Bush's new 'strong' dollar: the same old insanity

by Richard Freeman

George Bush and company have been imitating the economic policies of the first two years of the first Reagan administration. Part of the purpose of this is to create a short-lived appearance of calm in the dollar sector, the better to sell a traitorous arms control deal with the Russians. The whole world is once again expected to bail out the U.S. Bush administration. Such efforts cannot long be successful.

To further this goal, Bush's administration, together with Alan Greenspan's Federal Reserve, have initiated interest rate increases worldwide. The soaring dollar is a calculated feature of this policy. It works as follows: Fed chairman and former Morgan Guaranty board member Alan Greenspan—a student of Ayn Rand, who herself was a devotee of Friedrich Nietzsche—and Treasury Secretary Nicholas Brady have attempted to return to the strong dollar policy used by Treasury Secretary Donald Regan during the first half of the first Reagan administration. The aims of this policy are:

1) to loot the rest of the world, increasing the level of debt service drained from the Third World, as well as buying imported products cheaper, because of the exchange rate differential (this exposes U.S. trade war measures, accusing other countries of "unfair" practices, as total hypocrisy);

2) to artificially buoy the stock market, with the Dow Jones Index rising from 2,240 on March 23 to 2,517 on June 2, a surge of 12%;

3) to bring in funds to finance the U.S. budget deficit, not only the on-budget items, but the off-budget items as well, especially housing. The fact that Freddie Mac, the quasi-governmental, quasi-private U.S. secondary housing market mortgage purchaser, was allowed to go public on the stock market in a little-publicized move in December 1988, is part of this operation. The ultimate consequences for the economy can be nothing but disaster.

In response, the British have also raised interest rates. On May 24, the Bank of England raised the discount rate a full percentage point to an amazing 14%. (The economy is Prime Minister Margaret Thatcher's Achilles heel, largely of her own creating.) The German Bundesbank, the Bank of Japan, and the Banque de France have had to respond to this increase by raising their rates, to prevent the loss of funds in the form of flight capital. Reports in the media, including the London financial press, that the Germans have initiated the interest rate increases, are wrong and as far as can be determined, sheer propaganda. For example, on Jan. 29, the interest rate on three-month U.S. Treasury bills trading in London was 7%; the respective rate was 4.2% for Japanese treasuries and a little above 3% for German treasuries. By mid-May, thanks to Greenspan, the U.S. rate for the same security had been twisted up more than 200 basis points to above 9%. The Japanese had to raise their rate to 5%, and the German rate was pulled up to over 6%. The rates softened a little in the last two weeks of May.

The Federal Reserve began hiking the federal funds rate—the rate of interbank borrowed funds which the Federal Reserve influences—in late February. This reversed the Dow Jones stock average which had taken several weeks of a nasty fall starting in mid-February, as a nervous Bush, in office all of one month, looked on. The timing is exact. Bush also needed a re-invigoration of the *appearance* of the Potemkin Village "recovery," as background to complete the next phase of sellout negotiations with the Russians. In reality, the real economy collapsed further in the intervening period since the start of 1989, as even the rise in the heavily faked U.S. unemployment figures show.

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Greenspan's psychosis

Before developing each of the three major features of the Bush-Greenspan-Brady "high interest rate, strong dollar" policy, two points are in order.

First, it should be evident that the United States is playing with fire. The U.S. prime rate is already 11.50%, about four times the rate it should be. The Federal Reserve-directed federal funds rate is trading at 9¾-10%. The size of the bubble of debt and speculative instruments in the U.S. alone is *$18.3 trillion,* according to calculations made by *EIR* using Morgan Guaranty, Salomon Brothers, and Federal Reserve Board statistics. The bubble will explode if rates tighten. The growth of the U.S. paper economy continues at a dizzying pace.

For example, in March, credit card debt grew by a staggering $4.3 billion, and for the first quarter of 1989, credit card debt grew by $8.1 billion—the highest level in a decade. Plus, as other OECD nations raise rates to compete with the United States, they generate in turn their own internal debt bubbles.

Second, what little remains of the real physical economy is being wiped out. For example, despite $1,000-2,000 dealer rebates and financing ranging as low as 5.9% down to 0%, car sales in mid-May slipped to 6.8 million from 7.4 million earlier in the month. This is two-thirds the level of car sales in 1979, and significantly down from last year. New durable goods orders, which have been climbing steadily for the last four months, and which are cited by all the economic pundits as a sure sign of the overheated economy, are at $129.1 billion in April, *below* the level they were at in December. Capacity utilization figures are up, but only because there is much less capacity. In 1988, the U.S. steel industry produced 99.6 million tons of raw steel. Against the 1988 rated level of steel capacity of 112 million tons, this registered a seemingly impressive 89% capacity utilization rate. But the U.S. steel industry has dynamited or otherwise destroyed 48 million tons of capacity since 1977! Had the U.S. not destroyed or else modernized that needed 1977 capacity level of 160 million tons, the 1988 capacity utilization rate would only be 62%.

Georgios Bush Rex

Like Czar Mikhail Gorbachov of Russia, George Bush would like to ride a wave of adulation, created by his supposed achievements. Hence the three features of the "high interest rate, strong dollar" policy. In reality, the policy is a cheap imitation of Donald Regan's of eight years ago, which merely continued the Jimmy Carter-Paul Volcker depression.

We examine each of the three features cited above.

1) There are two means by which the strong dollar loots the rest of the world. First, by adding to the interest debt charges that drain the Third World of capital, as well as by attracting flight capital from nations all over the globe. Second, it makes the cost of imports cheaper, providing the United States with other countries' real physical goods. It is estimated that for each percentage point increase in American interest rates, the Third World makes an extra $5-6 billion in interest payments per year, with Ibero-America paying $3 billion. The higher dollar brings in funds from every country. According to Nomura Research Institute economist Mark Cliffe, Japan put $10 billion into foreign bonds in April, most of that in dollars. They also bid heavily at the $28 billion U.S. Treasury bond auction in early May. "Investors want to take their money out of Tokyo and put it in the U.S.," says Takenori Kato, the foreign exchange chief in Japan for America's Continental Bank. "Demand for dollars is tremendous" stated Liliana Nealon, a Union Bank of Switzerland vice president. The dollar stands at 1.98 deutschemarks and 143 yen.

The stronger dollar will allow the U.S. to steal more from the Third World. For example, in 1982, the Mexican peso traded at 40 to the dollar. The floating peso today is 2,460 to the dollar. Mexico must sell many more physical goods to the United States to earn the same amount in dollars. The U.S. hopes it can mask its import-dependency by cheapening the cost of imports. It won't work. In the first three months of 1989, U.S. capital goods exports, adjusted for inflation, actually fell. As the rising dollar makes U.S. exports more and more expensive in six to eight months, the trade gap will widen, sending Bush to certain ruin.

2) The rising dollar makes foreign investments in dollar-denominated stocks appreciate in value, even if the individual stock doesn't rise in price. This offsets the fear of buying stocks on margin, with borrowed money, because of the higher interest rates. This opened the way for foreign money to help artificially "bull" the stock market by 12% in the last 10 weeks. *Business Week* magazine underscored the trend with an article in its May 22 edition, "Europe's Smart Money Heads Back to Wall Street." Billions of dollars have crossed the Atlantic. For the first time in at least two years, a "window of opportunity" to buy American stocks appeared, said Walter Temperli of Vontobel and Co. Bank of Zurich, Switzerland. Temperli thinks the Dow Jones Industrial Average will advance to 2,600 by the summer.

3) Higher rates offered on U.S. Treasury bills and bonds, attracting funds from around the world, relieved the anxiety, temporarily, with which the United States entered each Treasury auction up until February of this year. This provided a seemingly smooth background against which Bush could conduct arms deals with the Russians. It also covered for one of the more remarkable Ponzi schemes in history.

And, now? The dollar has been run up, the stock market artificially re-inflated, all by means of policies whose consequences mean the destruction of the allies who support them. The means adopted have thereby increased the instabilities in the financial and economic system, and those instabilities will, sooner or later, surface with a vengeance, as they did between August and October of 1987.