EIR Economics

IMF and Soviets agree to bankrupt the U.S.

by David Goldman and Laurent Murawiec

The International Monetary Fund went to extraordinary lengths to ensure that press coverage of its Annual Report issued Sept. 12 would give the impression that the Fund expects a drastic collapse of the U.S. dollar in the relatively near future. In effect, the IMF staff has added the weight of its view to that of the majority of European bankers, who are disengaging from dollar operations as quickly as possible.

Both the International Monetary Fund staff and the European banking mafia appear to have converged with the financial strategy of the Soviet Union, which is accumulating dollar balances with the intention of dumping them for other currencies at the appropriate moment, according to Swiss financial sources. The Soviet attitude appears to be informed by what William Clark's old National Security Council staff believed was a plan to launch a "monetary Pearl Harbor" against the United States.

However, the dollar continued to rise, to another 11½ year high at the Sept. 6 Frankfurt fixing of 3.0272 marks, for reasons already stated in our Foreign Exchange article last week.

Although the dollar may come off some from such giddy heights, tight rates, a firm dollar, and weak metals could persist for a while, as long as we have the current "walk" on certain U.S. banks, rather than a "run" on the system.

September 14's 11⁹⁄₁₆ Federal funds rate is a red-flag indicator of the nature of the problem, i.e., the liquidity squeeze on the banking system and a general dollar shortage.

Another factor in the dollar's favor is the quiescence of the major Ibero-American debtors, meeting as this issue goes to press at the Argentine resort town of Mar del Plata. Wire service accounts received at deadline suggest that the Argentines have agreed to some terms acceptable to the International Monetary Fund. Although the nut will not be cracked as easily as the wire services suggest, the immediate threat of strong collective action by the debtors has for the moment receded. This does not convince the Europeans and Japanese that the crisis is abating, but it persuades them to take methodical rather than hasty steps to prepare for the worst.

The International Monetary Fund's efforts to stall major problems in the banking system merely convince depositors to move funds from offshore bank deposits slowly rather than quickly. The IMF's temporary success in containing the debtors contributes to an environment of slow-building liquidity pressures, and a strong dollar.

IMF sees 'abrupt collapse'

How brief the dollar's flight may be is, nonetheless, strongly indicated by the IMF's 1984 Annual Report. Here is UPI's report of the Sept. 13 IMF press briefing:

"The IMF warned Wednesday that any sudden collapse of the dollar could jeopardize world economies, even though some Third World nations have made surprising progress during the past year.

"High interest rates and the strong dollar attract both imports and investment from overseas, helping the economic recovery in the short run, but the 'bottom line' deficits in international financial transactions, a record $39 billion for the U.S. last year and nearly doubling this year, 'have disquieting implications,' the report said.

"'Abnormally high real interest rates hinder private capital investment and create major hardships for developing countries,' the report said.

"'The exchange rate developments lately . . . have produced a pattern that cannot be maintained' a staff member

added. 'They will produce at some time, one way or another, a correction. There is nothing inherently bad about that, of course, except if the correction came precipitously' [emphasis added].

"The concerns about an abrupt collapse of the dollar, which could accelerate the inflation rate and starve the country for credit, have been voiced before by Fed chairman Volcker.

"One staff director, who asked to remain anonymous, told reporters: 'The main concern expressed in the report is the continued strength of the U.S. dollar, ascribed in part to the strong U.S. recovery, relative to U.S. interest rates and in part, to less fully understood developments in market opinions' [emphasis added].

"Use of the words 'abnormal' when referring to high U.S. interest rates, and 'disquieting,' in reference to the U.S. deficit in financial transactions, were unusually strong language for the Fund.

"The report's language is negotiated among members of the Fund's executive board and calculated not to offend anyone—particularly not the Reagan administration, which won $8.4 billion in IMF support from a reluctant Congress late last year. . . ."

After such a strong "sell" recommendation by no less an authority than the International Monetary Fund, why should the dollar continue to rise?

First, the dollar is propelled upward less by market evaluations of its future prospects than by an outright, grinding shortage of dollars on the international markets, for reasons described above.

In addition, capital flight from strategically precarious regions is strengthening the dollar. According to Swiss sources, $2 to 3 billion shaved from Taiwan's trade surplus with the United States this year has stayed with U.S. banks rather than being repatriated. All over Asia, Chinese merchant families are reportedly shipping money to the United States, to the tune of perhaps $10-15 billion so far this year.

However, the ambivalence with which European bankers are watching the dollar's rise is evident in the terms of the new Mexican debt rescheduling.

According to Dow-Jones, a previously undisclosed aspect of the pact would allow non-U.S. banks to convert portions of their existing dollar loans—as much as $10 billion—into loans denominated in the banks' home currencies. This would push up the dollar because Mexico would have to purchase the U.S. currency to facilitate the swap.

The Mexican package could be a big factor benefiting the future value of the dollar, said Rimmer de Vries, chief international economist at Morgan Guaranty Trust. He believes the impact of the accord has already been felt on currency markets.

Since Mexico must take the proceeds of foreign currency loans and use them to purchase dollars, the temporary effect is to increase demand for dollars. However, at the same time, European banks are converting a significant portion of the asset side of their balance sheets to their own currencies. This hardly implies long-term expectations of further dollar strength; on the contrary, it is consistent with widespread European expectations of a spectacular dollar decline following the U.S. elections in November. At a more disturbing level, it raises the issue cited by Federal Reserve governor Henry C. Wallich, the U.S. central bank's principal liaison to the Bank for International Settlements in Basel: The high price of the American currency makes it increasingly unusable as a reserve currency. The Europeans prefer to shift to their own currencies for both funding and lending.

European bankers are trying to disengage as fast as they can from the dollar; if they replace their dollar loans by, e.g., sterling loans, they can get rid of dollar deposits and fund themselves instead in sterling deposits. The upshot is a growing disengagement from the apparently almighty, but almost unusable, American dollar.

Two ultra-secret meetings recently deliberated upon this subject. At the first, the main German, Swiss, and British creditor banks all agreed to push the "currency conversion" scheme on the debtors. The second, a debtors' group meeting, reviewed the scheme without enthusiasm, according to a well-placed London source, for the same reason that the European bankers promoted it: the debtors do not wish to accumulate non-dollar liabilities just as the dollar reaches its peak.

The Soviet role

According to a well-placed Swiss financial source, "The Soviets are preparing a major financial coup, like a gigantic corner on the dollar. And the key is whether they want Mondale in or can accept Reagan as he presently is. They have the means to collapse the dollar, and shoot Reagan down in flames without being detected: There are enough other reasons and other forces that could crash the dollar that financial markets would be a perfect screen for them, a smokescreen. And if they were discovered, so what? You see Reagan telling the American people that his policy has brought the dollar under Soviet control? He'd be finished."

Soviet bankers have been playing "a highly speculative game" on the markets, comments Wharton Soviet expert Jan Vanous. The Soviets are currently, deliberately *losing* money in their financial policy: While borrowing heavily on the euromarkets—at an annual rate of $8 billion—they instantly redeposit the borrowed money with the lender banks, losing on the margins, and keeping their deposits very short term. A new pattern emerged Sept. 12 with the first-ever Soviet European Currency Unit (ECU) loan, syndicated for the Soviet Foreign Trade Bank Vneshtorg by France's Crédit Lyonnais, $56 million at "very fine terms," market sources reported.

In short, Soviet bankers are in a position to dump several billions of dollars or more in a few seconds on any chosen D-Day. Geneva sources indicated that the outcome of the Reagan-Gromyko meeting scheduled for Sept. 28 may determine whether Moscow will use the financial weapon.