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The IMF demands advanced-sector consumption cuts

The following report was prepared by EIR*'s Economics Editor, David Goldman, and by our special correspondent, Dr. Michael Hudson, an economist formerly with the Hudson Institute, Arthur Anderson, and Chase Manhattan. The report reflects extensive off-the-record background discussions with economic and monetary officials at the IMF-World Bank meeting.*

1980's annual meeting of the International Monetary Fund and World Bank, the two most influential international institutions in world economic affairs, proposed to prolong the current world downturn into a five-year depression, as a matter of official policy. IMF Managing Director Jacques de Larosière told the opening session of the world convention for financial officials and international bankers, "Three problems dominate the state of the world economy: inflation, energy, and the plight of the non-oil developing countries." He proposed to deal with these problems in the following way:

- to suppress inflation through the discredited monetarist policies that have brought about both depression and double-digit inflation in Britain and the United States;
- to concentrate all available international resources on investment in *high-cost* forms of energy production, assuming an $80 per barrel oil price by 1990;
- to finance next year's $80 billion dollar payments deficit of the world's developing sector under "conditionalities" that have already produced mass starvation in Zaire, near civil war in Jamaica, and a military coup in Turkey after these countries accepted IMF dictates.

"In effect, the IMF is proposing to finance the Third World deficit"—equal to the debt service these countries must pay to banks on $350 *billion* of accumulated debts—"through a world depression," a senior European central bank official told *EIR*. The logic is brutally simple. If the economies of the leading industrial countries remain depressed, their banking systems will not be called on to lend heavily for economic growth at home. Instead, their financial resources can be applied to papering over the huge payments deficits of developing nations. Rather than mobilizing the productive resources of the industrial nations to export means of development to the southern hemisphere, the IMF wants to loot the industrial economies to merely refinance debts of the poor nations—which is in the interest of neither group.

A besieged institution

Although communiqués issued by the IMF steering committee, the Interim Committee, were carefully phrased to give the impression of consensus, no such policy could possibly bring forward a consensus from nations who cannot survive without economic growth. On the contrary, the IMF is a besieged institution, barely able to maintain political leadership over the world economy. Still, it remains in command by default, largely because Western Europe has postponed implementation of the projected European Monetary Fund for at least 15 months.

Opposition to the IMF program is so intense the strategy may collapse, because nations may deny the money required to bring it off. A former chairman of

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the IMF's Interim Committee, Sir Jeremy Morse of Lloyd's Bank, told *EIR* that to prevent a world payments collapse next year, the IMF, World Bank and other official institutions must be able to provide 40 percent of the total financing requirements of the developing countries, with private banks providing 60 percent.

However, neither the U.S. Congress nor the oil-rich Arab nations, the most important "hits" for additional IMF funding, are ready to bankroll the hated institution.

Funding blocks

First, the Saudis and Kuwaitis, whom Managing Director de Larosière asked for $10 billion, are blockading the IMF and World Bank, nominally because the fund refused a Saudi request to allow the Palestine Liberation Organization to attend the annual meeting as an observer. The fact is that the Saudis do not want their $200 billion in resources to be misspent in refinancing debts for the benefit of U.S. banks, although they are prepared to give money for actual development. Several top bankers interviewed at the meeting, including Richard Debs of Morgan Stanley and Robert V. Roosa of Brown Brothers Harriman, both former top U.S. officials, insisted the Arabs would have to ante up. But it is not certain that a U.S. administration, which has thrown its support toward Khomeini-style Islamic fundamentalism will be able to convince the Saudis to come across. The Saudis have not forgotten a stream of State Department leaks predicting the overthrow of the monarchy.

Even more damaging to the IMF's standing was action this week by Senate Republicans to block America's contribution to the current round of IMF funding. The IMF raises funds by drawing "quotas" from its 140 members, paid in the members' own national currencies. The member can draw its own quota as a loan, but if it wants to draw more, it must invite the IMF to run its economic policy, with disastrous results. For the IMF's operations the American quota contribution paid in U.S. dollars is more important than that of Brazil, paid in soft Brazilian cruzeiros. Under IMF rules, the members having 75 percent of all quotas (which are assigned by economic weight) must pay up before all the money can be collected. If the U.S. declines to pay, it will scuttle the entire $25 billion funding operation.

The Senate move, which blocks an appropriation bill for the IMF worth $5.5 billion until the end of the present recess and possibly until the next session of Congress in March 1981, caused consternation among U.S. and IMF officials. "Right now the IMF has enough liquid resources to keep going," a top Treasury official told *EIR*. "But in terms of confidence that resources will continue to be available, it's very bad." Even with the $25 billion increase under the present seventh review of quotas, the IMF would come up $10 billion short for 1981, officials calculate—a gap the IMF must make up one way or another from the Arabs. If Congress continues to balk, the entire world payments system will go on the skids.

In a speech to the House of Representatives two weeks ago, Cong. Jack Kemp attacked the handout to the IMF on the grounds that Congress should not fund an institution whose policies topple governments. This objection, and the political motive of embarrassing President Carter before the election, is responsible for Utah Senator Jake Garn's derailing of the appropriation bill in the Senate Banking Committee.

There is unfortunately not much to prevent these raids on the IMF from simply making an uncontrolled global payments crisis more likely than the murderous, orderly world depression the IMF proposes to conduct. No one has yet offered a replacement to the institution. The bottom line, British Chancellor of the Exchequer Sir Geoffrey Howe bragged to *EIR*, is that Britain's own monetarist program, is taking over the international institution. Asked how long Britain's 20 percent inflation would have to persist before he admitted Friedmanite monetarism was a failure, Howe replied, "It is now recognized that monetary policy has a crucial role to play, and monetarism has become the dominant discussion among the finance ministers and at the International Monetary Fund." Britain's disastrous policy has become IMF policy for the world.

IMF energy policy

In his opening address, Managing Director de Larosière warned against a "shift toward expansion" in the industrial countries, threatening that greater energy consumption would produce "upward pressures on the price of oil." Retiring World Bank President Robert McNamara, Lyndon Johnson's Secretary of Defense, backed up this threat with a "prediction" that oil prices would continue to rise at an accelerating rate to almost $80 a barrel in 1990. McNamara's recommendations could be summarized as, "burn people, not oil." There is no reason for oil prices to double again—McNamara cited no evidence for this—especially if the industrial nations offer the oil producers a stake in a nuclear-energy future in return for restraint on oil prices in the medium term. McNamara's dictum that "the price of oil . . . is likely to continue to rise in real terms by perhaps 3 percent per year," or the inflation rate plus 3 percent, is based on a British-authored draft paper handed to the Organization of Petroleum Exporting Counnries. The premise of the paper is that oil prices must rise this fast to make monstrously expensive synthetic fuels "economical." The U.S. and Britain have *opposed* Saudi Arabia's efforts to hold down oil prices on the ground that this will undermine the synthetic fuels program!

If McNamara's prediction bears out, the Third World will have to pay $280 billion a year for oil by 1990, "a level that would be difficult to finance by any conceivable expansion of exports, or increase in external borrowing," the World Bank president said. Therefore "the oil-importing developing countries should establish efficient import substitution in energy as one of their principal tasks for the 1980s," absorbing every dollar of external resources that do not already go to debt service. In sum, the World Bank—in combination with the British and U.S. governments—wants to continue the upward push of oil prices and force a "structural adjustment" on developing countries which will destroy all investment *except* in the energy sector. If the World Bank seriously wanted to reduce developing nations' dependence on imported oil, it would finance nuclear power plants—an alternative that McNamara specifically excluded from his list of possible energy sources.

Europe's waiting game

According to top-level European officials, France and West Germany went to Washington to wring out two concessions from the Anglo-American leadership, and achieved their extremely limited objectives. Otherwise, the Franco-German strategy is to hang on to economic health by their fingernails for the next 15 to 18 months when the new European Monetary Fund can be put on line—an extremely hazardous delay.

The concessions were the following:

First, the French succeeded in forcing through a change in the definition of the "conditionality" with which the IMF lends money, which amounts to giving troubled countries more money and more time to adjust their economies. At a Sept. 29 press conference, de Larosière alluded to the compromise position that as an "experiment" the IMF is easing terms of conditionality in some cases, and that the matter would be kept under day-by-day review. Whether the tiger will change its stripes as the French wanted is entirely questionable—as questionable as the IMF's obtaining the money to lend out in the first place. In his speech Sept. 30, de Larosière indicated that the basic Friedmanite character of IMF conditionality would *not* change, only that "it must be recognized that correction of disequilibria will often need to be extended over a longer period than that considered normal in the past."

Second, Anglo-American efforts to transform the IMF into an all-powerful world central bank, issuing its own currency, the so-called Special Drawing Right, were shunted aside yet again. British minister Sir Geoffrey Howe proposed, in his speech to the meeting, a virtual World Bank takeover of international lending, drawing the OPEC countries into "Joint Lending Programs" with the World Bank. Again, U.S. Treasury Secretary G. William Miller called for steps to make the Special Drawing Right an international currency, to "expand the use of SDR-denominated instruments by the private sector," and to create a "substitution account" to replace the role of the U.S. dollar as a world reserve currency by the supranational SDR. Both these plans will get nowhere.

One of France's top monetary officials, an adviser to President Giscard, talked frankly in a background discussion of Europe's slim hopes of avoiding economic disaster. In January 1980, France's President promised a dramatic new initiative to transform the world monetary system, an alliance between Europe and the oil-exporting countries on the basis of a new gold-backed monetary system. "It did not happen," the official said, "because when President Giscard made his speech, the price of oil was $20 a barrel, and by June the price of oil was almost $30 per barrel. France suddenly faced a payments deficit due to the oil price increase, of about $5 billion a year, Germany of about $15 billion." With their economies weakened, the French and German leaders did not dare adopt a broad monetary initiative. The launching of the European Monetary Fund, an alternative source of international credit to the IMF, will be postponed past the March 1981 implementation date to late 1981 or early 1982.

Retrenchment on leadership

The French official put forward a cold-blooded appraisal of the most optimistic scenario for the next 18 months. At best, Europe's big industrial nations will retrench and prepare for expanded exports to correct their oil-induced payments deficits. The middle tier nations, Portugal, Spain, Greece, and Turkey, will have to accept zero growth for the interim period, he said. And if the flow of money from the private banks, the IMF, and other sources can somehow be maintained, the world may just manage to avoid a collapse of international trade. He grimly noted that Federal Reserve Chairman Paul Volcker's interest-rate policy, which has brought the American prime interest rate back up to 13 percent, is a grave threat to the stability of the European Monetary System, the currency bloc that has sheltered Europe's economy from the worst effects of the Anglo-American depression.

By 1985, the official added, half of France's electricity will be produced by nuclear-power plants, reducing that nation's dependence on Mideast oil. But getting through until then depends on a set of "ifs"—continued refinancing of massive Third World deficits, stable oil prices, and Europe's ability to resist interest-rate war-

fare by the British and American central banks.

"It is extremely difficult for us to take the mantle of leadership of the West," said a well-placed West German banker attending the meetings. "The German economy is in trouble. The Japanese are much more competitive than we are on world markets. And because of our payments deficit the German monetary authorities will make it difficult for us to lend money to export our goods."

These economic problems acknowledged, the real problem is political. "Chancellor Schmidt is a good manager," the German banker continued, "but he is no politician." Until West Germany's elections Oct. 5 and France's Presidential elections in May 1981 are over, the French and West German leaders will bow to the authority of the IMF, even if the IMF is leading the Western economies into disaster.

Europe cannot accept the IMF's indefinite depression. "We have a young population," said the deputy central bank chief of one European country. "We have to give them employment, and we need growth of 4 to 5 percent per year at least."

But there is about an even-money chance that a disaster will overtake the financial system before Europe has time to put its affairs in order. In fact, this is Britain's last card to play against the Europeans. One journal circulating at the Annual Meeting, *International Currency Review*, is closely allied to the Keith Joseph wing of the present British government. It expressed unofficial British policy in an Armageddon scenario story. "Faced with a rapidly growing Third World debt crisis—underscored by Brazil's warning of possible debt-servicing difficulties next year, Turkey's unexpected demand for the rescheduling of $3 billion of debt incurred in 1979, severe imminent problems in Zaire and the clear prospect that Poland could default on its $20 billion worth of hard currency debt at any time—bank regulators are desperately seeking to protect their own domestic banking systems from a global financial crash." The Tory journal further predicts that "the central bankers' safety net will be found to be full of holes."

Britain's Conservative government is fully aware of the consequences of the global monetarist program that Sir Geoffrey Howe took credit for at his IMF press conference. Ultimately, the result will be the breakup of the world financial system and the retreat of nations behind exchange control barriers, as in the early 1930s. The appearance of the *International Currency Review* story at the IMF meeting should be sufficient warning that Britain is prepared to use a "Hayekian stabilization crisis," as the journal put it, as a weapon against the European Monetary System.

De Larosiere calls for restraint on demand

The following is an excerpt from the annual report to the International Monetary Fund meeting in Washington, D.C. Sept. 30, delivered by Jacques de Larosière, the Fund's managing director.

It must be recognized that many countries have noticeably tightened their economic policies since we met in Belgrade last year. These countries have given top priority to the fight against inflation, and elimination of negative real interest rates in most industrial countries is a sign of this awareness. But the member countries that have taken this firm stance against inflation now face a crucial test. Activity is weakening and unemployment is rising in most of the industrial countries; there is a danger that great pressure may now be exerted on national authorities to relax demand management policies. . . .

Assume first the industrial countries persist in their fight against inflation. Given the present very high rates of inflation in quite a few of these countries, this implies that they accept for some time a reduction in the growth of their nominal demand. It may be expected, on this hypothesis, that inflation in the industrial world gradually decreases, that the average rate of growth of real GNP advances from a low level, and that the recycling problem proves manageable. This scenario is certainly not ideal, and it could entail an increase in economic slack. It would, however, restore by the mid-1980s an environment conducive to sustained long-run growth. . . . Several years would have been lost in the fight against inflation. . . . Demand management policies and supplementary measures to restrain the growth in incomes need to be accompanied by measures to improve productivity and efficiency. In many countries, growth has been affected by structural problems, including poor productivity records and rigidities arising from the widespread quasi-automatic adjustment of wages and special benefits to rising prices. In some countries, the adjustment of relative prices to changes in the world economy has been restrained or prevented. Subsidies have been directed to the maintenance of outdated production methods and of industries in decline. . . . Through adjustments of tax structures and government spending programs, it is important to shift resources from consumption to investment without sacrificing overall fiscal restraint. . . .