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FOREIGN EXCHANGE

Yen's weakness rebounds against Premier Ohira

The yen could fall as low as 260 per dollar by the end of January. This is the "unofficial" estimate by Japanese bankers who watched it tumble from 222, just prior to the Volcker shock, to 237 at the end of October. Neither currency interventions by the Bank of Japan (BOJ)—up to $300 million on Oct. 30—nor an imminent 1 percent discount rate hike to 6.25 percent are likely to stem the tide.

The yen is being buffeted so wildly because structurally and politically Japan is much more vulnerable than Europe to the combined effects of credit and oil shocks. A recent *Asahi Evening News* article noted this well known vulnerability, then complained that Japan lacks the protection given Europe by the European Monetary System.

Three years of Carter administration trade and currency warfare have finally taken their toll on the export capabilities of Japan.

With an all-time record $1.4 billion current account deficit in September, Japan's deficit for the first nine months of this year totalled $5.0 billion. This is an amazing turnaround from 1978's $16 billion surplus. Moreover, the physical volume of Japan's exports fell 3 to 4 percent this year, the first decline since the postwar recovery.

Japan's U.S. markets were decimated by protectionism, and Japan failed to make up the difference in Third World markets.

Under the previous Prime Minister Takeo Fukuda, Japan issued long-term low-interest yen and dollar loans to developing countries for plant and machinery purchases. Under Washington's pressure, Prime Minister Ohira forced an end to this policy.

The trade problem has wreaked havoc on the internal finances of this export-dependent nation. When the Carter administration took power the yen was at 290. As Treasury Secretary Blumenthal's dollar depreciation effort took hold, speculators propelled a rise to 180 by November 1978—and a consequent dropoff of export prospects.

Steady oil price rises are sending the yen most of the way back down—but without a recovery of the lost markets, and with a much higher import bill.

Combined with the huge payments deficit, the yen plummet meant an 18 percent annual rate of

DOMESTIC CREDIT

Reuss wants to close the discount window

The following are excerpts of House Banking Committee chairman Henry Reuss's (D-Wisc.) proposal on credit policy, which exemplifies the degree of "liberal" support for Fed Chairman Volcker's credit rationing. The proposal came during an Oct. 29 session of the Banking Committee, in an exchange with Fred Schwartz, Vice-Chairman of the Federal Reserve.

Reuss: I have applauded the actions of Oct. 6 by the Fed and continue to applaud them. ... The discount rate is now at 12 percent; Citibank and other lenders are now lending at a prime rate of 15 1/4 percent. My question is, should the discount rate be increased: Doesn't it have a life of its own as a symbol to the world? What I am saying is that you should stop vitiating your overall monetary strategy and close the discount window except wherever there is a real liquidity problem. Having rid yourselves of the federal funds fetish, why not rid yourselves of the discount rate fiasco?
Schwartz: We are looking at the whole question of the discount rate, including your suggestion of a floating discount rate.

Reuss: No, I am talking about no discount rate at all; close down the window.
Schwartz: Well, that is a pretty stringent policy, the effect might be an even tighter policy than we would like. The discount window is a sort of a safety valve.

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inflation during the last six months. Inflation itself feeds a further fall in the yen, thus more inflation.

Japan is simultaneously the advanced nation most dependent on oil imports and the one least protected against arbitrary price hikes and outright cutoffs. According to the Ministry of International Trade and Industry, Japan will experience an absolute shortage of oil this winter, owing to cutoffs of so-called third party contracts by the Seven Sisters and other oil firms; the cutoff is expected to affect up to 30 percent of Japan's consumption. Direct deals with oil producing nations fill part of the gap. But 15 percent of oil consumption is now imported at the exorbitant $38-45 spot market prices, and the makeup has been insufficient.

Ohira's support for Washington's Camp David Mideast policy and his government's anti-Mexico moves have severely crimped Japan's ability to get sufficient direct deals from OPEC and Mexico respectively. Meanwhile, oil and other commodity price hikes comprised the brunt of the increase in Japan's import bill in this year's July through September period of 60 percent over July-September 1978. Further oil price rises will hit the yen.

Ohira on the line

Washington is trying to catch up with the political repercussions of Japan's predicament. Paul Volcker, Cyrus Vance, et al. may wake up one day very soon to find that their favorite, Masayoshi Ohira, is no longer Prime Minister of Japan. Many business leaders resent Ohira as, at least, unable to protect Japan from Carter's hostile actions, and at worst, liable to go along with Washington policies, as witness his tax hike proposal and his anti-OPEC stance.

The chairman of the Keidanren business federation, Toshio Doko, called upon Ohira to resign last week, seizing the occasion of the election setback of the ruling Liberal Democratic Party. Keidanren also opposed the interest rate hike the Bank of Japan is about to impose. A look at the dim prospects for the economy makes many business leaders yearn for the days of Ohira's predecessor, Takeo Fukuda. The campaign of Fukuda and his allies to remove Ohira has gained momentum in business circles, and at this point, Ohira's imminent demise is widely recognized as a distinct possibility.

Whether a new government will try to revive and expand low-cost export lending will then be the question. Otherwise Japan will continue to face its high yen/low exports, low yen/high inflation bind—and the threat that spreading U.S. depression will wreck world markets.

—*Richard Katz*

Reuss: How much lending has gone on through the discount window since the announcement of the Oct. 6 policy?
Schwartz: About three times as much as normal.

Reuss: Well, I must say, that's a hell of a way to run monetary policy. You bear down on the open market, and let anyone come in through the back door to the discount window.

The following are selections from the testimony of several noted liberal economists before the Joint Economic Committee of Congress Oct. 29:

John K. Galbraith: We are relying too much on monetary policy and administration pronouncements. ... The only safe approach is to use all the instruments of the government against inflation; hold in bank lending, cut the budget (I mean, of course, areas such as defense and unnecessary public works), heavy taxation on luxury goods, a tight control on the wage-price spiral and recognition that voluntary measures are not working, and bring down energy prices. We can have no talk of a tax cut.

Alan Greenspan: The danger today is not of a repeat of the events of 1929 from a deflationary standpoint, but of excessively inflationary policies rushed into place in response to a credit crunch.

Walter Heller (in response to a question from Henry Reuss: Do you agree that West Germany must adopt tighter fiscal and easier monetary policies?) ... I would. The escalation in West German interest rates hurt the dollar. The dollar problem is a deutschemark problem. We have a stronger deutschemark today at the expense of the world economy. This interest rate game is making the world suffer. And West Germany suffers as well. In the past five years, West Germany has had a smaller growth rate and a higher unemployment rate than the rest of the OECD. (Mr. Reuss replied: "I am glad to hear you say that. At least with our names, we can't be considered anti-German.")