

## EIR Economics

# James Baker goes to war against Germany and Japan

by Chris White

As he had promised, U.S. Treasury Secretary James Baker took the occasion of the annual meeting of the International Monetary Fund (IMF) at the end of September, to propose a broadening of the economic indicators employed by the Group of 7 industrialized countries in the coordination of financial policy. It is a thinly veiled declaration of war against the economies of West Germany and Japan.

Baker seems now to be shifting his own policy closer to that identified with the lobby for the Basel-based Bank for International Settlements in the United States—typified by aging guru Robert Mundell of Columbia University, and aspiring politicians Bill Bradley, the Democratic former basketball player, and Jack Kemp, the Republican former quarterback. That same Bank for International Settlements has, since the spring of 1985, promoted ways to bring the Comecon economies into the European Monetary System. Baker is now acting on behalf of that broader policy objective.

Baker proposed that the indicators employed by the Group of Seven be broadened to include a “basket of commodities,” such that international decisions on whether to raise or lower interest rates could be based on the price movements of those selected commodities. Higher prices would require higher interest rates, lower prices, lower interest rates. Among the commodities included in the index would be gold.

Apparently the plan presented was worked out in coordination with the British Chancellor of the Exchequer, Nigel Lawson, who alluded to a similar outline in his speech to the IMF. And the French minister, Eduard Balladur, has been quoted in press accounts, welcoming the proposal. The French are, like Kemp and Mundell, supposed to welcome the decision to include gold within the basket of commodities. The latter pair assert that the decision to include gold in the cited basket of commodities reflects movement back toward the discipline of the gold standard for the dollar, abandoned in favor of floating exchange rates by John Connally, George Shultz, and Paul Volcker in the period between 1971 and 1973.

The same proposal will increase the desperation quotient in Tokyo and Bonn.

The press outlet for this BIS gold standard lobby in the United States is often led by Lindsay Clark’s *Wall Street Journal*. On the eve of the IMF meeting, the *Journal* editorialized: “The IMF could do an enormous service, for example, simply by compiling and publishing a purchasing-power-parity index—an index of whether exchange rates reflect the same purchasing power in different currencies. . . . Just knowing what similar goods cost in different countries would throw light on the problem of floating exchange rates and a volatile dollar. It would at least give us an image of where exchange rates ought to be if we want an efficient international price mechanism and calmer financial markets.”

Calmness will probably be in extremely short supply if the proposed index is actually used for those purposes. The very floating of the proposal is sufficient to establish that when Baker told the Group of Seven that the United States continues to support the so-called “Louvre Accords” of last spring, the agreements under which the dollar’s descent has been cushioned, by Central Bank intervention, against the deutschemark and the Japanese yen, he wasn’t being truthful. Nor would the adoption of such an approach be welcome to the Third World economies, looted with increasing viciousness under the so-called “Baker Plan” for dealing with the debt crisis.

The reason is that the dollar remains vastly overvalued relative to the currencies of especially West Germany and Japan.

*EIR* applied some version of the standard Baker and others are now discussing to the internal purchasing power of the U.S. dollar and deutschemark in early 1985, back when the dollar was valued at more than DM 3.00 on exchange markets. Back then, one dollar in a U.S. supermarket bought roughly what one deutschemark bought in a comparable German store. Since then, both the U.S. and German economies

have continued to slide downward, with the U.S. economy declining faster. By Baker's touted standard, the dollar ought to be at parity with the deutschemark. In Britain, it is the reverse. There, the pound is as much overvalued relative to the dollar as the dollar is overvalued relative to the deutschemark.

The magnitude by which the dollar would still have to fall to come to so-called purchasing-power-parity with West Germany and Japan is sufficient to bring down everything. It's what Paul Volcker used to warn against, as "a hard landing for the dollar."

So much for maintaining the stability of the so-called Louvre Accords. Perhaps, then, Baker is simply trying to up the ante on the Germans and Japanese, who have consistently refused to do what the U.S. monetary policy team calls "adopting expansionist policies," by threatening to pull the proverbial plug. These demands were restated at the IMF conference by Baker, and by President Reagan. Since the U.S. dollar depends on maintaining an inflow of funds from especially the surplus nations of Germany and Japan, the differential between U.S. interest rates and those of the two other countries has to be sufficient to keep the funds coming. Since increasing interest rates in the United States is likely to have dramatic consequences, such as the collapse of whole sections of the banking system, Germany and Japan have been under pressure to lower their interest rates instead.

This demand to self-destruct was rejected by both during the ongoing proceedings. Japanese increases in internal rates show rather what Japan will do, than anything Baker and company might intend. But behind all that maneuvering, which itself may jeopardize the dollar system, and its banks, is something else.

### **The bubble-popping policy**

It has been the policy of the financial high-flyers associated with the BIS to bring about a deflation of the bubble associated with the dollar credit system. The purchasing-power-parity index of Baker and the *Wall Street Journal*, whether they know it or not, is a reflection of that BIS bubble-popping policy.

Adopted, apparently, during the monthly BIS meeting at the beginning of August, the BIS deflationary policy has shown up in the shake-outs of stock markets around the world which ensued from the changes in credit policy adopted by central banks, pursuant to that policy. First, the Bank of England increased rates, and the London stock market fell. Then the Italian central bank did the same, and the bourse in Milan fell. The proposal under discussion stems from the same intent.

Beyond that, tying interest rate and credit policies to the price movements of selected raw materials, would tie interest rate and credit policy to the decisions of the oil, raw-material, and food cartels who determine how prices will in any case

be rigged. These are the same financial forces who have promoted the agreements with the Russians which the President espouses, prompted by his wife's desire to go down in history. Reagan's desire has become the means by which these financial circles hope to realize various of their longer-term plans.

Baker might delude himself with the prescriptions of contemporary financial thinking, that he is actually fighting to save the dollar system, by blackmailing Germany and Japan with the prospect of what has been called a "hard landing" for the dollar, into continuing to provide the funds which have supported the continuation of the present insane U.S. policies.

Instead he is acting to ensure that, out of political confrontation with Germany and Japan, an altogether different agenda is actually implemented, the deflationary policy adopted by the BIS during early August. Before the meeting, Japan signaled in no uncertain terms that there is a limit to how far Japan can be pushed in its monetary policy. The signal was the decision to increase interest rates, announced on the eve of the gathering. The increase is, of course, the very reverse of everything the United States has demanded for more than the last year, and establishes that Japan will not go along with what the United States demands, beyond a certain point.

While not so dramatic, West Germany has allowed certain secondary interest rates to rise, demands. German political leaders have made clear repeatedly that their country cannot accept the political consequences of what the United States is demanding.

It's not possible to say just where the line might be drawn. However, it's well-known that, apart from the laundered proceeds of the world drug trade, Japan is the largest source of the funds that have let the U.S. government and its banking system stay afloat. Baker is helping to create the conditions in which the BIS deflation policy is implemented via the pullout of those funds.

It is only the Russians who can benefit from the continuance of this kind of nonsense in the name of economic policy. Except, of course, for the circumstance, that like the Gramm-Rudman "fix" Baker is said to have insisted the President support, the kind of package threatened in Baker's proposals to the IMF, will itself help to accelerate the pace of the crisis Baker and his friends are otherwise so desperately trying to delay. There could be some good in that. Perhaps under the approaching crisis that Baker and his friends are unleashing, it will be possible to do the kinds of things required to restore stability to the world financial system, and health to the economy.

Otherwise, what Baker is really proposing makes nonsense of all the platitudinous utterances about "cooperation" and "stability" that can be heard between the decadent receptions and buffets.