Foreign Exchange by David Goldman

A 'lenders' strike'?

The budget-busters are threatening President Reagan with capital outflows.

Congressional Budget Office director Rudolph Penner told a seminar held at the American Enterprise Institute in Washington, D.C., on Dec. 3 that the United States is now dependent on foreign capital inflows, and that matters could become extremely serious if inflows dry up. This is an argument first offered by Federal Reserve chairman Paul Volcker in July, and again as recently as last week; it was also the central thrust of the International Monetary Fund's *Annual Report* of September. The IMF warned of a "precipitous drop in the dollar" unless the United States took urgent measures to reduce its budget deficit, i.e., through unilateral disarmament.

Penner echoed the IMF's imprecation, warning that there might be "an international lenders' strike" and it "could be very serious business indeed." He added that the CBO is not forecasting such a development, but said that the reliance on foreign capital "poses a big risk."

At the same conference, Malcolm Fraser, former Australian prime minister, warned that international money managers were waiting to see if the administration cuts the deficit, arguing that they don't believe that the United States can go on spending more than it takes in year after year. "Heavy U.S. reliance on foreign capital is simply not a sustainable position," Fraser concluded.

The administration's spokesman at the affair, Council of Economic Advisors economist William Poole, rejected these warnings out of hand. It is wrong to say that the U.S. dollar can't remain high for the foreseeable future, Poole maintained, as long as the United States maintains a strong investment climate. He argued that those who insist the dollar will fall if no action is taken on the U.S. budget deficit and those who say the dollar will fall if the deficit is cut sharply, can't both be right.

The Council of Economic Advisors' position appears unchanged from its January 1984 *Economic Report to the President,* the thrust of which was to report the $100 billion per annum and up capital inflow into the United States as a permanent condition of financial life during the 1980s, and a major source of financing for the federal budget deficit.

Some administration economic advisors are less sure. One White House economist worries that a collapse of oil prices early in 1985 could spark a generalized banking crisis, and bring the dollar down in its wake. This perception is accurate, but too limited in scope. The post-winter collapse of oil prices will be flanked by 1) a rapidly declining American economy, 2) the worst of the post-harvest wave of farm bankruptcies, 3) rapidly falling U.S. commercial real-estate prices, and 4) the re-emergence with full vengeance of the Ibero-American debt crisis.

As long as the U.S. Federal Reserve System can play usurer to the world, there is no reason for the dollar, the vehicle for such usury, to decline. However, when the results of such usury undermine the financial institutions which issue dollar credit, the dollar's role as reserve and lending currency will disappear, perhaps in a matter of weeks, and the unprecedented weakness of America's trade balance will destroy the dollar exchange rate.

The oil price issue is central for one reason, namely, that a huge portion of the bloated debt structures of the past decade are based on an artificially high oil price. The most recent developments among the oil producers suggest that the oil price will fall sharply below the present $28-$29 level as soon as the winter is past.

Norway, whose price cuts last month prompted reciprocal British cuts and an emergency reduction in OPEC production quotas, is said to be on the verge of a further price reduction, under pressure from Norwegian oil customers. Rather than set prices during the week of Dec. 3 as expected, the Norwegian government delayed the decision until the end of December, "to avoid disruption of world oil markets."

Britain's national oil company, meanwhile, is reportedly on the verge of changing its own price system to match the so-called spot price, the daily-fluctuating price of the 10% or so of world oil consumption sold outside of regular supply contracts. This extraordinary measure would end the de facto cooperation of major oil producers with the OPEC group, and guarantee a plunge of world oil prices in its immediate wake.

The foreign creditors of the United States are, indeed, preparing a lenders' strike, but not in the form that Rudolph Penner's remarks might suggest. The British maneuver suggests a more devious, and more fatal, means of achieving the same result.