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DOMESTIC CREDIT MARKETS

Miller holds back on new credit tightening

Last week the *Executive Intelligence Review* advised its consulting clients that Fed Chairman Miller would not push for higher interest rates at the Federal Open Market Committee meeting on April 17. The *New York Times* and a host of seasoned economists were predicting the opposite. Those who followed their advice got burned on Tuesday when Miller let it be known that he opposes another interest rate hike at present, and interest rates fell sharply in the government and corporate bond markets in response.

In an interview published in the *Times* April 18, Miller explained that he opposes a new hike in interest rates because an economic slowdown is already underway in the U.S. We suspect, however, that the primary motivation was international. Like his predecessor Arthur Burns, Miller keeps one eye on what his counterparts in Japan and West Germany are thinking. The steady jacking up of U.S. interest rates since late last year was designed to prop up the dollar and attract capital back to the U.S. It has done that to such an extent that the West German and Japanese government bond markets are now badly hurting. Both nations have been forced to raise interest rates—despite the pernicious consequences for their industrial sectors—to close the wide differential with U.S. rates (see International Credit). Another upward blip in U.S. interest rates at this time might have been too much for the European and Japanese to swallow.

As to where interest rates are now headed, there is as much confusion in the money markets as there was before the FOMC meeting last week. Some market analysts think that the FOMC may actually have decided to tighten rates another notch, given the enormous amount of pressure for higher rates coming from the "recession now" lobby in the Administration—Treasury Secretary Blumenthal, "Inflation Fighter" Alfred Kahn, Council of Economic Advisors head Charles Schultze, et al. However, the FOMC gave no clear signs in the market April 18 of what decisions had been taken in its inner sancturn. The Federal funds rate, the rate over which the FOMC has direct control, hovered around $10^1/_{16}$, the same range it has held to for weeks.

There is little uncertainty about what the nation's regional banks are thinking about interest rates. The Southwest Bank of St. Louis dropped its prime rate from $11^1/_2$ to $11^1/_4$ percent on April 17 in a gesture of opposition to continued high interest rates. Southwest Bank was one of the banks which initiated the short-lived drop in the prime rate in late January of this year. I.A. Long, chairman of the bank, attributed the current interest rate move to the decline in a number of key measures of national economic activity—retail sales, consumer confidence, etc.—which suggest a lull in future loan demand.

It's no secret, however, that the small regional and country banks have gotten the foul end of high interest rates and have actually been lending at rates below prime for months to keep their long-standing customers supplied with credit at prices they can afford. The problem the regional banks have run up against is credit availability—they have been unable to compete for lendable funds at the current prohibitively high rates. The money center banks, on the other hand, who have taken advantage of the reflow into the dollar by issuing certificates of deposit in London, are flush with funds. The Federal Reserve has in effect created a two-tier credit system with its high interest rate policy, in which regional banks experiencing heavy loan demand are the banks cut off from credit.

How does Miller's latest pronouncements on Fed interest rate policy affect this situation? George Harbin of Dean Witter Reynolds said in an interview with *EIR* that he anticipates that Milller's backoff should have an "equilibrating" effect on world money markets. He thinks the dollar rise and the capital reflow will moderate slightly in the coming weeks. "We expect things to go sideways for a while," he reported.

Toward mandatory controls

While international considerations have for the moment forced the Fed to abandon its hardline approach to high interest rate and recession, new recession scripts are already coming from the scenario specialists. Former Fed Chairman Burns, who is now working as a consultant to Lazard Freres investment bank in New York, surfaced last week at the American Enterprise Institute. Burns contended that if the current "boom" in the economy continues unchecked, "six months down the road" the Administration "may be driven" to impose mandatory wage and price controls.

Another ominous note is the fact that Senators Helms and Proxmire have scheduled full Senate Banking Committee hearings for May 24 on lifting the President's authority dating from 1969 to impose credit controls. The Administration and the Federal Reserve Board have already leaked to the press that they would oppose any such rescinding of presidential authority, suggesting that credit controls are an option they will go with if given the political maneuvering room.

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