Click here for Full Issue of EIR Volume 1, Number 43, December 26, 1974

PETRODOLLARS CAUSE CHAOS ON FOREIGN EXCHANGE MARKETS

Dec. 24 (IPS)--Foreign exchange markets were in chaos yesterday as gold closed at the highest price ever, $193.50 an ounce in London, and the sinking dollar touched an all-time low against the Swiss franc and a seven-month low against the West German mark. Today this trend continued unabated.

The collapse of the U.S. dollar, the principal currency for oil payments to the oil-producing countries, is directly related to Rockefeller's failure to come up with an international petrodollar recycling mechanism that could channel these mounds of worthless paper to "development projects" where long-term profits would be guaranteed. Now, there are too many petrodollars chasing too few safe investment channels.

Just as the Swiss bankers had done earlier, Arab investors are now converting their latest bounty of dollars, acquired Dec. 20 as oil payments from the consumer countries, into gold. In addition, they are going for the stronger European countries. The Arabs are not attempting quick, windfall profits but are being forced to minimize their short-term losses.

Unwanted Petrodollars

Both the West Germans and the Swiss are panicked at the conversion of petrodollars into their currencies for fear that their currencies will be bid up and undermine their export competitiveness. As demand for their currencies increases, their goods would become increasingly expensive in relation to the dollar and other weaker currencies; goods and services produced by weak-currency countries would be relatively cheaper. To deter this, the Swiss are offering a negative interest rate on foreign deposits and the West Germans reduced their interest rate even further. Ironically, France and Italy, the two countries on Rockefeller's credit blacklist until recently, are now the beneficiaries of the dollar glut. Both countries have received upward of $1 billion each from the Shah as pre-payments for future technology exports to Iran.

Foreign exchange traders in New York believe that none of the recent crop of petrodollars is expected to reach U.S. shores. The fear of further straining their over-stretched capital equity ratios is prompting Rockefeller's New York banks to refuse any new petrodollar deposits. (Capital-equity ratio, the relationship of total deposits to the total claims on profit, is a critical index of a bank's economic health. Generally, the lower this ratio, the healthier the institution.)

Diverting dollars from European currencies and attracting them to the U.S. in an effort to save the value of the U.S. dollar will not work either. Petrodollar inflows into the U.S. economy in the absence of slave-labor energy development projects

© 1974 EIR News Service Inc. All Rights Reserved. Reproduction in whole or in part without permission strictly prohibited.

would be inflationary and would further weaken the dollar vis-a-vis gold and some European currencies. With the energy projects stalled, no matter where the petrodollars go, the net effect will be a weaker U.S. dollar. If this trend were to continue for a few weeks, the international monetary system, which is based on the purchasing power of the U.S. dollar, would collapse, plunging the world into catastrophe.

BANKERS' NIGHTMARE: BOOM OR BUST

Dec. 24 (IPS)--The top echelon New York banking community is anxiously trying to decide which is the worse nightmare: an inflationary spiral or a deflationary collapse.

These gentlemen know that any possible benefits of either reflation or deflation are far outweighed by the obviously disastrous effects that either will inevitably have. Their state of mind was summed up by one bond trader who, when asked if he saw any way between Scylla and Charybdis, replied, "I'm not smart enough to know."

The question facing the banks is whether to go on financing the massive debts of corporations and government at a time when orders, production--the whole real economic process--is at a standstill. Printing more paper to refinance the debts would be wildly inflationary. Yet without those pieces of paper, there will be a chain reaction of bankruptcies.

In January, U.S. corporations will be coming to the market to sell around $3.7 billion in bonds. They are rushing to sell their debt to meet immediate cash needs, as well as to turn short-term bank loans into longer-term obligations. But where will all the money come from?--especially since the U.S. Treasury will also be coming to the market to finance its gigantic budget deficit.

"I don't know where the money's going to come from" is the frequent response of corporate bond traders. Life insurance companies, bank trust departments, and pension funds will continue to be customers for corporate bonds, with the latter expected to be "seasonally" active. This January, however, their money will not be enough to hold up the market. Corporate bond traders expect money to stay very tight and rates very high. "Pump priming" is the only solution, but they admit it is no solution at all; it will only blow up the economy with more worthless dollars.

Henry Kaufman, partner of Saloman Brothers, an important investment house, represents the other pole of opinion. He is less worried about corporate and government financing needs, believing that they can be met. For him the real nightmare is an