deutschemark rate within the broader European currency group and about domestic inflation. They are entirely unconcerned about the dollar rate. There are no indications that Carter's advisors appreciate this point; however, the New York Federal Reserve, among others, does.

The Bundesbank now assumes that the inflationary effect of dollar inflows is limited by the depreciation of the dollar. Against West Germany's current-account surplus of DM 14 billion last year, which reflects an even larger volume of currency inflows, the Bundesbank was able to write down the value of its foreign exchange holdings by DM 6.16 billion, due to the 11 per cent depreciation of the dollar over the year. If the Bundesbank permits the entire brunt of flight capital activity to hit the dollar's parity, the amount of "imported inflation" will approach zero, and even become negative.

Further strong indication of the underlying weak position of the dollar is the willingness of the weaker European countries to ease monetary restrictions. On Jan. 5 Belgium lowered its discount rate from 9 per cent to 8 per cent. On Jan. 6 Holland lowered its discount rate from 6 per cent to 5 per cent. Both France and Britain are taking a less restrictive policy towards the rate of increase of monetary aggregates and-or bank lending. The French franc, which behaves as a "borderline" currency between the deutschemark and Swiss franc on one hand, and the lira and pound on the other, has moved almost precisely in tandem with the deutschemark.

Less significant factors weighing against the dollar include:

1) The seasonal end of repatriation of profits by U.S.-based multinational corporations motivated by Financial Accounting Standards Board regulations.
2) Continued weakness in U.S. interest rates, particularly as U.S. banks permit the runoff of money-market instruments they accumulated as window dressing for their year-end balance sheets.

Otherwise, there is no question that large Arab dollar holders will shy away from accumulating further dollars. Large Arab placements of funds in dollars virtually halted on Carter's election Nov. 2, due to Arab perception that Carter favored Israel more than did the present Administration. This Arab attitude will intensify as a result of, first, Carter's cool response to Sheikh Yamani's demand for a quid-pro-quo with respect to the moderation of Saudi Arabia's oil price increase, and secondly Carter's insistence on meeting Arab heads of state one by one over a period of months, rather than helping to convene a Geneva Mideast peace conference. This week, the West German conservative weekly *Deutsche Zeitung* attributed the dollar's overall weakness to Arab reluctance to hold dollars. As the dollar continues to depreciate, Arab withdrawals of dollar holdings could very well snowball.

On Jan. 5 the new Japanese prime minister Fukuda announced a reflation program including a mid-January cut in the discount rate and a $1.2 billion rise in government expenditures in the first three months of 1976. Probably the yen will tend to move in parallel with the dollar, while most European currencies move in parallel with the deutschemark.

New Activity Due to Business Confidence in Schmidt Monetary Policy

INTERNATIONAL STOCKS

Exclusive to NSIPS

The new spurt of activity in the West German equity market measured by a 3 per cent rise in the Commerzbank index during the past week after several months of total flatness, directly reflects the buoyancy of the deutchemark over the dollar and resultant business confidence in the Schmidt government. Schmidt, with the firm backing of the pro-growth wing of the Christian Democracy led by Schleswig-Holstein Minister Gerhard Stoltenberg, has resolved to maintain the integrity of the mark even under the current tremendous pressure to inflate emanating out of the Jimmy Carter transition headquarters in Plains, GA. (See Foreign Exchange report.)

In particular, activity was strong and future prospects are bright for the energy and machinery sectors. The former, typified by Veba Gelsenberg AG, are part of the European network including the Italian state oil company ENI which is developing relations with the oil-producing countries including Arab investment and joint ventures. The machinery sector, led by Mannesman, is about to benefit from a new spurt of East-West trade under the impact of increased Soviet initiatives for new mechanisms to finance expanded trade exemplified by their offer of Comecon transferable ruble financing to the West last month.

Schmidt made his commitment to expanded trade, with OPEC in particular and in general, in his year-end message to the nation. "Today, we can consider it an advantage that our most important oil suppliers can learn and experience practically, through their participation in our industry, what turning the oil spigot means for us and our economic well-being," he said, in a direct call for cooperation. "Isolated, single dealings of individual states will become more and more difficult."

Otto Wolf von Amerongen, president of the German Trade and Industry Federation, strongly seconded Schmidt in denouncing isolationism and dismissing all arguments against further expansion of East-West trade as "misinterpretations of the differences in the international division of labor."

The energy-related stocks are benefiting directly from the European-wide move for cooperation with the OPEC nations. Veba has risen a dramatic 11.9 per cent since the beginning of December, and 7.9 per cent in the past week alone, while West Germany's other major utilities company RWE has risen 8.1 per cent since December and 4.5 per cent over the last week. The government-controlled Veba is also Germany's national oil company, and is a member along with the state oil companies of Italy, France, and Belgium, of the "Euro-cartel" which these government companies have set up to challenge the U.S. multinational oil companies for control of the European market.

Mannesmann, the major machinery and engineering firm, did exceptionally well, rising 8.6 per cent in the past month, more than 4.6 per cent in the past week alone. Mannesmann, along with other machinery and engineering companies such as Siemens and AEG which also made gains, has already begun to participate in the new upturn in East-West trade which recently started up after total flatness during the summer and fall of 1976.

It should be noted that in general, the rise of most stocks took place virtually entirely within the past week, after a month of real doldrums for the Frankfurt bourse.

	(month end) Nov. 30	(closed Friday) Thursday Dec. 30	Friday Jan. 7	% Change on Week	Month
COMMERZBANK INDEX	725.2	727.4	748.9	+3.0	+3.3
Veba	113.3	117.5	126.8	7.9	11.9
RWE	159.0	164.5	171.9	4.5	8.1
Mannesman	171	177.5	185.7	4.6	8.6
AEG	82.8	82.5	84.7	2.7	2.3
Siemens	256.5	265.5	270.7	2.0	5.6
BASF	157.5	158.8	160.0	0.8	1.6
Bayer	135.5	135.6	141.0	4.0	4.1
Hoechst	137.1	136.0	141.5	4.0	3.2
Volkswagon	135.5	135.5	137.5	1.5	1.5
Daimler Benz	334.3	334.0	337.5	1.1	1.0

World Gold Reserves a Basis For New Credit System

GOLD

Gold has an intrinsic value, measured by the cost to society of the labor-power needed to mine and refine the scarce metal. This intrinsic value justifies, on the most elementary economic criteria, Itály's decision last week to revalue its massive gold stocks to the world market price of $135 an ounce, and motivates the flow of Arab money out of the bankrupt dollar into gold.

Secondly, because both the Soviet sector and Western Europe possess large amounts of gold — over $20 billion and not quite $80 billion at current market prices — this form of monetary reserve is the ideal "bridge" between the socialist and capitalist monetary systems.

Past this , however, the role of gold in the new world economic order is a question of the *political* readiness of countries to extend long-term credit to each other with the objective of raising the rate of *world* development to the maximum. Gold by itself gives us no magic solution.

The Fallacy of "Hard Money"

Specifically, the world is able to expand trade by $300 billion during the first year of operation of an International Development Bank-type monetary system. This is roughly three times the value of all official gold reserves at the market price. This figure of expansion of international trade, which will require long-term trade financing, will escalate geometrically, to the point that the volume of issue of international trade credits will exceed total international gold holdings several hundredfold.

This trade includes the transfer of the means of agricultural development to the Third World, agricultural equipment and machine tools to the Comecon sector, etc., with the purpose of bringing the entire world's population to the highest levels of living standards and skilled productivity reached in the industrial capitalist countries. A decade or more will elapse before most of the recipient-countries will be able to, or properly should, export more goods that they import to "repay" these loans.

Official Gold Holdings Of OECD Countries

1973 (a)

	Value $ Mill.	Volume Mill. Ounces	Metric Tons
U.S.A.	$11,652	275.98	7,822
U.K. (b)	886	20.99	595
Austria	881	20.87	592
Belg.-Luxemb.	1,789	42.37	1,201
Denmark	77	1.82	52
France	4,261	100.92	2,860
Germany	4,966	117.62	3.334
Italy	3,483	82.50	2.338
Netherlands	2,294	54.33	1.540
Norway	41	.97	27
Sweden	244	5.81	165
Switzerland	3,513	83.21	2,358
Canada	927	21.96	622
Japan	891	21.10	598
Finland	35	.83	24
Greece	148	3.51	99
Iceland	1	.02	1
Ireland	18	.43	12
Portugal	1,160	27.48	779
Spain	602	14.26	404
Turkey	151	3.58	101
Australia	311	7.37	209
Total OECD	$38,331 (c)	907.89 (c)	25,733 (c)

(a) December 1973.
(b) September 1973.
(c) Includes U.K. to September.

Converted at $42.22 per ounce of Gold.
Converted at 35,281 ounces = 1 Metric Ton.

Source: International Financial Statistics.