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International Aid, Debt, and Inflating

The less developed countries are urging the industrialized countries to meet next year to "solve" the pressing debt problem of the poor nations. Various aid schemes, all closely resembling those proposed in the past by the Trilateral Commission, have been proposed. Although the IMF and other international agencies may "assist" the poor nations to overcome the immediate threat of loan defaults, the long-term effects of the proposed "solutions" will be against the interests of both the "aided" people, making them an international welfare class, and the "aiding" people, whose own well-being will be retarded and whose social order will be threatened.

During a recent meeting at the United Nations, Third World member countries that had organized as the "Group of 77" called for the convening of a conference in January 1981 to discuss a number of issues. Specifically, the Group of 77 wants to work out a plan with the industrialized nations that would, by means of various transfer mechanisms, relieve the less developed countries (LDCs) of their international debt burdens, dampen the impact of high fuel prices on their economies, and stabilize the price of the LDCs' commodity exports. The Group of 77 proposals will seem familiar to those aware of the ideas propounded by the Trilateral Commission during the past 7 years, ideas that we discussed in *Research Reports* for May 17, 1980.

Ostensibly to aid the Third World countries, the following recommendations, among others, were made in several *Triangle Papers* published between 1973 and 1976: the IMF should sell gold at market prices, with the "gains" to be used for low interest loans to LDCs; more direct financial assistance should be given by the industrial nations and OPEC to the LDCs; and cartels should be formed for stabilization of commodity markets to prevent fluctuations in the earnings of the LDCs. In 1975 the International Monetary Fund approved the sale of 25 million ounces of its gold stock over a 4-year period beginning in June 1976. The last IMF auction was held in May 1980, and the Fund still holds 100 million ounces of gold. Some IMF officials and economists think this gold should be utilized in connection with a "substitution account" that would enable central banks to exchange unwanted U.S. dollars for foreign currencies or even for gold. These "excess" dollars accumulated by the IMF could be passed on either in the form of low-interest loans or outright grants to Third World countries having substantial balance-of-payments deficits. Of course, private commercial bankers would welcome this international "bailout" of their troublesome loans to Third World countries. At the American Bankers Association meeting last spring, top officers of many major banks called upon the IMF to play a larger role in lending to the LDCs.

These proposals form the core of a recurrent theme of the Trilateral Commission's *Triangle Papers*: the creation of a "new international economic order." In the final analysis, this "order" is based on the notion that a centrally designed and coordinated plan is needed "to assure the smooth management of interdependence" that the world economy now faces. This is the notion the Group of 77 repeats as its aim: The "only real solution . . . is the establishment of a new international economic order."

Who Is Aided?

One of the accepted notions regarding the relationship between the so-called rich industrialized nations (the "North") and the "poor," less developed countries (the "South") is that aid from the North is required if the South is to advance economically, if the gap between the "rich" and "poor" is to narrow or at a minimum not to widen, and if peaceful relations are to be achieved between the North and the South. P. T. Bauer, Professor of Economics, London School of Economics, has criticized for many years in numerous books and articles the argument that foreign aid helps the people of poor countries to advance economically. Professor Bauer has pointed out that much Western aid has gone to oil-rich OPEC countries, which can hardly be classified as poor in relation to other Third World countries.

Furthermore, aid has been granted to governments that have used funds in ways that have contributed significantly to the plight of their own citizens. Foreign aid has forced collectivization of farming in Africa, has funded the expulsion of ethnic groups (Idi Amin's treatment of Indians in Uganda in the early 1970's) who had constituted a substantial segment of the entrepreneurial and managerial class, and has enabled governments to impose restrictions on trade and flows of capital. Much aid has supported violations of the principles of the free market and the property rights of individuals. After governments, primarily one-man or military dictatorships, thus have stifled the marketplace from functioning and their people have been deprived of the opportunities to produce and trade the goods and services that would increase their standard of living, more aid has been requested to stave off even worse conditions.

Do-good international bodies, like the International Monetary Fund, the World Bank, and the United Nations,

EXPANSION EVEN MORE PROBABLE

Constant-dollar personal income originating in manufacturing industries now is appraised as clearly expanding. This change raises from 60 to 80 the percentage of primary coincident series expanding cyclically. This more forcefully suggests that the recession has ended (probably in July). The primary laggers, however, do not yet confirm the business-cycle expansion indicated by the statuses of the leading and coincident groups.

funded largely by Americans, have implemented programs that perpetuate the "vicious circle of poverty" gripping many of the LDCs. According to Professor Bauer, foreign aid will not improve the economies of the LDCs. He bases his assertion on the observation that all of today's developed countries began as underdeveloped countries and "progressed without foreign aid." The reason? According to Professor Bauer, "if all conditions for development other than capital are present, capital will soon be generated locally, or will be available to the government or to private businesses on commercial terms from abroad." But *if the "conditions for development are not present,* then aid . . . will be necessarily unproductive and therefore ineffective." [Emphasis added.] In plain language, if indigenous populations do not have the attitudes, education, and tools, coupled with social and political institutions providing for individual expression, the inflow of foreign aid probably will not achieve the desired goal of higher aggregate income, and if those aspects are present, the aid will not be needed.

The accuracy of this observation is supported by demands of Third World countries now for aid to ease their economic plight, even after they have received substantial foreign aid from the industrialized countries and international agencies. Brazil's foreign debt by the end of 1980 is expected to be $60 billion, and the possibility that Brazilian private and public borrowers may not be able to meet their repayment of principle or interest looms large. U.S. commercial banks have been in the forefront in urging the IMF to insure the banks' loans to the less developed, oil-importing countries. Inasmuch as U.S. banks hold approximately 36 percent of Brazil's outstanding debt, the bankers understandably are concerned about Brazil, and about other similarly over-indebted countries. The Trilateral Commission, composed of international bankers, academics, industrialists and other individuals with conflicts of interest, has made numerous proposals to alleviate the financial burdens of the Third World. Of course these plans also would help the balance sheets of the private institutions that have loaned billions of dollars to the Third World.

The "new international economic order" is based, in the final analysis, on centrally planned economic decision-making. As Professor Bauer cogently observes in *Dissent on Development*: "Comprehensive planning does not augment resources. It only concentrates power." Furthermore, "The state cannot create new additional productive resources. The politicians and civil servants who direct its policy dispose only of resources diverted from the rest of the economy." In spite of clear evidence that domestic welfare programs have failed to significantly reduce poverty in the United States and in other countries, central planners seek to have the IMF and World Bank become primarily international welfare agencies. Of course, the sums involved are much higher; world poverty is much greater.

Postponing Solutions, Promoting Problems

The total debt of the non-oil producing countries is nearly $400 billion. In order for the LDCs to repay principle and interest in real value (as differentiated from depreciated paper value) over the next few years, their economies will have to grow substantially. This will be a Herculean task. It is almost a certain impossibility, in part because their economies are shackled by controls and central planning. The more probable avenue of escape for LDCs is a financial rescue by international agencies.

As we described earlier, the creation of a substitution account within the IMF would be one method for continuing to "aid" the Third World. Another possibility is for the IMF to guarantee loans made by private commercial banks to the Third World, using as collateral the 100 million ounces of gold still held by the IMF (having a current market value of $70 billion). Continued loans or grants could enable the LDCs to manage their debt repayments over the next few years; however if the LDCs' oil and finished products imports continue to exceed the value of their exports, the current problems will simply arise again later. How then will the problem be handled? Might not the gold held by the IMF (but owned by the people of the member countries) end up in the vaults of the private bankers?

But that outcome is not the only way by which the people of the industrialized countries may be made to bear the cost of "aiding" the Third World leaders. At any given time, only a given amount of funds are available for loans. If international agencies make first claims on these funds for loans to otherwise uneconomic Third World activities, potential private commercial and industrial borrowers would be "crowded out" and investment and economic growth would be retarded.

Just as evidence points to the failure of social welfare schemes at the national level, so also does evidence indicate that borrowing requirements of governments (in order to fund budget deficits) tend to foster inflating because of pressure to avoid "crowding out." Moreover, social welfare spending has not appreciably reduced "poverty" domestically, and foreign aid has harmed the foreign people. However, excess domestic spending has promoted inflating, and international aid almost surely will do likewise.

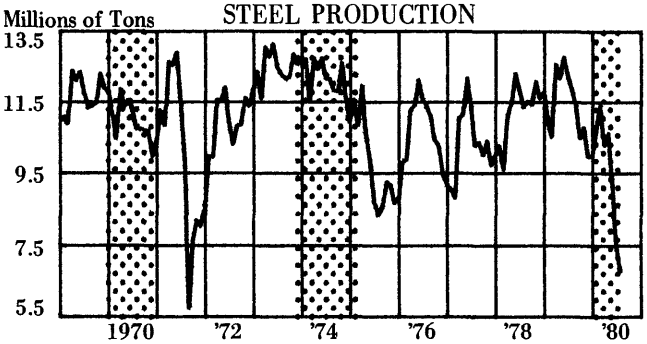
The intent of the proponents of international aid schemes is inconsequential insofar as the economic effects of the programs are concerned. Whether supportors of aid simply want to concentrate power for their own benefit or sincerely wish to help the "poor" countries, international aid probably will impede economic progress in both the "aided" and the "aiding" countries, while at the same time, by fostering inflating, it will tend to undermine social order in the advanced countries. Hardly can a more pervasively destructive scheme be imagined. Yet, the probability is high that it will be increasingly implemented in the months and years immediately ahead – all for the "good" of the poor.

STEEL PRODUCTION, USES, AND PRICES

Steel production for the first 7 months of 1980 has decreased sharply, as have steel shipments, new orders, and capability utilization. Some signs of future improvement are apparent, however: No. 1 steel scrap prices have increased for 2 months in succession, the downward spiral of U.S. auto sales and production seem to have ended, and general economic activity apparently has begun to expand.

During the first 7 months of this year, 49.3 million tons of "raw" steel (ingots, castings, and other first-stage forms of steel) were produced in the United States. This was 24.5 percent less than total steel production for the same period last year. During July 1980, domestic steel companies produced 6.8 million tons of steel, a monthly low for this cycle; in fact, output during July was the lowest monthly volume since August 1971, when 5.7 million tons were produced during a labor strike. During the 1973-75 recession, the monthly low volume of steel production was 8.4 million tons during July 1975. As Chart 1 shows, monthly steel output peaked for this cycle in May 1979, when 12.8 million tons were produced, trended downward through

Chart 1
STEEL PRODUCTION



December, increased during January and February, but has trended sharply downward since then.

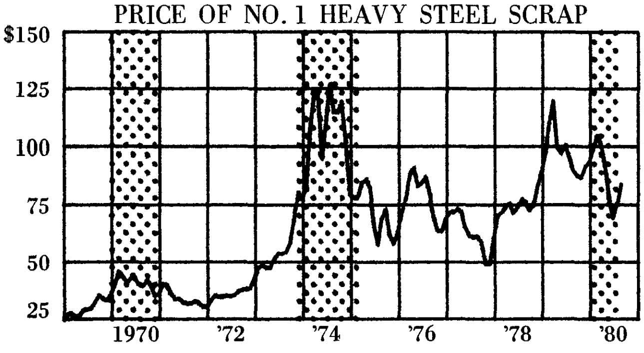
Net shipments of steel mill products by domestic producers peaked for this cycle in March 1979 at 10.3 million tons. Net shipments declined to 7.9 million tons during September 1979, increased slightly to 8.7 million tons during February 1980, and declined sharply to 5.4 million tons during July 1980. From the cyclical peak in March 1979 to the new low for this cycle in July 1980, net shipments decreased 52.4 percent.

Steel mill inventories increased to a record volume of 11.7 million tons in May 1980, having trended upward to that level from a trough of 8.7 million tons in March 1978. New orders for steel mill products, after reaching a peak for this cycle in January 1979 of 7.6 million tons, were down sharply to 3.4 million tons in May 1980 (the latest month for which data are available).

Although all currently available steel industry data indicate deterioration through July, more recent pertinent data suggest that July might have been the worst month for this cycle. As is shown in Chart 2, the composite price of No. 1 heavy melting steel scrap, as reported by *Iron Age*, reached a low for this cycle of $69.70 per ton in June. That price was 58 percent lower than the March 1979 peak for this cycle of $119.75 per ton. In the 1973-75 recession the price of scrap fell from a peak of $124.37 per ton in April 1974, to $58.00 per ton in July 1975. Since the June low of $69.70, the price of scrap has increased for 2 consecutive months, to $84.42 in August. Scrap steel is often accumulated in anticipation of future increases in production, and this accumulation is reflected in higher steel scrap prices. Thus, the 2-month increase in such prices may indicate that steel producers see some signs of improvement and are more optimistic about future production.

The decrease in sales of domestic automobiles has had a major adverse effect on steel shipments. Since 1973, the auto industry has received an average of 19.8 percent of

Chart 2
PRICE OF NO. 1 HEAVY STEEL SCRAP



total steel shipments. In November 1976, steel shipments to the automotive industry as a percentage of total monthly steel shipments peaked at 26.2 percent. In May 1980, 12.1 percent of the steel shipped went to the auto industry. In the 1973-75 recession, steel shipments to the auto industry troughed in March 1975 at 11.5 percent. If the recent improvement in the domestic automobile industry is extended in duration and magnitude, steel production may well have reached its cyclical low in July and now be on an upward path. If, however, the recent increases in U.S.-make automobile sales are only temporary, the steel industry may languish for some time. According to the statuses of the statistical indicators of business-cycle changes, recent advances probably are more than temporary, which implies that the steel industry also will improve cyclically during the coming months.

TPM: Protectionism

An important development for consumers and for the long-run future of the domestic steel industry is the anti-dumping suit filed by U.S. Steel Corporation on March 21, 1980. The suit is against 16 European steel producers in 7 European countries. Six hours after the anti-dumping suit was filed, the Commerce Department suspended the Carter administration's Trigger Price Mechanism (TPM). The TPM was first instituted in May 1978 as a method of avoiding large numbers of anti-dumping suits, which had proven to be costly for the Government and the industry. ("Dumping" refers to foreign sales of steel to U.S. customers at prices below the estimated cost of production in the foreign country.) The TPM is a minimum price floor based on the production costs of the Japanese steel industry plus 8 percent. Any foreign company attempting to sell below the price floor could trigger an investigation into possible "dumping," which could lead to the imposition of penalty duties.

U.S. Steel's anti-dumping suit is aimed primarily at the European Common Market steel-exporting countries. Since 1972, when steel imports were about at the same level as they have been in 1980, the Common Market's share of imports has actually declined from 44 percent to 31 percent. Japanese steel imports have remained fairly consistent at 36 percent of total imports since 1972. Other nations, which in 1972 accounted for 20 percent of imported steel, have increased their share to 33 percent during 1980. Excess world steel making capacity has led Canada, South Korea, Taiwan, and Brazil to begin aggressively pursuing a larger share of the large U.S. market.

The International Trade Commission is scheduled to make a decision on U.S. Steel's anti-dumping suit on October 17. Preliminary indications are that the administration will offer U.S. Steel tax breaks, an easing of pollution regulations, a higher price floor, and a "fast-track" anti-dumping investigation system. U.S. Steel's management has strongly objected to what it alleges has been lax enforcement of the old TPM by the Government, claiming that at times 25 percent of the foreign imports were "under the floor." The new system would hold the promise of speeding up enforcement of the new higher anti-dumping provisions of TPM and offer better protection for domestic steel producers.

If the administration does make these election-year concessions to U.S. Steel, the steel industry's benefit will be at the expense of consumers. The TPM is merely a disguised protectionist scheme to reduce foreign competition. It is ironic that an industry that so vehemently denounces Government intervention on matters such as safety, pollution, and taxation, can lobby for that same

Government to intervene in the market to protect it against "cheap" foreign imports. The steel industry's case for a laissez-faire Government policy toward business might be more convincing if it were consistent.

RUNAWAY GOVERNMENT SPENDING: A PRELUDE TO . . . ?

As we reported in *Research Reports*, August 11, 1980, the much vaunted balanced Federal budget for the fiscal year beginning October 1, 1980 has been transformed into a deficit of $30 billion as of mid-July. Thus, one of President Carter's major promises made during the 1976 Presidential campaign apparently will be broken, as so many other promises to eliminate budget deficits proved to be empty.

As Table 1 shows, Federal Government spending has increased from $33 billion in 1930 to $579 billion in 1980, a 16,555 percent increase. Government spending has nearly tripled just since 1970. Even after adjustment for "inflation," Federal spending has about doubled since 1960.

The real tax burden for the American people has been increasing markedly in order to pay for soaring Government spending. Personal tax and nontax receipts of the Federal Government as a percent of Gross National Product (GNP) increased from 6.6 percent (1949-51 average) to 9.8 percent (1979-81 estimate), a nearly 50 percent increase in the tax burden of individuals. Moreover, contributions for Social Security have soared from 2.0 percent of GNP (1949-51 average) to 6.8 percent of GNP (1979-81 estimate), a 240 percent increase.

Direct benefit payments to individuals in constant 1972 dollars were $33.1 billion, or 22 percent of the Federal budget, in 1960. By 1970 the total increased to $68.8 billion, or 31.2 percent of the budget. The latest estimate is that transfer payments for the fiscal year ending on September 30, 1980 will total $138.6 billion, or 48.4 percent of Federal spending. According to the *Budget of the United States Government, Fiscal Year 1981*, transfer payments during fiscal 1983 are estimated to reach 50.8 percent of total Federal spending. Inasmuch as this estimate was made before the severity of the present recession was realized, the so-called automatic stabilizers (unemployment insurance, food stamps, etc.) undoubtedly will boost Federal outlays this year and next. As a result, by 1983 both total Federal outlays and the proportion involving transfer payments to individuals probably will be much larger.

The burden of Social Security taxes also has been increasing markedly during the past decade, and those taxes are scheduled to continue this trend until at least 1985. In fact, the revised projected deficits of the Social Security trust fund may prompt Congress to increase further the maximum taxable base and the employee and employer tax rates in the near future. Present Social Security legislation provides for tax increases over the next few years as shown in Table 2. From 1965 through 1985, the annual rate of increase in the maximum amount of Social Security taxes will have averaged nearly 15 percent. This maximum tax burden falls especially hard on the middle and upper-middle income taxpayer.

Table 1

FEDERAL BUDGET TRENDS
(In millions of dollars)

	Receipts	*Outlays*
1930	$ 4,058	$ 3,320
1940	6,361	9,456
1950	39,485	42,597
1960	92,492	92,223
1970	193,743	196,588
1980 est.	518,000	579,000

Sources: *The Budget of the United States Government, Fiscal Year 1981* and *Mid-Session Review of the 1981 Budget.*

Table 2

SOCIAL SECURITY TAX RATES AND MAXIMUM TAX

Year	*Maximum Taxable Base*	*Combined Employer and Employee Tax Rate*	*Combined Employer and Employee Maximum Tax*
1937-1949	$3,000	2.00	$60
1950	3,000	3.00	90
1951-1953	3,600	3.00	108
1954	3,600	4.00	144
1955-1956	4,200	4.00	186
1957-1958	4,200	4.50	189
1959	4,800	5.00	240
1960-1961	4,800	6.00	288
1962	4,800	6.25	300
1963-1965	4,800	7.25	348
1966	6,600	8.40	554
1967	6,600	8.80	580
1968	7,800	8.80	686
1969-1970	7,800	9.60	748
1971	7,800	10.40	811
1972	9,000	10.40	936
1973	10,800	11.70	1,264
1974	13,200	11.70	1,544
1975	14,100	11.70	1,650
1976	15,300	11.70	1,790
1977	16,500	11.70	1,930
1978	17,700	12.10	2,142
1979	22,900	12.26	2,808
1980	25,900	12.26	3,174
1981*	29,700	13.30	3,950
1982*	32,400	13.40	4,342
1983*	35,400	13.40	4,744
1984*	39,000	13.40	5,226
1985*	42,900	14.10	6,049

* Rates and maximum taxes unless changed by the Congress.

The Federal government thus has legislated, in effect, a continuation of the "inflating-embezzling" scheme. As the "real" tax burden increases for middle-income Americans, less funds are available for private investment and spending. The level of economic activity then tends to slow, pressuring Government and monetary officials to adopt more "stimulative," i.e., inflationary, policies. Cost-of-living adjustments to Social Security payments then guarantee the need for higher and higher taxes upon the working public to support the System. The spending-deficit-inflating circle thus is completed, setting the stage for another, higher circle.

Sooner or later this upward spiral will be broken either by the Government's reducing its claims on the resources of the economy and terminating inflationary policies or by the public's forcing an end to inflating by refusing to accept the currency, that is, a "flight from currency." The coming Presidential election will reveal which of these alternative paths probably will be followed during the next few years at least.

PRICE OF GOLD

	1979	*1980*	
	Sept. 27	*Sept. 18*	*Sept. 25*
Final fixing in London	$395.50	$672.00	$697.75

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