Emergency Presidential Statement on the Economic Crisis

Issued by
United States Labor Party
1976 Presidential Candidate Lyndon La Rouche

New Solidarity International Press Service

P.O. Box 1972 General Post Office
New York, New York 10001
Phone: (212) 279-5950
TWX 710-581-5679

May 1975

May 2, 1975

The magnitude of the liquidity crisis the world faces between now and the middle of this year overrules the wish of persons in political life to dabble any further in partial solutions or evasions of the issue at hand. We state the problem bluntly: unless we take appropriate measures within the next several days and weeks, the world monetary system will undergo the most thorough breakdown it has experienced since the seventeenth century. The extent of the crisis is documented below in quantitative form, and the necessary solution, formulated by U.S. Labor Party Presidential candidate Lyndon LaRouche in his call for the formation of an International Development Bank, is detailed below.

At this moment, there is no serious political grouping either in North America, Western Europe or the socialist bloc, whose operational view of the world economic crisis differs markedly from that presented here. Only indecision and the absence heretofore of a competent programmatic solution have delayed the emergence of this issue as the central topic of political deliberation.

Presidential economic advisor Alan Greenspan has acknowledged the existence of unstable fictitious capital. Behind Greenspan's warning against undue optimism concerning the prospects for recovery this week, sources close to Greenspan made clear, is a simple comparison of the international payments due through the middle of 1975, and the productive activity available to support them.

This week, the leading bank economists appended to their prediction of an "early recovery" in the U.S. sector a further prediction of an "early bust" to follow, projecting into the near future what must occur within the next two months. On the other side of the Atlantic, every political and business leader of standing is known to hold in contempt predictions of an economic recovery and various alchemical formulas offered to achieve it, privately or publicly.

For the first time in a decade, months have passed without a single contribution to the discussion of "international monetary reform" from concerned governments or financial institutions. As the International Monetary Fund moves towards its June Interim Committee meeting without an agenda, the character of the monetary thinking on the part of the leading U.S. financial circles is best characterized by their public decision to let Great Britain break open economically, as a "purely domestic affair."

Immediately the consequences of the world monetary crisis and the lack of competent response from government and financial circles internationally are visible in the 40 per cent annual rate of collapse of the U.S. industry and imports, and similar rates of economic deterioration throughout the advanced sector. Without remedial action the alternatives are two: a disorderly wave of bankruptcies surpassing any experience of the past century, or triple-digit inflation by the end of 1975. In either case, the level of output of the United States, Western Europe and Japan may be conservatively expected to fall to half of peak-1970s levels within the next several months.

Liquidity Crisis

We summarize the character of the international payments situation:

Through June 30, 1975, $115 billion in debt service obligations are due in external payments from non-financial corporations and national governments, against approximately $300 billion in world exports during the same period. In ratio form, payments on debt-service account equal almost 40 per cent of payments for actual goods and services across national borders, a debt-burden insupportable except through the issuance of new credit in the dollar sector at a speed sufficient to destroy the dollar as a currency.

Prepared by the Intelligence Staff of the International Caucus of Labor Committes, the figures cited above represent a highly conservative estimate based on estimations of outstanding Eurocurrency and other private international lending, and governmental debt, and upon projections of current trends in international trading volume and prices through the second quarter of 1975.

While the absolute volume of international payments on debt service account through June 30, 1975, represents a substantial but not striking increase over the corresponding period of the previous year, a number of factors place the current period in an entirely different realm of experience. First, international trade then absorbed the heaviest impact of world inflationary tendencies, as export prices rose by 44 per cent against a real volume increase of 9 per cent. While during 1974 debt service requirements were partially met through price increases in international trade, commerce has been affected by strongly deflationary price trends as well as absolute decreases in volume since the first of the year, in the most heavily-weighted sectors of trade, including energy, basic commodities, food and steel.

Secondly, the volume of publicly-announced international bank credits rose last year by over $28 billion, indicating a much greater actual rise in such credits. This year, such international lending ran at an annual rate of little more than $12 billion. Eurodollar banks, whose typical asset to capital ratio is about fifty to one, are not capable of meeting these needs. The only significant source of international lending during 1975 has been the international bond market, in which $3.1 billion in new issues were placed during the first quarter of this year, compared with $3.2 billion during the whole of last year. But the pool of funds behind this market has run dry and new issues have suffered a sharp decline in recent weeks, indicating that little relief will be forthcoming from this sector.

Finally, the availability of oil producers' funds as a source of new capital for international lending has declined sharply. According to Morgan Guaranty Trust, first quarter asset buildup of members of the Organization of Petroleum Exporting Countries amounted to only $9 billion, compared with $17 billion during the fourth quarter of 1974 and $55 billion during 1974 as a whole. Both declines in oil consumption internationally and direct and indirect price reductions in recent months account for this drastic reduction in oil revenues.

The components of international debt service due for repayment through June 30 are estimated in Table A, (see following page). An annual rate of $600 billion for international trade, compared with $770 billion during 1974, is considered a conservative projection of trends during the first quarter of this year.

Several national governments are already in default or on the verge of it. Neither from the commodity price side nor the refinancing side has there been an indication of a possibility of easing the $140 billion debt burden of underdeveloped countries.

To summarize the magnitude of the threatened liquidity crisis within the U.S. domestic sector itself, we employ the following rules of thumb:

For every dollar received by corporations during the second quarter of 1975, 48 cents will pay debt service.

For every dollar received by consumers after taxes, 33 cents will pay interest and principal on consumer debt.

For every dollar received by farmers in the same period, 90 cents will be required to meet debt service obligations.

This occurs against corporate liquidity positions which are four times worse, in terms of the ratio between current liabilities and cash or equivalents on hand, than in 1929.

New York City, one of the world's largest financial institutions (long term liabilities of $13 billion) and the backyard of the world's largest group of banks, is an exemplary case in point. By June 30, the City must roll over $2.2 billion in notes. Its total income during the same period is estimated at $2 billion. By arithmetical certainty, no level of austerity in the City budget can delay the City's insolvency. New York State, which bailed out the City in April by going to the capital market for a $400 million short-term loan on the City's behalf, cannot make a dent in the problem. Nothing short of a massive injection of Federal monies can delay the City's bankruptcy, and such a decision by the U.S. Treasury would be interpreted correctly as a political commitment to a policy of hyperinflation, with immediate disastrous consequences to confidence in the dollar abroad and at home.

Table B quantifies the magnitude of the liquidity crisis in the U.S. (see following page).

Noting that every corporation's account receivable is another corporation's account payable, the insupportability of these ratios without an unprecedented rate of new credit expansion is obvious. Indeed, the banking system has made clear through public statements and through the continued reduction of commercial and industrial loans that it does not intend to extend this measure of new financing. Furthermore, the Treasury's decision yesterday to raise $750 million in bonds and $9 billion in notes virtually ensures that all new bank credit will be directed to financing Federal debt, as banks buy Treasury bills in order to rebuild badly-damaged liquidity positions.

Bank reserves against expected loan-portfolio losses trebled between the first quarter of 1974 and the first quarter of 1975. This will not begin to cover the volume of loan losses which may be expected during the second quarter as a result of the liquidity bind documented above. Worst of all, banks now hold $80 billion in Certificates of Deposit which must be rolled over during the next 90 days. The cash requirement of corporations through June 30 on debt-service account alone is more than twice that amount. The current situation in bank liquidity, in which two of the country's seven largest banks hold real estate investment trust loans greater than their shareholders' capital, cannot bear such a rapid drawing down of Certificates of Deposit.

Within the U.S. sector and internationally, the question of debt moratoria on a gigantic scale has already been settled by the application of generally-accepted accounting procedures. Either a crushing proportion of dollar (and other internationally circulated) assets must become bankrupt or the currency itself will be destroyed.

As Alan Greenspan is acutely aware, a crunch in both international and U.S. domestic payments during the first quarter has been avoided only at the expense of production. A reduction of industrial output ranging from 10 to 20 per cent (compared with previous-year levels) in most national sectors has made all available incoming revenues of corporations available for the payment of debt service. This has merely aggravated the inevitable crisis at the end of the second quarter, when a wide range of payments come due. As a general rule, austerity imposed upon the productive sector in order to sustain payments to the non-productive sector rapidly erodes the basis of future payments.

(Estimates for the above tables are based on data from the Federal Reserve Bulletin Statistical Abstract of the United States, the Quarterly Bulletin of the Bank of England, the Quarterly Survey of Manufacturing, Mining and Trade Corporations of the Federal Trade Commission and World Financial Markets, published by Morgan Guaranty Trust).

The Solution

The conclusion from the above analysis is self-evident. To prevent a general collapse of economic activity, two steps are immediately required:

Table A

INTERNATIONAL DEBT SERVICE, FIRST HALF 1975

Interest and Principal on international bonds	$ 4 billion
Eurocurrency short-term debt (excluding interbank)	70
Service of medium-term Eurocurrency loans	10
Government-to-Government debt service (including international institutions	5
International lending of U.S. banks	1
Debt service on international trade	25
	$115 billion

Table B

1) Corporate debt (non-financial corporations)

Due to banks	$ 43.0 billion
Due in maturing commercial paper	7.4
Due in other short term loans	17.0
Due on debt securities	10.5
Interest on trade accounts	13.0
Due in sales and excise tax	59.8
Due in income tax	36.0
TOTAL	$186.7 billion
Non-inventory accounts receiveable (adjusted for first quarter 1975 sales declines projected through second quarter)	$390 billion
Debt obligations + income	48 per cent

2) Proprietors' farm debt

Short-term obligations	$ 13.80 billion
Mortgage payments	1.56
TOTAL	$ 15. 36 billion
Farm income, 2nd quarter 1975 (projecting rate of decline from 4th quarter 1974 to 1st quarter 1975 through 2nd quarter)	$ 16.9 billion
Current income + current debt	91 per cent

3) Consumer debt

Consumer debt due 2nd quarter (estimate)	$ 64 billion
After-tax disposable personal income (adjusted for unemployment, less foreign transfer payments and rate of personal savings projected downwards)	$192 billion
Current income + current debt	33 per cent

removal of the fictitious debt burden from production, and a sharp increase in productive output. The appropriate format for this program was outlined by U.S. Labor Party candidate LaRouche at a widely-observed press conference in Bonn, West Germany, April 24.

The United States Labor Party and the International Workingmen's Association propose three immediate steps to satisfy these general requirements during the period ahead:

1) An immediate moratorium for a two-year period on the payments to the unproductive sector listed above.

2) The pegging of European and Japanese currencies to the Transfer Ruble of the Council for Mutual Economic Assistance as a means of ensuring orderly currency conditions.

3) Immediate tri-partite negotiations between the advanced sector, the socialist bloc, and the underdeveloped countries for the creation of an International Development Bank.

Our task is not to institute debt moratoria, which are instituting themselves rapidly enough, but to institute them in an orderly fashion in order to free all available funds for production. Holders of debt may ask themselves whether they wish to insist upon immediate payment upon their assets and receive a nickel on the dollar, or suspend debt service for a delimited period. As LaRouche has emphasized, at that point, the population may decide through democratic means whether to resume payment of debt service or not.

From the standpoint of production, not one penny of the debt service payments listed above can be justified. The banking system has withdrawn from the business of financing production; its sole concern at this point is to juggle debt.

Once this noxious burden is removed, new credit may be issued directed towards specific productive goals. Drawing upon the U.S. Labor Party's extensive body of published material on reversing the collapse of production and eliminating the immediate threat of mass starvation, we present the following credit requirements for the first year of an international production-based credit program:

10 million tractors	$ 70 billion
Conversion of 50 per cent of auto industry to tractor	10
Fertilizer production (170 million tons)	17
Chemical plant expansion	8
Desalination equipment	3
Pumps, 40,000 cum/sec capacity	1
Electric generators, 3 million kw	1
Construction equipment	6
Transportation equipment and related infrastructure	5
Sub-total for agricultural development	$121 billion
Oil and Gas development	$ 5 billion
Steel plant and equipment	2
Machine tool production	15
Defense Industry Conversion	10
Cement Industry Expansion	5
Building Materials Industry Expansion	18
Fusion Power Development	3
Sub-total for non-agricultural production	58
GRAND TOTAL	$179 billion

Once unproductive debt is suspended, the total volume of new credit required to revive production internationally represents less than the corporate debt within the next three months in the United States alone. The above credits will accomplish the worldwide development tasks which the U.S. Labor Party has identified in prior public statements.

The immediate targets are the agricultural development of the Rio de la Plata region of Latin America, the Ganges-Brahmaputra river basin of the Indian subcontinent, the Sahel region of Africa, and the Fertile Crescent of the Middle East. In addition, the funds will be provided for the mechanization of Soviet agriculture and the immediate upgrading of North American and European agricultural production to maximum-capacity levels. Depending on the speed at which this program is implemented, the product of this program will be the expansion of food production by 50 to 100 per cent during the next year. In eliminating hunger during the next three years, and raising the world's living standards to Western levels within the next decade, Western industry will have sufficient work in sight to return almost immediately to full capacity utilization.

Financial arrangements for this program must be settled upon by participating nations and instructions passed on to the Directors of an International Development Bank. Subject to negotiations, the general format of the International Development Bank's operations is nonetheless clear. Member nations will subscribe to the Bank's capital stock according to negotiated quotas, in a "reserve ratio" appropriate to the creation of assets of close to $200 billion during the first year of operation. Two circumstances enable the International Development Bank to create this volume of long-term credit: first, the regeneration of economic activity through such credit issues will exercise a profoundly counter-inflationary effect on the world economy; secondly, new credit issues by the International Development Bank will replace the present counter-productive debt structure in the field of international and domestic payments, so that the actual ratio of outstanding credit to production will decrease sharply.

On this basis, actually-trivial questions such as currency arrangements settle themselves. Once the U.S. sector sheds the burden of a portion of $5 trillion in outstanding debt, new investment in dollars will represent real and expanding value. A firm relationship between the dollar and a European-Japanese link to the Council for Mutual Economic Assistance's Transfer Ruble can then be set through negotiations.

Apart from long-term credits, as the LaRouche proposal outlines, the Bank will provide a discounting facility for bills of exchange in international trade. Once the international debt burden weighing on world trade has been pushed aside, this facility can create funds as the need arises, using procedures detailed in the U.S. Labor Party's "Brief on the Euro-Ruble."