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Book Review:

'Towards Full Employment And Price Stability'

TOWARDS FULL EMPLOYMENT AND PRICE STABILITY
SUMMARY of a report to the OECD by a group of independent experts.
OECD, Paris; June 1977
$4.50, 52 pages.

Since the release of the report under consideration here earlier this month, the annual meeting of the finance and foreign ministers of the 24 nation-members of the Organization for Economic Cooperation and Development appears to have accepted the basic principles it sets forth. Certainly U.S. Secretary of State Cyrus Vance's suggestions towards an OECD "master plan" worked out among the leading countries on an annual basis point in the direction of the "Full Employment" report's recommendations.

This strongly suggests that the American media vastly underrated the importance of the document, and that even the more extensive reviews of such foreign media as the London *Financial Times* failed to anticipate the true intent of the study. For behind the impenetrable technocratese of the OECD experts' report there is a simple and unmistakeable message: to put the economic policy footing of the advanced capitalist countries on the lines of Germany in the 1930s.

From the communiqué of last week's ministerial meeting only an approximation of this emerges, in the form of recommendations for deflationary austerity in the weaker OECD members, "markets" oriented appreciation of the currencies of the stronger members, and scads of new official financing through the realization of the old Kissinger $25 billion "safety net" plan, and the so-called Witteveen special facility for balance of payments financing through the International Monetary Fund. But the darker aspects of the "Full Employment" study are waiting for implementation just beneath the surface of public policy, especially in the United States, which is being given the bums' rush towards Schachtian economy. Earlier this week, before the ministers left for their annual meeting in Paris, a high-level meeting of Treasury, Federal Reserve, and New York banking officials occurred in Washington, with recommendations identical to those of the OECD study. These include managed raw materials prices, elimination of "cost-of-living escalator-induced inflation," massive official financing of deficits, and the "psychological use" of monetary policy to avert panic over inflation.

Schachtian economy, the best modern reconstruction of which is Brazil, involves systematic looting of labor-power through reductions in living standards, and reduction of skill-levels through a shift from capital-intensive to labor-intensive production. This is done to support a rapidly-inflating government (or government-related) debt structure. Schachtian economy combined pick-and-shovel work on the Autobahnen and war build-up. The enlightened authors of the OECD study do not explicitly say anything that grating. But they surround the unstated premises of their report with the full array of Schachtian devices required to see such a program through.

The study was commissioned two years ago by then U.S. Secretary of State Kissinger, previously, then, and now an ardent follower of Nelson Rockefeller. To the panel were appointed Paul McCracken, formerly Chairman of the Council of Economic Advisors under President Nixon, a member of David Rockefeller's Trilateral Commission, as chairman; and former Governor of the Bank of Italy Guido Carli, a Rockefeller family associate since his 1958 groundbreaking work on economic warfare planning for NATO, the most pro-dollar of European central bankers at his Bank of Italy post between 1961 and 1975, and a close personal friend of David Rockefeller. Other members of the panel include French Trilateral Commission member Raymond Barre who resigned to become Minister of Foreign Trade of France (and afterwards Prime Minister), who was then replaced by fellow Trilateral Commission member Robert Marjolin, the former Secretary-General of the OECD. From West Germany came Herbert Giersch of Kiel University, former chairman of his country's council of economic "wise men," and intermittently a key organizer for the Brookings Institution's "tri-partite conferences." The single panel member from a developing country, former Turkish Deputy Prime Minister for Economic Affairs Attila Karaosmanoglu, is presently Director of Development Policy at Robert McNamara's World Bank. On the record, then, it is no surprise that these economists should espouse Nelson Rockefeller's brand of "enlightened Schachtianism" in their final draft.

Most of the report is unreadable economists' jargon, e.g., "it should be increasingly possible and preferable for the authorities to frame monetary and fiscal policies

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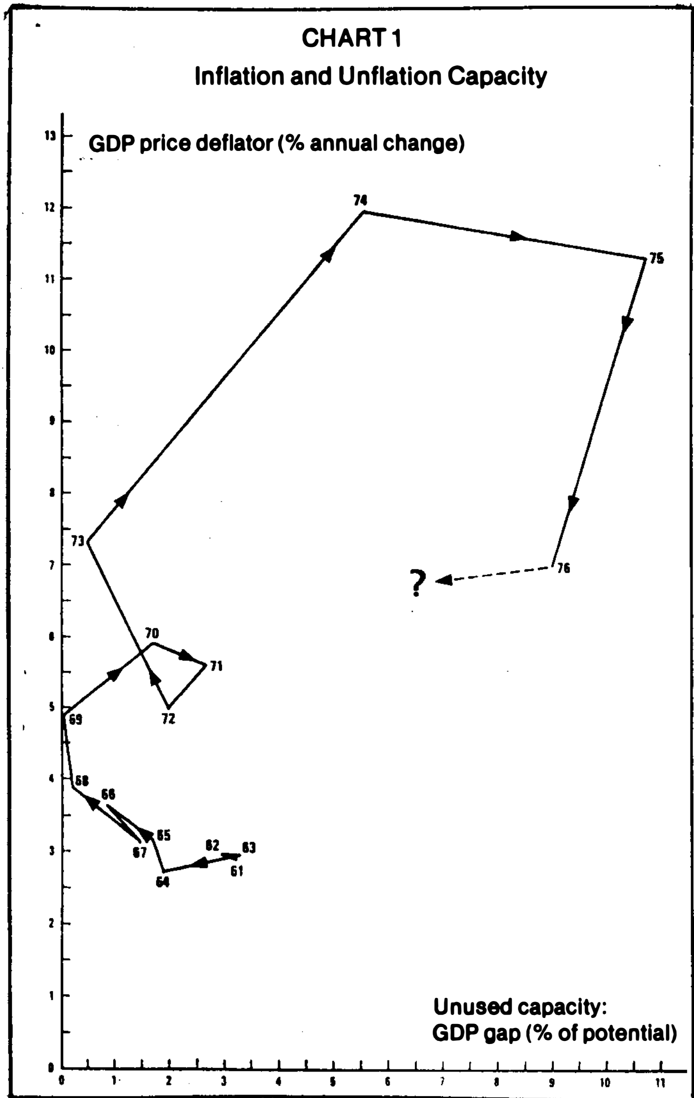
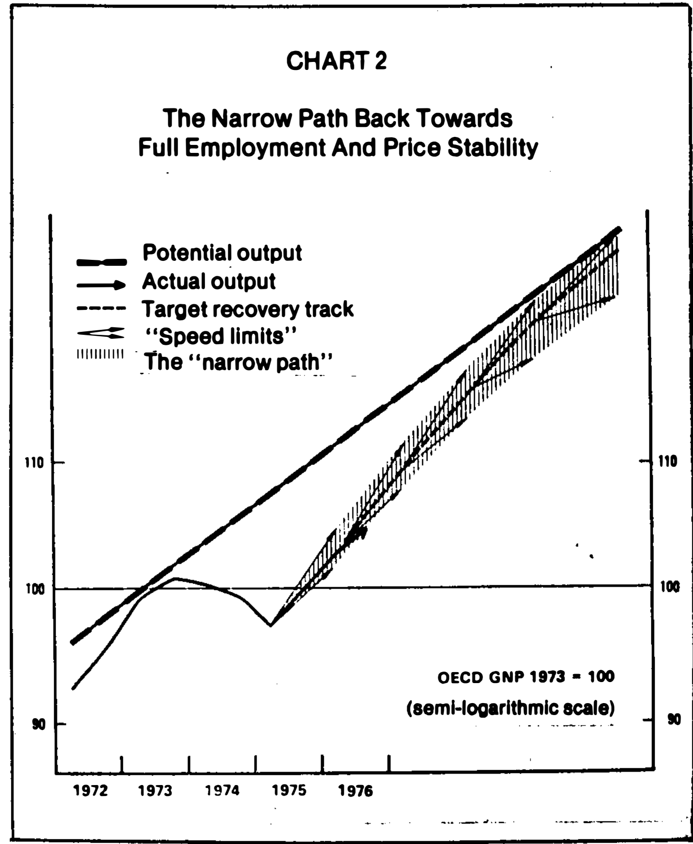
in the light of medium-term requirements and leave correction of minor deviations of aggregate demand from the desired course to built-in stabilizers designed to reinforce such self-correcting forces as exist in the economy (p. 30)." Or, "governments... should also provide a regular analysis of how far deviations of the actual budget outturn from the target reflect discretionary action rather than automatic stabilizers, and how it is eventually intended to rescind or offset the discretionary anti-cyclical action that has been taken." All such catch-phrases refer to concepts that have not been taken seriously much since 1974, and which the OECD group itself otherwise ignores.



In discussing "What Went Wrong," the report sinks to unintentional lampoon of conventional "demand management" economics. The worst gaffe is reflected in Chart 1 which shows the shifts in a modified Phillips Curve (economic activity vs. inflation) as a series of great curlicues which resemble the path of a confused insect on the economists' notepad. At this level, the report's recommendations fall into the worst banalities of official writing:

> At the present time, the authorities should aim to steer demand along the relatively narrow path consistent with achieving a sustained recovery. The lower limit is set by the need for a rate of expansion sufficient to encourage a recovery in investment, both through spreading overhead costs and improving profit margins, and through creating expectations of the need for additional capacity in the reasonably near future. The upper limit is set by the point at which a rapid increase in aggregate demand would re-ignite inflationary expectations *(p. 29)*.

These profound considerations, illustrated hypothetically in Chart 2, leave out the question the financial press, let alone the business community, raises every morning: have the upper and lower limits crossed? Mr. Leonard Silk of the *New York Times*, for example, notes that 6 percent real GNP growth plus 6 percent "built-in inflation" require a 12 percent rate of money supply expansion. (Most economists are now pegging the rate of built-in inflation around the current rate of increase of wages, at above 10 percent). If money supply is less than 12 percent p.a. (and there is now compensating rise in the velocity of turnover), the difference will not come out of inflation, but out of levels of real output. Considering that the Federal Reserve's announced target for the narrowly-defined money supply is a range of 4 to 7 percent growth p.a., and that the investment community would be extremely upset at a rate of money growth twice as fast as Dr. Burns wants, the OECD economists' view becomes pure fantasy. In the real world, the "lower limit" of money supply growth required to sustain current output is already *above* the "upper limit... which would re-ignite inflationary expectations."



The above line of reasoning prompted the London *Financial Times*' editorial comment that the report is "unfortunately but predictably weakest" on the "broad central issue of policy management," a remarkable British understatement.

Nonetheless, the report gets better as it goes along. The first section, tracing the origins of the present crisis, lumps together monetary expansion associated with the 1972 elections, the rise in oil prices, the associated erratic movement of commodity prices. "The most important feature" of the 1971-75 events, the economists write, "was an unusual bunching of unfortunate disturbances unlikely to be repeated on the same scale, the impact of which was compounded by some avoidable errors in economic policy." The reader is left to stare at the spiralling shifts in the Phillips Curve and wonder why, as the study group reports, "there has been a severe deterioration in the short-term trade-off between activity and inflation."

By page 37, the report finally puts down a simple answer — the problem is labor costs. Secondary hindrances to capital investment, the report says, include "risk premiums," the fact that entrepreneurs "are less confident," and "less certain about the availability and future costs of energy and raw materials." But the central cause is "a secular rise in the price of labor and other input costs relative to output prices, and reduced flexibility in the adjustment of labor inputs in response to output fluctuations." (This, turgidly expressed, is the "downside rigidity of wages" that Robert V. Roosa used to complain about). The high labor price leads to "a more persistent form of structural unemployment," even if "cyclical unemployment falls."

After pages of mumbling about matching the flow of savings to budget deficits and so forth, the economists have finally said what they are talking about. In a brief and astonishing section entitled, "Better Functioning of Markets," the core of their domestic policy programs comes through all in a lump. Until this point the study group insisted on a tone of conservative, even market-leaning academicism (e.g., "the severe problems of 1971-75 can largely be understood in terms of conventional economic analysis," and so on). In their section on markets per se, they make clear that their objective is to eliminate markets in favor of Schachtian dirigism. By topic:

1. Labor Markets

The OECD study wants "action more directly aimed at increasing the flexibility of wage structures." Repeating its earlier point, the study warns:

> The tendency towards less flexibility in labor markets may be one of the main reasons why in recent years the unemployment rate at the peak of the cycle has steadily increased in most countries. Unemployment amongst youths and women has gone up at the same time as vacancies for adult male labour have increased. Rigidities in the labour market are partly psychological and legal, but are also related to inappropriate wage differentials and the rising costs of hiring and firing labor *(p. 44)*

In addition, the report suggests tax incentives to employers of the type that the Carter Administration attempted to work into its "stimulus program," namely, using the fiscal system to encourage the expansion of labor-intensive, low-wage, low productivity employment, at the direct expense of high capital formation, capital-intensive employment.

Professed admirer of Schacht and Hitler, Eli Ginzburg, the U.S. "manpower specialist," Carter Labor Secretary Ray Marshall, and others have been sounding this concept out for some time, i.e., degrading the quality of labor-power to loot their way out of the economic crisis. The OECD group feints in the direction of corporativism, e.g., "governments should discuss regularly with the organizations representing business and labor the general evolution of prices and wages to be aimed at over the coming year or so, consistent with achieving or maintaining high employment levels..." and, "A prices and incomes policy for the private sector becomes both more necessary and more feasible the larger and more strongly centralized are the national organizations representing business and labor." It is ambivalent on the issue of building Autobahnen and other primitive Bauarbeit forms of public work ventures. But the basic Schachtian premise is there, namely, that the source of the problem is a rising wage scale — rather than viewing a rising wage scale as indispensable to economic growth — and its solution degrading the quality of labor power to fit the productivity levels of miserable levels of real capital formation.

2. Capital Markets

Incredibly, the OECD authors make indexation of the capital markets their one, central plan, dropping the idea in passing. Indexation, now used in Brazil and not too many other places, involves tying the interest paid on a security to either the cost-of-living index or some other adjustment mechanism in order to guarantee the lender a real rate of return. Outside the capital markets proper, anything can be indexed to anything. Commodity prices can be indexed to overall inflation (this is in any case the point of the buffer stocks for commodities the report's authors propose a bit later). Wages can then be indexed to the price of raw materials. In effect, this is what has happened in Brazil, the model of indexation, where the regime controls all prices, and real wages have fallen 50 percent as a result. But such accelerated forms of looting of labor-power are not that far away from the richest of the industrialized countries. In the ongoing negotiations between the Unites Steel Workers and U.S. copper companies, there is a proposal on the bargaining table to index the wages of copper workers to the market price of that metal! Considering that copper has fallen from almost $1.50 a pound at its Spring 1974 peak to about $0.61 a pound now, below its cost of production, the implications are terrifying. On present recollection, the last time such a wage agreement existed in the United States was when southern migrant labor in the 1960s was paid according to the quality of the beans they harvested.

The OECD group does not draw out all the implications of their suggestion, but it does hint at them in proposing

> the removal of institutional obstacles to the issue of indexed bonds. These would reduce uncertainty for borrowers and provide savers with better protection against inflation. *Availability of indexed bonds*

should also help to stabilize prices of other assets, such as land and raw materials, in inflationary periods. Most of us also believe that governments themselves should also be prepared to issue indexed bonds. *(p. 45)*

It would have been Hjalmar Schacht's dream come true to see such things happen. Schacht's system combined inflationary issues of government paper for military and make-work spending with systematic reduction of the quality of labor-power. Under the OECD schema, indexation would tie one to the other by simple arithmetical formulae and eliminate all the uncertainties of Schachtian planning.

Nothing shows up the deceitfulness and the true intentions of the study better than the indexation plan. After all the rambling about non-inflationary growth, what the authors propose is a device that is notoriously the last resort against hyperinflation, which has gained credence nowhere in the advanced sector except among the British followers of Milton Friedman (*London Times* Economics Editor, now Ambassador to Carter's Court, Peter Jay, made the only serious plea for indexation to come from an industrial-country economist during the height of Britain's inflationary crisis in 1975).

To wrap up, the authors propose not exactly commodity indexation but something very close to it:

> action to reduce the vulnerability of the world economy to shocks, arising either from interruptions in supply or sharp fluctuations in demand. As regards food, we agree on the desirability of building up security stocks of cereals. For industrial raw materials, we support policies designed to encourage international investment, consistent with desires of host countries to maintain sovereignty over their resources, and in some cases action to reduce the stability of commodity prices through buffer stocks. *(p. 46)*

Put it all together: breaking up the wage market under the slogan, "increase the flexibility of wage structures;" indexation of the commodities and capital markets; the assumption of inflation and austerity; these elements and their combination are the Schacht system revived in its entirety.

If this were not sufficient, the study betrays itself by proposing the Schachtian trump card, i.e., paying off industrial workers through shares in their enterprise, "peoples car" swindles, and related devices, through which Schacht skimmed off 20 to 30 percent of German wages that had already fallen to half of their 1928 levels. It recommends

> more radical solutions which introduce an 'equity' element into wage payments, for example through schemes for employee participation where renumeration is partly in the form of share issues and dividends, or profit-sharing. *(p. 39)*

Finally, McCracken, Carli and Co. give their wholehearted endorsement to the most extreme elements of Jimmy Carter's homespun Schachtianism: the energy and environment programs. "Full use (should) be made of the market mechanism," the authors say, to "provide a firm long-term perspective for energy prices," presumably by jacking them up as Carter wants. "Additional measures may be required," the authors say, "to improve efficiency in energy consumption," presumably by mandatory conservation. Further, "we support policy instruments, which rely on the price mechanism, to make 'polluters pay,' " as American industry already has, through the nose. They add coyly, "In some cases, however, an element of direct regulation may be unavoidable."

But the OECD report does not merely want Schachtianism "autarky" to the 24 nations of the OECD and beyond. Under their heading, "The International Dimension," the McCracken-Carli group demands a distribution of world trade that will not overstress the credit structures of the countries that have already been brought to the brink of collapse, and place a correspondingly greater burden on the economies of Japan, West Germany, and the United States. The single international criterion is what the international banks will accept! Given "an increased role for private financial markets (i.e. the group's patron, the Rockefeller family) in the provision of international liquidity," consequently "it is a matter of some urgency that a greater share of the oil deficit be borne by countries whose external credit-worthiness is intact." The danger is that "some countries have run up debt so massively in recent years that their external credit-worthiness may now be becoming exhausted."

All this must be managed from the top, the authors conclude in their final paragraphs:

> This emphasizes again the need for closer consultation and better co-ordination of demand management policies...the degree to which the world price level as a whole has become sensitive to fluctuations in demand, and the rapidity with which loss of confidence affecting investment, inventories and consumers' behavior seems to spread out from country to country, underline the fact that close international cooperation is an essential ingredient of a program directed towards getting back to full employment and price stability. *(p. 52)*

Fluctuations in demand? There is an obvious fraud in the formulation: the report bears almost no mention of the relationship between the OECD countries and the Third World, and no mention at all of East-West trade, the two leading areas of export expansion. "We cannot claim to have dealt adequately with the problems of the less-developed countries," the authors admit, but there is no mention of the latter channel of trade whatsoever. Up until the industrial collapse two years ago these were the fastest-growing parts of international trade, the clear domain of world economic expansion as a whole. Except for a few passing references to the mass of debt, the OECD report takes as a given condition the strangulation of international trade and development efforts under the rule of the Eurodollar market. Since the international debt structure has prevented the world economy from expanding through the development of its backward sectors, and slowed the expansion of East-West economic cooperation, the debt structures themselves are about to

collapse.

To alleviate this collapse the authors propose to turn the crisis back against the advanced-sector economies themselves; the thinking is identical (but less honest) than the similar demands by Federal Reserve chairman Arthur Burns, and Assistant Secretary of Treasury C. Fred Bergsten, for massive cuts in U.S. energy consumption to ease the strain of the U.S. payments deficit.

Since the McCracken-Carli study contains layer on layer of deception that must be stripped away before it becomes intelligible, it is fair to insist that there is an element crucial to their proposal that they have failed to mention altogether. This is the sine qua non of Hjalmar Schacht's system, arms production. Not the economists, but their employer, Nelson Rockefeller, is trying to steer the NATO countries towards a medium-term buildup of armaments with a perspective of confronting the Soviet Union sometime around 1980. There is no coincidence in the simultaneous emergence of the OECD report, and President Carter's first signals in favor of building the B-1 bomber on which U.S. conservatives place so many false hopes. Nothing intrinsic to the OECD report proves this allegation (see The Spirit of Camp Pocantico, *EIR* Volume IV No. 24). But it does explain two anomalies that stand out like flashing red lights. One is the inadvertently-betrayed expectation of hyperinflation, to be cured through indexation. The authors clearly expect their "budgetary targets" and the "difference between private savings and private domestic investment" to be huge.

The second, the one the *Financial Times* complained of, is the assumed 5.5 percent growth rate potential. This figure is plucked out of thin air, as the editors say, "a ghost in the machine." But if Paul McCracken, Guido Carli, and Robert Marjolin are not merely gibbering, but have a thought-out reason for making such a projection, they are projecting 5.5 percent growth to occur on the same basis that Schacht achieved high "growth" in Germany between 1933 and 1937. The "ghost in the machine" the *Financial Times* fears speaks fluent German.

— David Goldman

Inflation Vs. Illiquidity

BUSINESS OUTLOOK

While the bulk of the bank and investment house market letters are painting a rosy picture of the U.S. economy — bubbling over about the favorable technical conditions in the money markets, the coming boom in business spending, and so forth — insiders at the same institutions are operating on the basis of an entirely different set of economic expectations. The insiders' view does leak out into the public from time to time — for example, in *New York Times'* Leonard Silk's column June 23. Silk there promoted the views of Harvard Professor Daniel Bell, one of the authors of the "quality of life" Triple Revolution doctrine. Bell, says Silk, finds "striking parallels" between today and the 1920s and 30s, and says that today's insoluble crisis is inflation. Bell then asks blithely whether democracy has a future.

The inflation specter was also high on the agenda of a recent private meeting of government and private sector financial leaders, where the use of interest rate manipulations for psychological effect was freely discussed.

But the scope of this insiders' meeting was much broader. After admitting that the LDC debt situation was a "difficult" one, the attendees hammered out a strategy of getting the U.S. government, not the banks, to underwrite the risks of the upcoming debt rollovers and of manipulating upward commodity prices — on the model of coffee — to support debt repayments. Part of the international strategy involves mixing the straight refinancing with loans for some Third World "development" projects, both to attract the capital of regional and other conservative bankers and to provide the countries with some means of earning foreign exchange to repay their debts.

On the domestic side, the program is energy conservation and austerity — specifically the elimination of "cost of living clause-induced inflation." Energy "development" e.g., coal gasification, which according to sources at the Washington Federal Reserve is Fed chief Arthur Burns' latest all-consuming interest — will be thrown out as the capital formation bone.

Inflation vs. Illiquidity

But anyone who looks beyond the barrage of government economic statistics every month fully appreciates the Silk-Bell 1930s analog. The U.S. economy is caught in a bind, where it faces either inflation, on the one hand, or illiquidity, on the other. In May the rise in consumer prices slowed to a 7.2 percent annual pace. The slowing of both industrial and now food prices, however, threatens to plunge both of those sectors into bankruptcy. The big change in consumer prices last month came in the break in food prices. Fresh vegatable prices dropped 13.5 percent, while supermarket prices of fresh fruits, eggs, and beef also fell. The threat that wheat prices might go through the ceiling is over; wheat prices fell below government support price levels last week on the news of the harvesting of an unusually large and rich wheat crop. However, the other side to this good news is the fact that a record harvest, taken together with the drop in grain exports, threatens the heavily indebted farm sector — and its regional banks creditors — with extreme illiquidity.

The rise in industrial prices has been slowing down since early March. Between last October and early March, the Bureau of Labor Statistics index of 13 industrial materials prices rose 11.6 percent; but early March through mid-May the index was flat, and in the last four weeks it has lost 4.9 percent. The *Journal of*