Monetarist policies are undercutting the strength of Europe's NATO partners

by Michael Liebig

The following is an abridged transcript of the presentation by Michael Liebig at EIR*'s May 10 conference in Washington, D.C. on "Taxes, Credit, and the Future of the U.S. Economy." Mr. Liebig, an executive director of* EIR, *is based in Wiesbaden, West Germany.*

I am going to discuss briefly today the interconnection between the domestic and external security situation in NATO—specifically the European part of NATO—on the one side, and the high interest-rate policy on the other.

It should be clear that military-strategic potential, war-fighting potential, and at the same time war-avoidance potential of any nation has to be based on the idea of *logistics.* In the history of military strategy this has been understood, from Machiavelli to Carnot or Scharnhorst, or here in the United States in the 20th century by General MacArthur, or in Europe by General de Gaulle. You cannot separate the logistical base from military capability of a state. I think it is somewhat remarkable that President Reagan in his recent West Point address pointed to this.

In the debate during the last months in Europe, this issue has played a major role. Chancellor Schmidt some time ago said that from his experience with military matters in general and from his political experience he had come to the conclusion that the notion of military strategy, as exemplified by Mr. Buchan, founder of the London International Institute for Strategic Studies, [IISS], was inappropriate because it excludes the financial and economic foundations of military and strategic matters.

Federal Reserve Chairman Paul Volcker got into office under the Carter administration—and I think that this is a fact which is very closely watched in Europe. The question is whether the kind of policy that was pursued under Carter will simply continue under the Reagan administration, which started from different premises.

Now the Volcker policy is nearly identical to the policy initiated in early 1979 by the Thatcher government in Great Britain. I think that everybody in the United States who is concerned with the effect of financial policy and especially high interest-rate policy on security—domestic and external—can draw very definite conclusions from what has been going on in Great Britain over the two years since Thatcher took power.

The high interest-rate policy in the United States and Great Britain has been forced during the last years upon the rest of the NATO countries, and that represents a dangerous threat to the internal and external security of the NATO countries individually and to NATO as a whole.

Lothar Ruehl, the West German deputy government spokesman, pointed to this at a meeting of the Wehrkunde group in Munich late in February. Mr. Ruehl used to be for years military correspondent at NATO headquarters in Brussels, and the conference included top-level people concerned with military affairs in NATO. He said:

> Ever-growing speculative amounts of capital are moving from Europe into the American dollar because of the high interest rates in the U.S. . . . Should this discrepancy continue, or even expand, the Americans should be aware that this will lead to at least a partial collapse of the deutschemark and possibly the Swiss franc. . . . Then we will have a situation in which money movements out of Europe will turn into actual capital flight. Under these conditions the West European economies will lack precisely those resources that are the precondition for an expansion of our defense efforts.

This was said in February, and whoever has watched the financial and economic situation in the NATO countries since then knows that this is what has happened.

We can outline seven principal effects of this policy. First, economic instability in France contributed decisively to the defeat May 10 of French President Valéry Giscard d'Estaing, thereby weakening Schmidt in Germany. Second, the European Monetary System was derailed as a result of Giscard's ouster, and financial analysts are predicting that François Mitterrand will soon pull the franc out of the EMS. Third, the crucial high-technology capabilities of small and medium-sized firms are being wiped out. The tax base which such firms represent, as well as the depressed housing, auto, and other industrial sectors, are being eroded, increasing the budget deficits of governments. High interest rates reduce state refinancing capacity.

Fourth, Europe's export potential is being undermined—and the West German economy in particular cannot survive without exports, the key to its economic and political stability. Fifth is a significant reduction in employment thereby created which produces an increased potential for social political instability. Sixth, exports to the developing sector nations can no longer be financed. This has forced a deterioration among so-called LDCs from a desperate situation to something like a hopeless situation. This cannot be seen purely in economic and financial terms, since it results in political destabilization, civil wars, and regional conflicts, with very immediate implications for the global situation.

The seventh point, which is in a way the most important, is that all of this high interest-rate policy allegedly was designed to fight inflation. Yet the result of two years of high interest rates in Europe is that inflation is worse than ever. Many of those people, like Volcker himself, who are pushing for high interest rates actually say more or less publicly that it is not intended so much simply to fight inflation, but that high interest rates are effectively being used for so-called structural readjustments of the world economy as well as the national economy toward a "postindustrial" orientation.

The United States could rely in NATO—up to the 10th of May—upon the Franco-German alliance as the pillar of stability for global security and in respect to the Warsaw Pact. This no longer exists. Giscard is out and the military cooperation, in the context of NATO, between France and West Germany is pretty much out the window too. Under Giscard and Schmidt a "division of labor" developed between France and West Germany, in which France concentrated on building up its nuclear deterrent capability while West Germany concentrated more on the conventional side.

One has to be aware, whenever there are complaints about arms spending in Western Europe, that during the fiscal year 1980-81 the increase of the French defense budget was 18 percent, something I can assure you will change under the government of François Mitterrand. France had a major nuclear deterrent buildup: six nuclear missile-launching submarines, the development of the neutron bomb, the development of the mobile counter SS-20, which could be a crucial factor in the European nuclear balance, and the development of other tactical nuclear weapons systems. All these are now in question.

From the West German side, there has been a rather ambitious conventional arms buildup, including the Leopard II tanks, a rather sophisticated antiaircraft missile system, a buildup in naval strength, the "Tor-

Chancellor Schmidt: 'economics is the key'

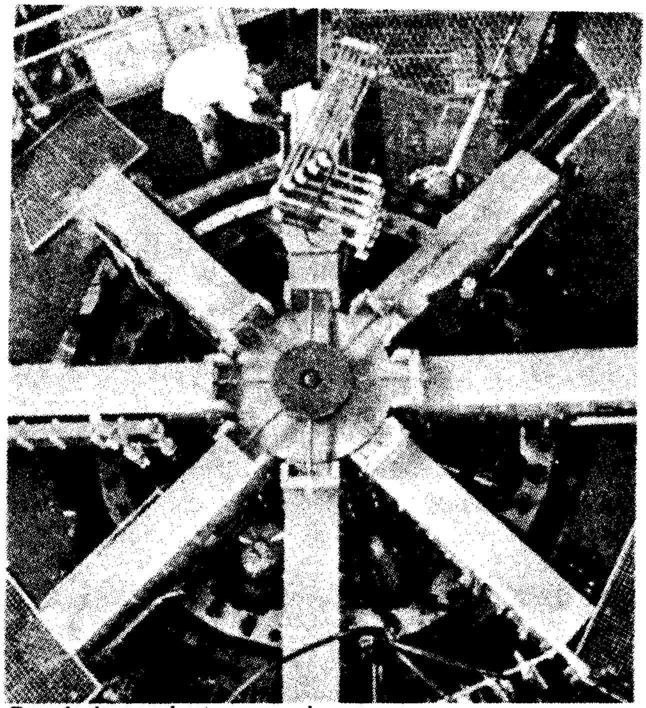
West Germany's Chancellor Helmut Schmidt in 1977 leveled a criticism against the failure of Western—notably British—defense analysts to take into account the close relationship between military security and economic development. The following is taken from his Oct. 28, 1977 address to the London International Institute for Strategic Studies (IISS), in honor of the Institute's founder Alastair Buchan.

In preparing for this lecture I picked up again Alastair Buchan's book *Power and Equilibrium in the 1970s*. It is an important and a very thoughtful book in which Alastair analyzed the structure of world politics only five years ago. He concerned himself mainly with the power equilibrium among the United States of America, Western Europe, Japan, the Soviet Union, and China. Brilliant thinker that he was, he did not at that time devote much attention to the economic, the social, and the domestic aspects of Western security, which I will list today as a new dimension. . . .

What exactly are these new dimensions? First, economic development. By this I mean the necessity to safeguard the basis of our prosperity, to safeguard free-trade access to energy and to raw materials, also a monetary system which assists us in reaching those targets. There was a feeling not too long ago that we had only a few problems in this field. But the oil crisis, the phasing out of the Bretton Woods agreement, worldwide inflation, unemployment, and too little economic growth have changed the picture and given rise to widespread insecurity.

Second, social security. By this I mean the necessity to achieve and maintain social peace at home, making the goods and the jobs available for our people and at the same time bluntly telling them that there are limits to what the state can do for them. . . .

Third, domestic security. By this I mean the necessity to strengthen and defend our society against terrorists whose sole aim is to destroy the fabric of that society through acts of brutal killing and kidnapping.



French plasma physics research.

nado" and "Alphajet" programs. Now, as an immediate result of the monetarist high interest-rate policy, these programs are in danger.

In France, the interest rate has doubled over the last three months or so from around 12 percent to 22 percent. There are 1.7 million unemployed and an inflation rate of about 14 percent. The French franc went down in an even shorter period from about 5 to the dollar to 5.75 right now.

Italy has a prime rate of around 23 percent. Medium-sized industries, which are important economically as well as politically, can only get credit at between 25 and 30 percent; consumer credit in both France and Italy runs above 30 percent. In an area like the Mezzogiorno [in southern Italy] you have a potential for social unrest which may lead to quite a few surprises this summer. The lira went down during the past half-year or so from about 750 lira to the dollar to 1,150 now, and inflation is at 20 percent.

In West Germany the interest rate doubled from around 5 percent six or seven months ago to 12 percent today. But again, you cannot take these figures in strict economic terms. In West Germany there is a special situation, because you have to consider also East Germany, which has no unemployment to speak of. It is simply not possible politically for West Germany to increase its unemployment to 2 to 2.5 million—we simply cannot cut the social expenditures and unemployment benefits. There are very real political factors which have to be taken into account.

Let me review it from another side. Suppose you have a West German depression—and right now things are heading in that direction. That is the best way to destabilize the southern flank of NATO in a matter of weeks or months. We have around 2 million Turkish guest workers and their families in West Germany. And in a depression those Turkish guest workers are going to be the first to be fired. Just think about the Turkish situation and its importance to the NATO southern flank—and this is bad enough—and add to this hundreds of thousands of Turkish guest workers migrating back to Turkey. Then you get a very interesting idea of what the situation on the southern flank of NATO is going to look like.

Now let me proceed to another European country, which is Great Britain, since I think we can learn most from the situation there. Thatcher started with the monetarist high interest-rate policy even before Volcker.

There has now been a two-year time period in which to test the alleged effectiveness of the monetarist policy. The result is that the economy is worse than ever before and that British defense capability is significantly reduced. What the British government is advocating openly now is dumping the procurement of military equipment of an advanced technological level in favor of "clever designs" to substitute for high technology.

Anybody who thinks that with an overall decaying and shrinking industrial base you can insulate certain relevant military areas is wrong—it simply does not work. State-of-the-art weapons systems—which the other side is moving toward—can only be produced with an expanding overall industrial infrastructure.

The second conclusion to be drawn is that the basis for having state-of-the-art military equipment is in-depth industrial regeneration and in-depth economic growth. Any notion of "sunset" and "sunrise" industries that defines the very hard-core skeleton of the economy as something obsolete is incompetent.

The third conclusion I would draw is that only on the basis of such a healthy and growing economy can advanced scientific research, R&D and advanced technologies necessary for national defense be achieved. Only on the basis of a healthy, growing economy—and a crucial feature of this is, for example, a civilian nuclear program—are research and development efforts in the area of plasma physics economically feasible.

When I spoke not too long ago with a prominent strategic thinker in Britain, he somewhat fatalistically declared that he expects in the course of the 1980s that the general tendency will be toward war, maybe general war. What he said was quite to the point. If the threat that a monetarist h

not done away with, then this kind of monetarist economic and financial policy will not only endanger external and internal security, but may actually get us into war.