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End of recovery myth threatens U. S. position

by David Goldman

The Western nations' chief economics body, the Paris-based Organization for Economic Cooperation and Development (OECD), has threatened President Reagan with economic disaster should he refuse to cut the American government's budget. The OECD's demand, repeated in public statements by leading European Social Democrats during mid-January, is equivalent to unilateral U.S. disarmament. The same demand has been repeated since February of last year by International Monetary Fund managing director Jacques de Larosière, and since July 1982 by Bank for International Settlements President Fritz Leutwiler. However, the OECD report does more than demand American defense budget cuts; it reports, with some accuracy, on the means by which the economic ground may be blown out from under U.S. government finances.

The OECD report on the United States economy says that the supposed American recovery will be "short-lived," that the U.S. dollar will fall by about 20 percent, that inflation will rise by at least another 4 percent, and the stock market will collapse—wiping out roughly $500 billion in paper wealth of American households—if President Reagan fails to cut the budget deficit.

Ill-motivated as the OECD report may be, the unpleasant reality is that it does not go far enough. As *EIR* documented exhaustively in our October Quarterly Economic Report, the Federal Reserve invented the industrial-production recovery out of thin air (raw data for physical production show a marginal decline of the real economy during 1983), while the Bureau of Labor Statistics faked inflation data to show better price results. It is not a matter of whether an existing "recovery" will fail, but rather that an economy that has been dead in the water for a year will return to the rate of decline seen during 1982.

Political disaster for Reagan

The implications for President Reagan are drawn from the OECD report in a London *Financial Times* editorial of Jan. 16, which argues:

"One of the many ironies about the current recovery in the U.S. economy is that worldwide disapproval of the principles behind President Ronald Reagan's economic policies has grown in direct proportion to the success of these policies in practice. The survey of the U.S. economy published [Jan. 15] by the Organization for Economic Cooperation and Development is the latest example of this apparent paradox. . . a sustained critique of President Reagan's central policy failure, which 'bodes ill' for the medium-term future of the U.S. and the world as a whole.

"This failure is, of course, the U.S. government's inability to control its budget deficits. But the OECD is no more able than President Reagan's numerous other critics to identify specific penalties which he will face in the near future if his present policies are maintained. The overvaluation of the dollar 'may appear compatible with a sustainable balance of payments position'; high real interest rates may lead to a 'marked deceleration in house building'; a rise in personal savings may weaken consumption. In general the recovery may prove 'shorter-lived' and more 'modest' than the normal experience. But this is hardly the stuff of a supremely confident politician's election-year nightmares. . . .

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"The question which critics of Reaganomics should be asking more forcefully is what happens when market sentiment turns? A fall of 20 percent in the dollar would raise prices by 3 to 4 percent, the OECD estimates. Household wealth has increased by $500 billion or 23 percent of disposable incomes, as a result of the boom in the stock market between mid-1982 and mid-1983, the OECD mentions at another point in its report. What would happen to consumer spending if this windfall were to melt away as a result of waning confidence in Wall Street. . . .

"The latest news of slackening retail sales and money supply growth may even suggest that the long-awaited decline of the dollar and Wall Street is about to begin. But persistent critics of Reaganomics have lost too much money and prestige on such expectations already—for the moment they may be safer to blame the modest setbacks not on the deficits but on December's frigid weather."

Supposedly, the budget deficit, now estimated at $200 billion plus an additional $100 billion of "off-budget" financing, is the source of high interest rates which will abort the American recovery. The opposite is the case: Fed chairman Paul Volcker's high interest rates caused the budget deficit, creating a self-feeding spiral of Federal red ink. Not only does the OECD, a supranational institution staffed by the British Foreign Office, avoid attacking Volcker; it endorses Volcker's demand that Reagan throw out his defense budget.

Soviet assets attack U.S.

To the extent that the neutralist content of the OECD report were obscure, a barrage of attacks against the President from European Social Democrats made the point unmistakable the week of Jan. 16. Former West German Chancellor Helmut Schmidt, now a Soviet submarine in West German politics, warned at a Georgetown University meeting in Brussels Jan. 16 that "egoistic economic policies" pursued by Washington would wreck the Atlantic Alliance.

Schmidt said, "The economic mess today is a greater danger right now to the coherence and political stability of the alliance than the Soviet threat." He accused the Reagan administration of bringing about "the highest interest rates since the birth of Christ," blaming it all on the budget deficit.

Schmidt did not mention that the Soviet Union, with at least $30 billion worth of speculative dollar purchases in the last two months, was one of the major factors driving the dollar up—and may be the principal trigger for a dollar crash early in 1984.

Arguing for American defense budget cuts as a means of reducing interest rates on behalf of the Atlantic Alliance makes Schmidt's argument ring hollow. Arthur Burns, American ambassador to West Germany, more frank in private discussions, suggests that since Europe will be pushed into "neutrality" in any event, the defense cuts should take the form of reduction of American troop strength in West Germany!

French President Mitterrand's finance minister Jacques Delors joined in the exercise over the weekend. He said that over the course of the past year over $150 billion in Western European capital has fled to the United States (probably a gross overestimate), in a speech to a group of Socialists in Paris Jan. 14.

Delors said: "If the speculative illness of the dollar continues, shouldn't Europe take measures to hinder the flight out of the European currency?" Delors did not specify what measures Europe might take to stop the outflow of capital. He went on to propose "a new issue of SDRs by the IMF because there is a lack of international liquidity."

Delors' point is identical to the OECD's: The supposed U.S. recovery is based on gouging Latin American and European economies, i.e., a total of about $200 billion in capital inflows since Volcker's "Columbus Day Massacre" in October 1979.

However, these polemicists fail to mention that Volcker's Dracula-like policy of sucking up flight capital from the rest of the world was coordinated through the International Monetary Fund, the institution which they want to "cure" the problem. Once again, International Monetary Fund "surveillance" (supranational dictation of economic policy), a favorite plan of Delors, was offered as a solution to the mess, this time by Italy's central bank governor Lamberto Dini in a New York speech last week.

Swiss promote dollar crash

The OECD's conclusion concerning the imminent problems of the American dollar on foreign exchange markets is now popular in Swiss banking circles. The *Neue Zürcher Zeitung,* the Swiss Nazi bankers' leading daily paper, suggested Jan. 9 that "central bankers are concerned that the sharp rise of the dollar might be followed by an equally rapid and marked fall of the dollar." In sequence, the *New York Times* of Jan. 13 quoted Swiss banker Hans Mast warning, "The faster the dollar goes up, the more we fear a destabilizing collapse."

This apparently was the main subject of the meeting of central bankers at the Bank for International Settlements the weekend of Jan. 14. West German central banker Karl-Otto Poehl emerged from the meeting to warn that the dollar must go down, and it would be a pity if it went down too fast.

Well-placed New York banking sources point out that the vast majority of big European money has already moved into the dollar, and the last runup of the dollar represents a stampede of suckers attempting to get out of German marks and other European currencies. Once the Soviets cover their long dollar position, i.e., sell off the hoard of $30 billion or more that they have accumulated, and the Swiss and British join in the bash, the dollar will collapse, forcing up U.S. domestic interest rates and generating chaos in U.S. bond markets.

Although President Reagan has resisted the blandishments of the European decouplers as well as their friends in the United States, a dollar crash will present him with the choice of cutting the budget to "preserve financial order," namely, accepting IMF controls over the U.S. economy, or declaring war-emergency measures.