.S. policies, that is indeed the perspective ahead. It is a message to get your house in order, or face the consequences. Yet, since Sept. 15, America's powers-that-be have insisted to the world that nothing is fundamentally wrong, that the same methods of crisis management that have been employed since 1982, can be employed again to stave off disaster.

By increasing interest rates, Europe is asserting that it will not necessarily go along with the crisis-management methods the U.S. crowd is so accustomed to employ. Thus, the Bundesbank and its backers are acting, actually, to hasten the development of the deflationary spiral of which LaRouche has warned.

LaRouche has been the one political figure in the United States who has accurately projected the course of economic developments from the late 1950s onward. He has been able to do this because he developed the scientific method, on the basis of the earlier work of the German mathematical physicists Bernhard Riemann and Georg Cantor, and the philosophical method of Gottfried Leibniz, by which economics as such might be subsumed under the physical sciences. Since he projected, in 1979, the economic effects of Federal Reserve chairman Paul Volcker's increased interest rates, he has been proven to be consistently the most accurate, in political and economic forecasting, while those who have opposed him, have proven themselves to be absurd.

The collapsed junk bond market was one component in the financing of the wave of mergers and acquisitions that has swept the U.S. economy since 1982. Speculative increases in stock and real estate prices fed the insane expectation that debt could be taken on, wildly in expense of cash flow, to be repaid out of the proceeds of the eventual sale of parts of the company taken over. The process appeared to work in a rising market, since increasing prices were assumed to permit further increases in debt. In a falling market, the assets for sale do not cover the increasing charge of debt service, and the leverage is reversed against the lenders.

Reality vs. perception

The American side insists that this is not happening. "Yes," it is sometimes conceded, "there is a shake-out of the speculators. But that has been insulated from the market as a whole. In any case, the fundamentals remain strong. There is no reason to fear the type of deflationary collapse of which LaRouche now warns." Such is the view of those who have opposed LaRouche in the past, and who have been proven wrong before.

Their problem now, is that they are not talking about the kind of deflationary collapse of which LaRouche has warned. They look at the money side of the process, and insist that what is primary is *perception*: If people perceive the economy to be going up, then it is going up. So perceptions can be managed, day by day, week by week, and as long as they are so managed, there will be no such development of the kind of which LaRouche has warned.

Clinically, this approach is called psychosis. To the psychotic, the real world, and comprehensible processes, effective in the real world, do not exist, only the contents of one's own head.

This is what people in Europe have begun to conclude, and it is why the Bundesbank was used to increase interest rates. The idea is that the shock which will follow, may perhaps help bring such Americans back to their right minds, by stimulating their minds to function.

Contrary to the "perception managers," the real world including the economy is governed by knowable physical principles. They have got it all wrong. They ought to have listened to what LaRouche had to say, while they still had the chance. He told them repeatedly to forget about money, prices of assets, book-values, and markets. Concentrate instead on the processes under way in the physical economy. Compare the evolution or devolution of the physical economy—measured, per capita and per hectare, in terms of the composition of a standard market basket of producers' and consumers' goods—with the growth of debt and debt service requirements.

As LaRouche has insisted, since the late 1970s the physical economy has been in a process of collapse, while the claims of debt and service have increased astronomically. Under the so-called "recovery," since 1982, the per capita and per hectare composition of such market baskets collapsed back to the levels of the late 1960s, while debt doubled and doubled again, from about $3 trillion to $12 trillion, and since 1985, speculative claims increased by the same $1 trillion a year, that debt was increasing by. Debt service requirements have increased beyond the capacity to service such debt.

The deflationary spiral is determined in the realm of physical economy, not in the realm of perception managers' heads. LaRouche developed the method by which such processes might be analyzed, and proved that the economy, as a special type of living organism, is governed by the same physical principles that govern the development of the universe as a whole. Thus he now insists that the quality of development of the deflationary spiral will be determined as the acceleration of a nonlinear shock-front.

American perception managers insist they can delay such a process into next year, when the same methods can be employed again. Their principal means to do that is to have recourse to hyperinflation, which will itself help ensure that what they most seek to avoid, is exactly what happens.