The new system, now incorporated in the articles of the IMF, retains the basic philosophy of Bretton Woods.

The principle obligations charged to nations under the new articles of the IMF are of two classes; first, each country must exert itself to direct its policies toward orderly growth with reasonable price stability (fiscal conservativism—ed). Second, each nation must avoid manipulating its rate of exchange with the end of achieving an adjustment of unjust competitive advantage (no government intervention—ed.). . . . (and avoid) maintaining rates of exchange at artificial levels. But we must admit frankly that neither our new monetary system nor any other similar system could obligate sovereign nations against their will to adopt certain economic and financial policies at national level. Because of these differences all major countries have the responsibility to collaborate on internal discipline which is essential for significant stability in the international monetary system.

We must make the system function by means of surveillance.

To be able to give an operative context to the new system the IMF must develop and augment surveillance procedures in regard to nations' policies—as much in the wide revision of general economic and financial policies of members as in the (mere, usual—ed.) direct revision of their exchange rate policies. We consider surveillance by the IMF as the cornerstone of a new system . . . the vertebral column . . . which provides the means of evaluating responsible international conduct and permits that the influence of the international community will be made felt by those nations which have failed in complying with their obligations.

The U.S. is totally committed to the success of this procedure. For this end, we have formulated specific proposals which comprise three requisites: First, the IMF must possess complete information on the policies and accounts (i.e., monetary—ed.) of the member countries; second, as an institution the IMF must be organized in such manner as to be able to bring to fruition effectively its responsibilities of surveillance, with the participation of political officials of high level within their own governments. Third, the IMF must have techniques to let fall all the weight of moral suasion of the world community toward the compliance of each country with its international obligations . . .

I believe that in future the importance of SDR's will widen. They have an important potential in the long term for the system, and the U.S. worked during the 60s to help to establish this activity . . .

A second possible evolution which could occur in future and which today is receiving renewed attention is the development of a European monetary unit.

How Miller's Credit Policy Undercuts International Banking

Treasury Secretary Blumenthal appears to be having much success in his latest announcement of plans to put the world under an IMF dictatorship. The reason is that the American business community has swallowed the well-propagandized line that Federal Reserve Chairman G. William Miller's high interest rate policies, which are identical to those of the IMF, have stabilized the dollar and will thereby promote an investment boom in the U.S.

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In fact, not only is the "Miller bubble" rapidly destroying the U.S. economy and the dollar—but that is what it is *intended* to do.

The Miller bubble has now passed from stock market investment to straight acquisitions and direct financial operations, with the consequence that little or no international investment in development of the Third World is available and thus expansion of U.S. exports. Although the current rate of international lending is still high, and the "borrowers' market" for syndicated medium-term Eurocredits appears to prevail, bankers are sending out signals that they will not increase their exposure.

There are two features to this development that will damage the American economy. The consequences for trade and international stability of even a relative pullback in international lending are self-evidently catastrophic. But it is the capital reflow into the U.S. accompanying Miller's high interest rates that ironically sets up the dollar for another blowout. This kind of "support for the dollar," against a projected $30-40 billion annual trade deficit, through speculative reflows gives Blumenthal and his allies virtually hair-trigger capability to instigate a new dollar crisis.

The facts of the matter are these.

Manufacturers Hanover Bank projects that their overseas profits during 1978 will drop to half of the total from 56 percent last year. At the Mexico City International Monetary Conference May 22, Chase Manhattan Chairman David Rockefeller warned Mexico that it should reduce its rates of borrowing in favor of "moderate growth"—provoking an angry response from Mexican finance ministry official de la Madrid.

Citibank's Senior Advisor of International Operations, Dr. Irving S. Friedman, defended Mexico's international borrowing as "normal and natural," adding that Mexico has "used and managed" external credit effectively, and has "a record of servicing debt fully and promptly." But Friedman singled out for special praise advocates of the "low growth" approach, e.g., former Mexican finance minister and present InterAmerican Development Bank Chairman Ortiz Mena.

Some bank analysts are already predicting that the two years of easy international credit will give way to stringency within the next few weeks. Although spreads

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charged to developing-country borrowers are still falling, which normally would absorb excess liquidity in the market, special conditions apply. Exemplary is Toronto Dominion's $188 million syndication of Malaysia last week, at a thin 5/8 percent above the London interbank rate. The Canadian bank's aggressive rate-cutting reflects the state of liquidity less than it does the determination of Canadian, British and other banks to get into the U.S. dollar market.

The key to the medium-term trend, which has immense implications for the developing sector and international trade, is the reflow of capital to the United States under conditions created by Miller. Commercial banks are, and have been for the last few weeks, funding domestic loans with foreign deposits, rather than shipping funds abroad, according to the pattern that had prevailed for years.

The surface-effect of the reflow of capital first appeared in the stock market. Foreign net purchases rose from a normal 8 percent of total to an unprecedented 20 percent in recent weeks, according to Securities and Exchange Commission data, coincident with the stabilization of the dollar. However, the stock market is falling—by 20 points on the Dow-Jones average this week as of May 25—and the dollar remains stable, despite heavy foreign liquidation of U.S. securities.

Two related phenomena are at work.

First, the British and Canadian banks are virtually pulling up stakes and moving to the United States (see Business Outlook). At the Mexico City meeting, British bankers talked volubly of their plans to increase their presence in the American market, following two well-publicized takeovers: Hong Kong and Shanghai's purchase of Marine Midland, and National Westminster's purchase of National Bank of North America. Midland Bank's Chairman Lord Armstrong boasted that his bank is receiving sell offers from American banks regularly, and is currently determining which to buy. Barclay's Bank, said chairman Anthony Tuke, is planning further acquisitions.

According to a Barclay's officer, "The problem with American banking is that there are too many banks. We'd like to see about 13,000 of them go (there are 14,000 banks in the United States—ed.), and have nationwide banking the way we do in England and Canada." Barclay's is currently funding its growing American loan business from abroad.

Apart from banking, European investors are piling into the American market. One Dutch pension fund currently has a British consulting firm working out an investment program for its assets in American real estate. The rate of foreign acquisitions of American firms has skyrocketed.

Perhaps more importantly, although there is a real loan demand, Miller's credit tightening policies have forced all borrowers to jump in *now* rather than face percentage-points higher interest rates later in the year. There is a "rebound" of economic activity now ongoing merely to bring the economy back to 1977 levels following last winter's coal strike. But this is not a healthy loan demand.

With operating profits down 24 percent from comparable 1977 levels, corporations are borrowing for working capital, (not for new investment) and consumers are borrowing at an 18 percent annual rate of increase to maintain merely *current* levels of retail sales.

Particularly since Miller has forced rates up artificially by tightening liquidity in the banking system each time the Treasury comes into the market to refund debt, the Fed Chairman has set off a "borrowers' panic" of marginally determining proportions.

This year so far, overall credit demand has risen at a 35 percent annual rate. This is what has prompted banks to fund their domestic assets from external sources.

The International Monetary Fund is already projecting international liquidity problems as a pretext for arrogating to itself additional credit-creating power. Cited in the *Economist Financial Report*, IMF Managing Director Johannes Witteveen is reported to have told bankers that "the large increases in world trade and prices had outstripped liquidity, reserves were highly concentrated in a few industrialized countries and a large number of countries' reserves were borrowed, rather than owned."

Translated into reality, what Witteveen is saying is that the forced concentration of the world's dollar liquidity into the buying-up (and stripping down) of North American industry will mean no dollars available for Third World development. Thus, the developing sector will be obliged to come begging to the IMF for Special Drawing Rights . . . the City of London's favored non-currency for recycling debt.

—David Goldman