Carter's Schachtian budget proposals

by David Goldman

President Carter's budget for Fiscal Year 1980 proposes a drastic transformation of the American economy, comparable on a point-for-point basis to Hitler's Finance Minister Hjalmar Schacht's plan for Germany during the 1930's. That comparison is not a vague allusion, but a matter of simple comparison. Two features—one stated and one unstated—have escaped most budget analysts, despite the fact that these features of the budget will scar the American economic system for years to come.

First, the actual budget deficit including all the various off-budget, "government-sponsored," "govermnet guaranteed" and similar borrowing requirements, is officially projected to be $91 billion during calendar year 1980, in a "best-case" scenario. With a snap economic down turn, it could be much worse. The deficit would be $130 billion if the budget did not program in a $40 billion tax increase.

Second, the Treasury is currently preparing extraordinary measures to make the outsized deficit financeable. According to Treasury and private banking sources, Secretary Miller will use the Treasury's 260 million ounces of gold to obtain financing for the deficit. More precisely, the Treasury will employ a combination of uses for gold to finance the budget deficit through the capital account of balance of payments.

Unimagineable a few months ago, the startling reversal on gold policy—now expressed in top-secret staff documents—is a minor change relative to the scale of decisions embodied in the new budget. The administration has opted for a national-autarkical war economy, including:

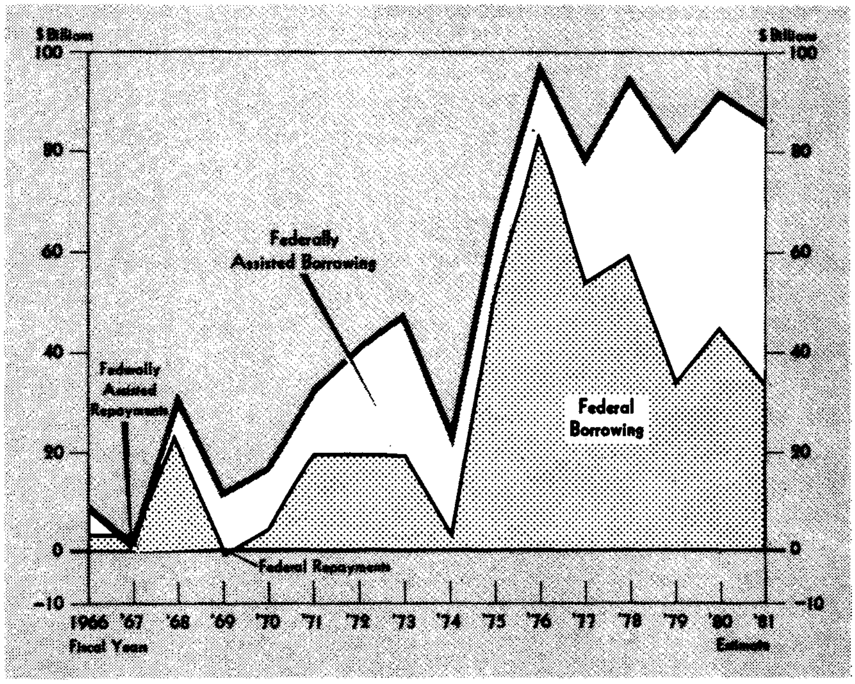
1) A $15 billion and perhaps larger increase in defense spending;
2) Attrition through inflation of virtually all social programs and transfer payments;
3) A $7 billion reduction in the outlays of federal and government-sponsored agencies for housing;
4) A major commitment to energy autarky through the most obsolete and inefficient technologies; and
5) A staggering increase in the rate of taxation.

More than in previous years, the most important parts of the budget have been hived off into the polite fraud known as "off-budget spending." The purpose of this fraud is to leave the congressional committees and financial press with a bare bone to gnaw, while the off-budget agencies do precisely what the administration wants. The accompanying graph published in the *Special Analyses of the Budget of the United States Government: Fiscal Year 1981*, tells most of the story. Most of the federal deficit, i.e., most borrowing for new programs, now occurs on the "off-budget" side. This procedure began during the final year of the Ford administration, in the form of massive subsidies to the housing market, a fact later regretted in print by President Ford's economic advisor Alan Greenspan. However, under the Carter Administration, off-budget financing dwarfs the "on-budget" federal deficit.

It must be pointed out that a recession deeper than the 1 percent decline in GNP forecast by the administration would add perhaps another $40 billion to the deficit, in the opinion of Manufacturers Hanover Trust economists, pushing the deficit past proportions which most economists can deal with conceptually.

Whether or not the economy breaks down, the size of the best-case-scenario deficit is the first Schachtian feature of the Carter budget. In anticipation of this deficit, which Salomon Brothers calculated at $44 billion at the outset of the year, the bond market lost a clean 10 percent of its paper value during the past four weeks. If the administration's forecast of 11 to 12 percent inflation is correct, bond prices have another 10 percent to fall, according to Arnhold S. Bleichroeder Vice-President, Erwin Shubert. Shubert adds that if inflation raches 20 percent—a figure forecast by this publication and various private sector economists—bond prices will fall between 20 and 30 percent. Private long-term credit has already been crowded out, and matters will get much worse very quickly.

Federal and Federally Assisted Borrowing



It does not matter much if Federal Reserve Chairman Paul Volcker chooses to finance the deficit by allowing significant monetization of federal debt and rising interest rates, as he has during tte past two months, or whether the administration opts for some form of credit allocation. The net effect will be identical to the impact of Nazi Finance Minister Schacht's successive issues of "Mefo-bills," the paper of the *Metalforschungsinstitut*, the funding agency for war production.

$40 billion tax bite

The second Schachtian feature of the budget is the extraordinary tax increase in the face of recession, the one plank of thelrogram that drew some howls from the corporate sector. The $40 billion tax increase includes the following:

1) $14 billion in personal income taxes, due to inflation rushing taxpayers into higher brackets;
2) $414 billion of additional Social Security deductions;
3) $11 billion in crude oil taxes.

The final category is important, because the potentially explosive debate over whether the windfall profits tax would fund special energy programs, or be applied to general revenue, simply failed to take place. As it happens, Carter's various synthetic fuels programs will be financed off-budget, adding an additional deficit financing requirement to the already onerous oil tax: the worst of both worlds.

Perhaps even more important than the gross size of the off-budget operation is the change in its content. Previously, off-budget financing was dominated by the various federal agencies—Ginnie Mae, Fannie Mae, and so on—who support the secondary mortgage market. The real boom in these agencies' activities started with the Ford administration's frantic preelectoral attempts to stage a recovery, and helped to trigger the spiral in the resale value of private homes during 1976-1979. Severely flawed, their lending activity nonetheless helped to support the homebuilding sector. Taken as a group, they will spend $9 billion less in 1980 than in 1979, a reduction which amounts to a death sentence for the homebuilding industry.

Table 1 shows a corresponding group of increased (and some new) off-budget categories, the most important of which constitute a $9.7 billion addition to spending. All of these categories are directly or indirectly related to the twin administration goals of military production increases and energy autarky.

For example, the $300 million rise in rail subsidies will be devoted almost exclusively to coal-carrying lines. The Chrysler loan is, at least in part, a preparation for capacity conversion to defense uses, as is the $900 million rise in aircraft loans. The one major category that does not conform to this pattern is the $900 million outlay of the Commodity Credit Corporation, which represents compensation to farmers for Carter's embargo on grain sales to the Soviet Union. The energy expenditures are for synthetic fuel plants otherwise uneconomical at crude oil prices of less than $40 per barrel, for the pumping of additional oil into salt domes from which it cannot at present be recovered, and so forth. This is in a budget which eliminates all funding for the fission fuel breeder reactor, drastically cuts fusion power research and development and presumes the virtual elimination of the country's nuclear program.

The mild recession fraud

Clearly, the Economic Report of the President, which projects a mere 1 percent fall in Gross National Product during 1980, is intended to be a self-fulfilling prophecy. The basis for this projection is the relationship between federal spending and economic behavior during the fourth quarter of 1979, when the policies expressed in the new budget had apparently already gone into effect. From the standpoint of Table 1, there is nothing contradictory about the failure of real GNP to fall, despite huge dislocations in the auto, construction, and steel sectors—three of the economy's biggest determinants. The difference was made up by a 23 percent per annum rise in defense spending during that quarter, an even larger rise in other categories of government spending, and some gearing-up in anticipation of larger defense orders to come.

Even so, the apparent stability of both the deflated Gross National Product numbers and the Industrial Production Index is not likely to last. Consumer spending only remained stable, in real terms, through the depletion of savings, bringing the savings rate down to the lowest in the history of that statistical series. Consumers apparently concentrated spending on soft goods while eliminating spending for durables, leaving auto at 23 percent below the previous-year's levels, home construction down 25 percent, and, consequently, steel down 10 percent.

However, additional output in the aerospace, communications equipment, and business equipment sector helped "stabilize" the indices. Certainly, they must decline further as consumers run out of savings accounts. The administration projects only a slight decline, expecting that the additional military and energy-related spending programs now coming on line will take up the slack.

The problem is that virtually all the additional economic activity planned into the budget is nonproductive, in the strict technical sense that it involves goods that do not reenter the reproduction process of the economy. From the inflation standpoint, military goods or synthetic fuels plants do exercise demand, but do not create supply (at least, in the latter case, not at current price levels). The inflationary possibilities arising from this direction of the economy are prodigious.

Last week, *EIR* published the results of a computer study of the projected military and related spending increase, employing the Riemannian LaRouche model. This model, developed for *EIR* at the proposal of contributing editor Lyndon H. LaRouche, Jr., analyzes ratios within the productive sector, rather than Gross National Product. The study showed that within two years of the inauguration of a military buildup policy of the type proposed by the administration, the economy would suffer such depletion of resources as to stop functioning in its previous mode.

In their own way, the financial markets have anticipated the worst, battering government long-term securities with unprecedented fury. With great reluctance, the Treasury will have to pledge its gold reserve in one fashion or another to prevent interest rates from rising out of control (see GOLD). Otherwise, the actions of the government would force an economic crisis much sooner, force the nation into sudden, deep recession, and tear the proposed budget to shreds. The Treasury is hoping that it wil have time to dig its own grave; it may not even enjoy that dignity.

Table 1
The Transformation of the "Off-Budget" Budget
(in millions of dollars)

Planned increases*	
Energy Security Trust Fund	$300
International Security Assistance	1,200
Commodity Credit Corporation	.900
Geothermal Resources Fund	.300
Energy Security Reserve	1,500
Energy Security Corporation	.800
Rail programs	.300
Aircraft loans	.400
Chrysler Corp. guarantees	.900
VA Housing	3,400
TVA States Energy Corp.	.684
TOTAL	**9,700**

Planned cuts	
Farmers Home Administration	$2,400
HUD low-rent subsidies	.300
Federal Housing Administration	1,000
Government National Mortgage Agency	2,600
Guarantee of New York City loans	.300
Federal National Mortgage Assoc.	2,200
Federal Home Loan Mortgage Corp.	.200
TOTAL	**9,000**

*Net change for 1980 minus net change for 1981
Source: Special Analyses of the Budget of the United States Government: Fiscal Year 1981.