

International banking lending: will it shut down?

A featured OpEd piece in the London *Financial Times* of May 30 purports to analyze what the effect on the international lending markets of the expected OPEC price increase will be, citing OECD estimates of a \$45 billion current account deficit for the developing countries during 1979. The *Financial Times's* conclusion is that while the international markets will not collapse under the strain—a prospect the article moots—banks will operate under compulsion from the American Federal Reserve, the Bank of England, the Bank for

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International Settlements in Basel, and the International Monetary Fund as the “arbiter of the terms of credit.” Either stronger supervision, per the proposal of Bank of England Governor Gordon Richardson, or straight reserve requirements on the Eurodollar deposits of the international banks will force bankers to move their LDC loans “onshore” and impose much tougher terms.

In fact, the scenario circulating in London reflects less what must necessarily happen than what the official agencies cited by the *Financial Times* want to see happen. As *Executive Intelligence Review* reported last week, the brunt of the American government proposal to slap reserve requirements in the 15-20 percent range on Eurodollar deposits is fear that the Western Europeans and Japanese will run off with international lending, as they have done during the first four months of 1979.

A type of fake objectivity has muddled the actual state of international credit flows, as witness the *New York Times's* May 29 discussion of the alleged reflow of Eurodollars back to the United States. According to the *Times*, the \$4 billion net reduction in U.S. banks' claims on their Euromarket subsidiaries indicates that the gigantic flow of funds back into the dollar—measured by the \$17 billion net reduction in dollar obligations held by foreign central banks during the dollar's boom days, January through April—has in

large part gone to American banks, and the Eurodollar market is coming back “onshore.”

The *Times* is, in fact, in substantial error; most of the dollars that flowed out of foreign central banks' portfolios (and flowed out of the central banks' main investment vehicle, the government debt of the United States) went into European and Japanese commercial banks, and thence to the developing sector in the form of syndicated loans. That is the main incentive for the State Department and Treasury's sudden insistence on imposing Eurodollar reserve requirements: the stated objective, as published by this service, is to wipe the Europeans and Japanese out of the lending markets. Their central bank-commercial bank collaboration accounts for the fact, which the *Financial Times* discussion found strange, that the international “borrowers” market for LDC lending has persisted despite the last and the current round of oil price increases.

American commercial banks purport to find inexplicable the willingness of the European and Japanese banks to make loans at spreads of one-half of one percent and even less, which barely cover administrative expenses. The answer has been in the headlines of the European press for several months: the foreign banks are sacrificing temporary profitability in order to maintain customer relationships with nations whose credit standing will zoom once the European Monetary Fund comes into effect. Since the American commercial banks despair of their Administration giving them access to the new European development financing facility, they have tended to line up with the Bank of England-Federal Reserve combination for shutting the Europeans and Japanese out. (Technically, G. Gordon Richardson and G.W. Miller have different proposals for rigging the Eurocurrency markets, but the intention of both proposals is the same).

The market development which most dramatically shows up the silliness of the financial forecasts associated with Miller and Richardson is the spectacular rise in the price of gold, whose price is now at \$278. If the constriction of the Eurodollar market and the

movement of dollars back onshore is so imminent, why has gold had its most striking price advance this year? The argument that what is occurring is a disorderly rush out of all currencies is stale and wrong. The leading European institutions and their Arab customers have a deal to put the price up as part of the new reserve basis of the European Monetary System. In part, the rise in the imputed reserve-price of gold to \$300 an ounce or thereabouts from the previously agreed figure of \$230 to \$240 compensates Europe for the rise in oil prices; the Arabs are becoming major gold holders and lose little on this basis. The only major loser is the United States.

The success or failure of these monetary arrangements depends strictly on the outcome of the Franco-Japanese plan to replace the oil multinationals with a system of multilateral oil-for-technology exchanges, which the Saudis and Mexicans have both proposed through a number of media. One European banker

expressed it this way: "By all rights the French securities markets should have collapsed, because France is now paying more for oil than it can afford. However, the institutions have faith in the French government's policy of promoting capital formation and expect to profit in the medium-run. The rise in the oil price as such can be dealt with; what must be avoided at all costs is a shock to supply."

In sum, the United States stands to lose both oil and money. What the European governments have not yet answered is the question, what happens if they succeed? If their oil and monetary package goes through at the expense of the United States—without winning the United States to their policy—the world monetary system will still be subject to continual destabilization.

—David Goldman

'Facing up to the reality of the world oil crisis'

The following is excerpted from a London Financial Times article of May 30, entitled "Finance for the Second Wave of the World Oil Crisis," by Nicholas Colchester and John Evans.

... The recent appearance of the international capital markets could scarcely have been predicted four years earlier. The funds have been coming out of the industrialized nations to be re-lent via the international banks to the developing nations. In a borrowers' market the developing nations have been borrowing more than they strictly need to finance their reduced current account deficits. It was, and so far remains, a "borrowers' market." This is ...partly because a growing throng of international banks emerged ready and eager to intermeditate in the flow of funds.

At a moment when the pace of increase in oil price is causing alarm and surprise it is natural that bank analysts are again focusing on the extra funds which OPEC will have at its disposal and the extra needs for funds which will be created in the less developed countries which have no oil. The question is whether

the international banks, which have now emerged as the main channel through which balance of payments financing takes place, will be allowed, able or willing, to repeat their post-1973 performance.

... This time around, according to Morgan Guaranty, the current account deficits of the non-OPEC developing countries should deteriorate by some \$7.5 billion to an estimated \$35 billion—roughly half the rise being due to the oil price. ...In terms of indebtedness the recent rise in the debt of developing countries has been very marked, partly because they have been taking advantage of the market to build up reserves. ... It is clear, too, that private banks are now the mainstay of this accumulated debt. They account for 50 percent of all LDC risk against 36 percent five years ago. ...

It is an irony that a new campaign which is building up to apply some sort of uniform controls to Eurocurrency market lending should coincide with the moment when the need for Eurodollar recycling may suddenly increase. ... The new emphasis on prudence in international lending may also raise the importance of the International Monetary Fund as an arbiter of credit worthiness. ... The hope now is that an increased emphasis on banking prudence rather than a crisis will see to it that funds are provided to the developing world in a way which faces up to reality.