International Commentaries

Growing Likelihood of Early Financial Crisis

The threat of a catastrophic financial crisis, as a result of such factors as the U.S. current account deficit, the derivatives bubble, or the U.S. looting of other nations to prop up its speculative mania, is the subject of a number of commentaries in the world press.

Italy

Mario Platero, *Il Sole 24 Ore,* financial daily, Aug. 25.

The annual meeting of the U.S. Federal Reserve, opening on Aug. 25 in Jackson Hole, will debate the threat of a global financial crisis, according to correspondent Platero, who obtained copies of the speeches in advance. He reports that three positions will be presented: 1) Globalization presents no risk of global crises (Michael Mussa); 2) there is a threat of a global crisis, but it can be dealt with through "dollarization" or "euroization" (Paul Krugman); and 3) the threat is real and comes from the U.S. trade deficit, which could provoke a serious dollar crisis (Maurice Obstfeld and Kenneth Rogoff).

According to the third view, "A sudden adjustment of the U.S. current account balance could provoke a strong dollar devaluation, and the risk of a deep and rapid correction, according to our calculations, is very real." Obstfeld and Rogoff say that "now it is not too early to consider pre-emptive measures." Their timing, however, is wildly over-optimistic, as they warn of a run on the dollar and investment outflows *within the next five years.*

Germany

***Frankfurter Allgemeine Zeitung,* Aug. 25.**

"The ticking gold derivatives time bomb" could pose a "threat to the international financial system," writes the leading German daily, reporting on a study, "Gold Derivative Banking Crisis," published by the Gold Anti-Trust Action Committee (GATA). The study has been sent to the U.S. Congress.

The committee emphasizes that the decade-long fall of the gold price, while gold consumption has been much higher than gold production, can only be explained by a conspiracy involving both central banks and private financial institutions. The total volume of the gold derivatives market remains unknown, as many of these derivative contracts are being traded in the unregulated over-the-counter (OTC) market. But it can be estimated, says the GATA report, that "short" positions on gold—which include the obligation to buy gold at a future date—have already surpassed the equivalent of 10,000 tons of gold, about four times as much as the world's annual physical gold production. If the exposure of a large financial institution in gold short positions were to become public, this would trigger a panic buying of gold by other traders, thereby causing a dramatic price increase. This in turn could pose a threat to the international financial system. The sudden $84 per ounce increase of the gold price last September would be only a mild version of what could happen then.

Japan

"Japan Learns the Painful Lesson of Allying with a Bully," *Asahi Shimbun* on the Internet, Aug. 23.

"Japan bit the bullet for the U.S., by buying treasuries to maintain an alliance with the world's only remaining superpower," the article begins.

It gives a history of the enormous Japanese financial bailouts of the U.S. economy, since it "was afflicted with chronic 'twin' deficits in the 1980s." Cash-rich Japan "eagerly used its financial windfall to plug America's huge current-account and budget holes. Consequently, Japan became the largest of all creditor nations—at a price." This "mass investment in American securities that propped up the dollar and helped the United States maintain its economic supremacy left many Japanese investors badly burned."

The United States, with its massive budget and trade deficits and fragile dollar, was a financial black hole. "High interest rates fed by the gaping hole in the nation's account books were sucking in foreign capital, every bit of which was needed to fill the vacuum. As the dollar strengthened, the trade deficit kept ballooning. High interest rates kept the dollar artificially strong, but an abyss lay underneath."

The September 1985 Plaza Accord, the G-5 agreement to bring down the dollar against other currencies, began "the nightmare for Japanese investors in U.S. securities." Japanese investors in the U.S. were hit with mounting foreign exchange losses, as the yen was forced up against the dollar. Former Vice Minister of Finance for International Affairs Tomomitsu Oba, who helped David C. Mulford, U.S. Treasury Undersecretary for International Affairs, put together the Plaza Accord, said he had "feared the accord would force Japan to sacrifice its own money to facilitate U.S. hegemony. Oba's concerns were justified. . . . Oba later learned that the U.S. government had masterminded a strategy to lure Japan into playing a preconceived role to assist the dollar's soft landing."

Asahi quotes an anonymous senior Ministry of Finance official saying: "It was as if the Americans were trying to intimidate us into playing ball with them by warning us that we would be in serious trouble if the dollar collapsed. As the U.S. budget deficit was swelled because of massive defense spending, Japan—dependent on the United States for its security—had to avoid any serious dissension with Washington."

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