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When will the big money exodus begin?

Treasury Secretary James Baker III's "drop dead" to Japanese Finance Minister Miyazawa endangers money inflows.

Speculation that Japanese Finance Minister Miyazawa's emergency trip to Washington Jan. 21 might produce some temporary agreement to support the dollar evaporated, and the U.S. dollar headed back toward the Carter administration low point in what dealers described as "panic selling" Jan. 22.

That leaves Japan little choice but to negotiate with Washington in a way Washington understands. Since the President is fixated upon the Dow-Jones index of the New York Stock Exchange, the one message the Japanese can deliver that the White House might appreciate, is to cut off new money into American securities markets. Since Japan invests over $50 billion per annum in U.S. securities, using the proceeds of its global trade surplus, such action might command Washington's undivided attention.

Financial sources in Tokyo suggest that the appropriate timing for such action might well be the February auction of U.S. Treasury securities.

Last Oct. 31, the Nakasone government bent over backwards to support American securities markets and the dollar. As Tokyo sources explained this to *EIR* at the time, Prime Minister Yasuhiro Nakasone hoped, in vain, that funding the administration's Potemkin village recovery would help the Republican Party's election chances.

The public face of this support program emerged in the so-called "Baker-Miyazawa" deal, which in effect set a target rate for the yen/dollar parity at 165 yen. Now that the yen is trading at 152, and the U.S. Treasury has leaked a target of 140 yen to the dollar, the Japanese support program has been repudiated, in favor of outright competitive devaluation.

It appears that the sorcerer's apprentices of the Reagan administration are likely to succeed beyond their wildest dreams, and trigger a dollar collapse that will shake out the American debt pyramid (see page 4).

On Jan. 18, doomsayer Stephen Marris, the former chief economist at the Paris headquarters of the Organization for Economic Cooperation and Development, warned that the current collapse of the dollar will lead to a world recession. Marris now augurs at the Washington-based Institute of International Economics. He gave the warning in an interview with West German television (Channel 1) the night of Jan. 22. As he explained, the dive of the dollar value would lead to an exodus of foreign investments, which would "force" the U.S. Federal Reserve to increase the interest rates to keep the money in the States. This would accelerate the process of world recession.

The Jan. 18 *Washington Post* cited Richard Reid of London's Phillips & Drew brokerage firm, who says: "I have a horrible feeling there is a considerable downside to the dollar." Reid and others say sooner or later the United States will be forced to take strong action to defend its currency—which could well include raising interest rates or taxes sharply. They say a recession in the United States would trigger a "worldwide recession" that "would put serious strains on financial institutions whose borrowers might not have the cash coming in to keep up payments on their loans."

The United States, the world's largest net debtor, is in danger of a mass exodus of foreign capital, leading to a drastic rise in interest rates, and a collapse of all securities markets (not to mention real estate). That is why Federal Reserve chairman Paul Volcker, who has long warned of the potential for such a disaster, is reportedly aghast at the Treasury's handling of the current mess.

None of this appears to square with the spectacular increase of the Dow-Jones industrial average during the past two weeks, coincident with the dollar's sharp fall, and heavy liquidation of U.S. securities by foreign investors.

Historians will recall, however, a similar phenomenon during the weeks leading to the Oct. 22, 1929 market crash. During September and October, foreign investors, especially the British, liquidated heavily. The large American commercial banks bought what they liquidated, and then some, in an effort to keep the bubble going. By the time the banks' effort collapsed, under the weight of combined Bank of England-Federal Reserve efforts to "dampen speculation," the American banks had dug themselves into a fundamentally worse position, through the preceding eight weeks' of market support operations.

Since the Dow-Jones average has bedazzled the President, who has followed like a man chasing a will-o'-the wisp into quicksand, what better alternative for Tokyo than to send it crashing down?

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