

Paul Volcker is a thug

Behind the Fed nominee's prodollar pose

Within hours of President Carter's nomination of New York Federal Reserve chief Paul Volcker to replace G. William Miller as head of the Federal Reserve System, a soaring U.S. stock market had registered the gullibility of American businessmen. The international response, however, appears to be informed by longer memories about the man the *New York Times's* Clyde Farnsworth has anointed "one of the most skilled monetary tacticians of the age."

While Mr. Volcker's more recent distinctions feature his repeated public assertions that G. William Miller has been too "lax" on the credit reigns, it is without doubt his earlier educational and financial-government career that is the basis for the skeptical international assessment of President Carter's "conservative" choice. European and Japanese leaders—and in particular former Finance Ministers Giscard and Schmidt—gained an intimate knowledge of "Volcker policy" in eyeballing sessions that featured then-Treasury Secretary John Connally during the August 1971 dollar crisis, when the British and their domestic stooges conspired to force the dollar off gold and drive American world economic leadership to its nadir in a rampage against Europe and Japan. Contrary to the *Wall Street Journal* editors' attempts July 26 to underline his "fairly small role" in the 1971 disaster, it was in fact Undersecretary for Monetary Affairs Paul Volcker who prepared the script and did the coaching for the acknowledged "quick study" Connally.

A summary review of this and other highlights of Volcker's career will show that, beneath the cultivated pose of a shrewd, soft-spoken New York financier—a "conservative"—the hulking Mr. Volcker, perpetually sucking on a thick, dark cigar, carries the proven credentials of an overgrown thug for the dirtiest and most immoderate of British political and financial policies and methods.

Education: in the Royal Fabian tradition

Educated at Princeton and Harvard, Paul Volcker's training was critically augmented in 1961 with a year at the London School of Economics, the British Fabian bastion, where he studied the United Kingdom's post-war monetary policy which centered around containing the dollar and U.S. trade and investment. In 1962, Volcker was funneled into the Kennedy Treasury Department, where he worked under the general tutelage

of Undersecretary for Monetary Affairs Robert Roosa during the latter's conversion to SDRs as a replacement for the dollar. In 1963 Volcker was promoted to Deputy Undersecretary to Treasury Secretary C. Douglas Dillon. With Lyndon Johnson's election in 1964, Volcker left the Treasury and in 1965 returned to Chase Manhattan Bank, where in 1957 he had been a "financial economist," this time as "Vice President for Forward Planning."

Interestingly, it is 1967, midway in Volcker's second Chase tenure, that a policy manifesto entitled "Gold and the Dollar" appeared in the year-end *Foreign Affairs* magazine under the joint byline of two otherwise unremarkable Chase Manhattan officials. Billed as the ultimate defense of the gold-exchange standard, this policy statement in every significant detail prefigured the actions taken under Volcker's guidance on August 15, 1971 and afterwards to destroy the gold-exchange standard—to break the link between the dollar and gold, and move toward what the manifesto refers to as a "new source of international liquidity." This is standard parlance for the British plan, pushed since at least the early 1960s, to replace the dollar-gold exchange standard with a reversion to John Maynard Keynes's scheme for a "world central bank" greased with "paper gold" Special Drawing Rights, rejected at Bretton Woods thirty-odd years ago.

Volcker gets his chance

With the Nixon victory in 1968, Paul Volcker was plucked from Chase Manhattan and installed as Under Secretary for Monetary Affairs in the Nixon Treasury Department. From at least the time that Nixon began tying the noose around his political neck—marked by the appointment of John Connally to take over Treasury to deal with a deepening domestic and international economic crisis whose dimensions and implications Nixon never succeeded in comprehending—Paul Volcker had immediate control of American foreign economic policy.

Both Connally and Peter Peterson, ferried into the Nixon White House in January 1971 as the Assistant for International Economic Affairs, were tutored by Volcker. It was Volcker who directed staff work in the Treasury Department from at least the beginning of the year to fashion and organize support for a dramatic new "get tough" policy for the dollar, and it was

Volcker who directed the select group to move into high gear as early as July to hammer out the exact steps ultimately announced on August 15: (1) shut the gold window; (2) throw up an import surcharge; (3) demand revaluations and other political and trade concessions from Europe and Japan as the price of relief from the disastrous effects of steps (1) and (2); and (4) begin the "long process" of negotiating "international monetary reform" based on, in Volcker's own words, an "orderly dwindling of the role of gold."

Critical assistance

Mr. Volcker was not left to implement his plans single-handedly. In fact, on two crucial occasions, he received absolutely critical assistance. First, on Aug. 6, 1971, Henry Reuss's international financial subcommittee of the Joint Economic Committee, under ranking Republican member Jacob Javits, leaked a report calling for the U.S. to float the dollar off of gold. An unprecedented dollar-dumping binge was predictably triggered. The situation was desperate, but not yet hopeless. Despite attempts to hype up alleged massive French demands for U.S. gold, a credible pretext for shutting the gold window was still lacking.

Then, on or about the morning of Friday the 13th—a little touch of black humor which afforded the London *Economist* editors a rich snicker—Britain cabled the U.S. Treasury and demanded \$3 billion worth of gold. It was this astonishing action which by all accounts forced the Camp David decision to junk the dollar-gold link.

Transcripts of the emergency August 15 meeting show that here Connally premiered his soon-to-become-infamous bully routine, this time for the benefit of a caged and credulous Nixon. It was also the occasion for Paul Volcker to debut his quiet, "conservative," I-must-reluctantly-agree routine. Volcker argued not only that the gold window must be shut, and hard bargaining with Europe and Japan commence on that basis immediately, but that to preempt speculation in gold the U.S. should sell some gold and in other ways "demonstrate that gold is not that important."

Mutt and Jeff

By the time Americans had heard Nixon's extraordinary August 15 address, Paul Volcker was on his way to Europe, stopping first to chat with British Finance Minister Lord Barber, and continuing on to the continent to commence the extortion proceedings. With Connally routinely obliging the press with headlined demands and threats at successive meetings and press conferences, Mr. Volcker proceeded to gain credibility as the accommodating antidote to the avowed maniac Connally—a hoax which ought to be loudly exposed once and for all.

The climactic moment at one of the late 1971 Group of 10 meetings in Europe—widely cited as indicative of Mr. Volcker's winsome playfulness—reveals the crux of the Mutt and Jeff act that Connally and Volcker perfected against Europe and Japan. Volcker provocatively challenged European and Japanese persistent resistance to revaluation, suggesting "hypothetically" a U.S. devaluation of, say, 10 to 15 percent. Connally, chairing the meeting, reportedly picked up the idea, proposing a formal discussion beginning with a 10 percent U.S. devaluation. The predictable silence descended, and exasperated finance ministers were left to cable desperately back to their governments for further instructions. (As chronicler Robert Solomon noted, Volcker would have preferred to start the discussion at 15 percent—Connally was quick, but not that bright.)

U.S. relations with Europe and Japan have never recovered.

The "Volcker plan"

But fracturing ties with America's allies was not an end in itself—the policy content in this madness was elaborated increasingly as the hostile stalemate between a severely compromised Europe and Japan and the Anglo-Americans gave way to the post-Smithsonian agreement sideshow of "international monetary reform" negotiations during 1972 and 1973.

The centerpiece American proposal for the Group of 20 deliberations which began in the fall of 1972 was known as "the Volcker plan." As Robert Solomon pointed out, the "Volcker plan" bore "a striking resemblance to the Keynes plan of 1943." Volcker would simply substitute the IMF for Keynes's "clearing union" and the SDR for Keynes's "bancor." Solomon further notes that Mr. Volcker was proffering a plan on behalf of the United States in 1972 which the United States had rejected outright in 1943.

That epitomizes the ironies surrounding the career of the "conservative" Mr. Volcker. By mid-September of 1971, the *New York Times* was forced to comment on the apparent anomalies of America's foreign economic policy and its sponsors. "Mr. Volcker is an extremely loyal servant of the President," the Times intoned, and one of the most vociferous spokesmen against the "concept of flexibility of currencies." In February 1969, after taking office, he said that wider fluctuations had been discussed in academia—and they could stay there. In June 1971, testifying before the Joint Economic Committee, he sharply opposed Reuss's proposal to cut the gold link and float the dollar. "And yet," sighed the *Times*, "according to reliable reports circulating here, Mr. Volcker was the principal architect of the President's new economic structure."

—Susan Cohen

Volcker's endorsement of controlled disintegration

In the Nov. 9, 1978 Fred Hirsch Memorial Lecture at Warwick University in England, Paul Volcker outlined the necessity of having the International Monetary Fund "manage" a world economy in which the dollar would be phased out. New York Council on Foreign Relations economist Fred Hirsch wrote the Council's Project 1980 economic sections before his recent death.

Volcker's speech, excerpted below, was published in the January 1979 issue of the London monthly The Banker.

...I was tempted to take as my text today one of Fred Hirsch's last dicta: "A controlled disintegration in the world economy is a legitimate object for the 1980s. ...". The phrase captures what seems to me the prevailing attitudes and practices of most governments in this decade, as they struggle with two central issues that bedevil so much of our negotiations and our actions, not just with respect to money, but over the full range of international economics. ...

...The United States no longer stands astride the world as a kind of economic colossus as it did in the 1940s, nor, quite obviously, is its currency any longer unchallenged. Now, other centers of strength and power have arisen in the industrialized world, and they will need to share in the leadership. Developing countries have a new economic importance and political consciousness of their own.

...Let us be aware of the difficulty of controlling disintegration, once fairly started. ...

I do not suggest that we stand on a knife's edge, forced to choose between integration and autarchy. But I would much rather take as my rallying cry, as a focus for necessary negotiations, as an ideal from which to measure progress, the challenge of "managing integration" rather than disintegration...

...The happy days of Bretton Woods, often viewed today with nostalgia, were a special case, workable because of a particular economic and political setting.

It was symptomatic that hardly were the last books on the "dollar shortage" published than new authors set to work on the "dollar crisis." Triffin, as early as 1959, only a year after the restoration of European currency convertibility, produced the classic description of the ultimate fallacy of operating a system on the basis of increasing use of a convertible reserve currency. The "Triffin dilemma" inspired a long collective effort to reinforce the system by creation of a new international reserve asset....

The system held together for a decade and more after the first signs of weakness, despite the resistance to more fundamental adjustment measures....

But in the end, the inherent contradictions in the system were too great. With the benefit of hindsight, it would seem that an erosion of the United States competitive position was implicit in the postwar arrangements. First Europe and later—with even greater momentum—Japan brought its industrial capacity and efficiency close to United States standards. It took some 20 years, but eventually the United States payments position was irreparably undermined....

Finally, in August, 1971, the United States did move decisively to promote the adjustments that seemed necessary...

...Mr. Connally's manner may have grated some foreign (and a few domestic) ears, but it was no mean feat to manage a devaluation of the proud dollar in a way that did not turn American opinion and policy inward....

...We have had plain enough warning of the fact that international money, any more than domestic, will not manage itself. It will deliver neither the promised autonomy nor integration if we fail to deal with some of those issues that were unresolved in earlier efforts at more structured reform....

As Fred Hirsch emphasized some years ago, the transition toward a European system could pose difficult problems. I hope we will all be alert to dealing with the complications that the transitional period could present for international cooperation on a wider scale, to protecting the legitimate role of the IMF, and to the implications of decisions within Europe for the monetary system as a whole....

All of this raises questions of governance—if the system is to be managed, who will do it and how. The obvious institutional focus is the IMF, and it plainly has a full plate of work ahead. I have long felt that, if that work was to proceed with full effectiveness, the effort of the international bureaucracy—however able—and it is very able—needs to be reinforced by more active regular participation by politically responsible officials of member governments. That is, of course, the rationale of the council authorized by the new articles. To a degree, the function has been performed on an interim basis by the advisory council. But it would seem to me useful, more than symbolically, for that body to assume now full legitimacy by transforming itself formally into the council, and renewing the sense of commitment to develop its surveillance function [along with] more or less continuous consultation among the "trilateral" countries: Japan, Europe, and the United States. And the consultation must extend to the highest level. The recent practice of "economic summitry" points that way.