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THE NEXT RATCHET

NEW YORK, Jan. 25 (IPS) --Industrial production in the United States has now clearly entered the next phase of its ratchet collapse.

U.S. automakers, after examining shrinking sales figures and their own inventory pile up, announced plans to place 17,500 workers on "temporary" furlough during February. The auto industry, which had been trumpeted during recent weeks as the principal component of the "recovering" economy, now appears headed for an even more drastic shutdown of capacity by early spring.

Chrysler Corp, in particular, which has been tottering on the edge of bankruptcy for more than a year, has seen its inventories of unsold cars rising again to precarious levels, going from a 74 day stock in November to 91 days in December while statistics revealed that its share of the shrinking U.S. market declined drastically. The same inventory run up, created by increased production schedules over the last 2 months has also occurred among other automakers.

Production schedules for the entire first quarter are still based on the projection of producing 300,000 more autos than anticipated sales.

The Commerce Department's announcement this week that consumer durable goods sales -- of which autos are a significant component-- fell 5.1 per cent for the week, has prompted auto industry executives to reevaluate production schedules on a week-to-week basis -- a process last used during Fall-Winter 1974 which saw nearly half the industry shut down.

On Jan. 22, the Commerce Department reported that December figures for durable goods orders (orders for products such as machinery which are essential to industrial production) were down 0.5 per cent, continuing their four-month decline. If orders for transportation equipment, including autos, are excluded from these figures, orders for all other durable goods fell a whopping 4.4 per cent. The drop was so precipitous that Herman Liebling, the U.S. Treasury's top staff economist, would only comment that the numbers "don't seem to make any sense." -- especially in light of the government's insane talk of a strong recovery.

The weakness in auto and durable goods will soon trigger a ratchet shutdown among suppliers of those sectors- especially the steel industry. Total steel shipments for 1975 were under 80 million tons, compared to 109 million tons in 1974 and more than 30 per cent below the estimated capacity of 135 million tons. Production in the fourth quarter was only 20 million tons.

As a result, Armco and National, the U.S.'s fourth and fifth largest steel producers respectively reported this week that their fourth quarter earnings fell by over 50 per cent.

The only area for increased orders in recent weeks, according to industry purchasing agents, has been in sheet metal from the auto industry, which consumes 20 per cent of industry output. With the bottom having already fallen out of everything else, steel industry executives are privately mapping plans for new shutdowns.

Even assuming that auto orders were to hold up -- which no one assumes any more -- steel analysts had projected steel production for the first quarter of 1976 to be under 22 million tons. No one seems to have any idea what could reverse this situation and are reaching for some non-existent scheme. When asked where orders would come from to reverse this disastrous situation, one analyst replied, "Ford's energy program," referring to the recent Project Independence energy pyramid schemes put forward by Vice President Rockefeller and most recently proposed in the State of the Union message. He would not elaborate on how this would work or what would happen if Congress rejects the Rockefeller plan.

This collapse of basic U.S. industry is greatly exacerbated by the rapidly deteriorating international economic situation. The demand for commodities such as copper,iron, steel, etc. has collapsed over the last period and major U.S. producers are being caught in the squeeze. Kennecott Copper for example, reported that its fourth quarter earnings were down 56 per cent due to the collapse of the market price of copper.

Similarly, multinationals are now having the profit pictures for the European and Third World subsidiaries fall apart. Most won't be as lucky as near bankrupt Chrysler which forced the insolvent British government to bail it out under threat of closing up shop in Great Britain.

RETAIL SALES PLUMMET

On top of this, the Commerce Department this week also reported that retail sales fell for the first time in four weeks, destroying the fantasy of advocates of a so-called "consumer-led recovery." According to one Wall St. analyst, despite all the talk in the press of a strong Christmas season, retail stores are maintaining a bare-bones inventory position since they "lost their shirts" during the collapse last year and don't want to be caught in a similar position. The analyst discounted any reports on sales increases, saying that because of high fixed costs retail stores were pushing thier merchandise out the door at the expense of their profit margins. Several major chains are reported to be near insolvency. Even a professional optimist like Assistant Commerce Secretary James Pate reluctantly admitted that consumer spending would not be able to provide an impetus to to the much-publicized "recovery."

THE CREDIT COLLAPSE

The Federal Reserve Bank of New York reported Jan. 22 that Commercial and Industrial loans by the major New York banks dropped by $300 million in the past week, bringing the three week decline to $1.7 billion -- a rate unprecedented since the last Great Depression. The inability of the banks to make loans, and hence create demand deposits, was reflected by a further drop of the basic money supply (M1) by $1 billion this week bringing the total drop to some $3billion over the last two weeks.

James O'Leary, vice-chairman of the U.S. Trust Co., said that under these circumstances supplying reserves to the banking system by the Federal Reserve System was like "pushing on a string."

The apparent excess funds generated by the collapse of production has already driven down all short and long-term rates. Holdings of Treasury securities by New York banks fell more than $750 million last week, as the spread between three month Treasury bill rates and the Federal fund rate narrowed to one basis point. (a basis point is 1/100 of a percentage point) Large Certificates of Deposits -- one of the principal sources for generating bank income-- fell over $650 million during the week, $2 billion over the last three weeks. This unprecedented drop is an indication that people are shying away from credit markets in search of more profitable speculative outlets.

Billions of dollars held by insurance companies, pension funds, and other financial institutions are now pouring into Wall Street -- a source of quick paper profits. The Dow Jones industrial average continued its dizzying climb this week, on record trading volume. The average has climbed over 100 points in January. Prophets of recovery pointing to this sheer speculative activity claim that "prosperity is around the corner." The fact that the stock market is booming only because the economy is falling to pieces is evidently something that most investors will fail to realize until after the bust -- which is in the offing sooner than most people dare imagine.

BACKGROUND TO THE COLLAPSE

The reasons for this renewed downturn are rooted in the so-called "upturn" of April-September, 1975, -- which represented no economic upturn at all.

The entire increase in production during this period was related to a slowdown in the rate of inventory accumulation as inventories were passed on from manufacturers to the wholesale to the retail level. This inventory "swing" represented 80 per cent of all domestic investment over the same period. Meanwhile, capital spending in constant dollar terms dropped ten per cent, and housing and construction were severely depressed. Thus, by fraudulently improving corporate liquidity the collapse in capital spending and actual disinvestment represented by plant closings, etc., gave a short-term boost to the economy.

Equally important, this "upturn" was accompanied by the actual collapse of working class income. To the extent there was any increase in consumer sales it was entirely related to workers dipping into their savings to the tune of $30 billion. During these months personal disposable income actually dropped in constant dollar terms, a fact which can be most easily explained in terms of astonishing employment trends. From May to September 1975, the total workforce actually contracted by 3 million people, or 4 per cent. As a result, the entire increase in industrial production shown during that period must be accounted for by a record increase in productivity more euphemistically known as speed-up.

To the extent that transfer payments such as unemployment compensation, and the 1975 tax cut financed a certain temporary expansion, the process merely generated greater government debt, requiring greater austerity measures to prop it up -- and so on in a downward spiral of collapse.

The collapse of capital spending and consumer income put a brake on this so-called upturn as early as September. At that point, retailers and wholesalers began to cut back orders from manufacturers, a trend which picked up in November when general orders dropped by 0.5 per cent and orders for durable goods dropped by 3.2 per cent. As a result, October and November industrial production growth rates plummetted by 50 per cent, hovering around zero.

November represented a key inflection point in the new downturn. Reflecting the previous drop in manufacturers orders shipments dropped by one per cent, the first such drop in five months. Business sales also dropped by almost one per cent. Meanwhile inventories at the manufacturing level increased, reflecting involuntary accumulation. This upturn foreshadowed the next ratchet in production collapse - now being felt.

The November downturn would have been more precipitous had it not been for the artificial inflation of the consumer durable sector. This sector -- and especially the highly touted auto industry was propped up by massive infusions of consumer credit while workers dipped further into savings for pre-Christmas buying.

Fourteen months of massive inventory liquidation, layoffs,and construction and capital spending cutbacks has wrung from the economy huge amounts of funds that have flowed into the coffers of the nation's financial intermediaries and institutional investors. With no outlet for productive investment these funds are starting to find their way back into the speculative dream maker -- the stock market.

Analysts already estimate that investments in corporate bonds will be only half what they were a year ago, and that those investments related to manufacturing production will plunge from $11 billion to $2 billion. Investment in tax-exempt securities is expected to drop 30 per cent.

The alternative investment is government securities, but the huge excess of funds is driving down interest rates here to the abysmal level of other investments.

Similar developments produced the 1929 market crash. But there are two major differences between now and 1929. First, the liquidity crisis is much worse: the ratio of the economy's debt to income is at least four times greater today than in 1929. Second, the present stock market splurge reflects much more a full-scale liquidity crisis centered in the banking system throughout the entire bankrupt dollar sector.

Since the ratio of debt to equity in the financial system represented by the relationship of huge bank loans to actual ownership instruments such as stocks, for example, is far worse than in 1929, the outcome of the present crisis will not simply be a stock market crash, but an immediate full scale collapse of the banking system as well.

WORKERS FACE EXHAUSTION OF BENEFITS

Approximately 65 weeks ago the biggest wave of layoffs hit

U.S. industry. By February and March those workers' unemployment benefits will run out. There is at present no legislation in place to extend those benefits. The absence of any economic recovery -- and the onslaught of a new downturn -- guarantees that those workers will not find new jobs. To survive, they will be forced onto the welfare rolls or forced to liquidate their savings or both.

At the end of December, thousands of workers -- (there are no statistics yet of how many) -- were informed that the "insured" unemployment rate in their states was too low for them to be eligible for the 26 weeks of federally-funded supplemental benefits.

Under federal law, eligibility for supplemental benefits is determined by the "official" rate of unemployment among workers covered by regular state unemployment programs. These notoriously manipulated figures are lower than the actual jobless rate among all workers. Workers in the District of Columbia and 20 states, primarily the relatively well-off energy and agricultural producing states -- no longer qualify, because the employment picture statewide is too good! As of Nov. 22, 1975 188,000 workers in those states were receiving supplemental benefits.

FORETASTE OF NELSON ROCKEFELLER'S NEW FEDERALISM

President Gerald Ford is getting strong backing from Vice President Nelson Rockefeller for one of the major policy proposals contained in the State of the Union address of Jan. 19 -- the need to take responsibility for the delivery of social services out of the hands of big government and returning it to the states. As anyone who reads the papers realizes, these states are either bankrupt or near bankruptcy themselves and are now bowing out of picking up the tab for such costs.

An examination of the problem of welfare payments reveals that the burden has already been shifted to the states and various municipal subdivisions.

A researcher at the New York State Department of Labor indicated today that during Jan.-Sept.'75, the number of New York State residents on aid to dependent children federally-reimbursed relief remained stable, while the general assistance roles -- those funded exclusively by states and cities -- increased dramatically. He said that at first this trend was puzzling, because one would expect unemployed workers with exhausted unemployment benefits to turn up on ADC relief. His explanation was that case workers were putting those workers, who were actually eligible for the federally-funded program, onto general relief because there was "so much red tape involved with getting them on the federal roles."

Much of the red tape is obviously designed to reduce the size of the federal welfare commitment. The new HEW secretary has made it one of his objectives to get the ineligibles off the roles. Ford's proposal to tighten up federal control over "eligibility" is aimed at accelerating this process which will eventually leave hundreds of thousands of unemployed workers without any relief whatsoever.

According to this same researcher, more and more unemployed workers in New York State are turning up on welfare -- the state and locally funded program. A study he did following up what happened to the first group of workers who exhausted their 65 weeks of benefits last July showed this, and he had planned to update the

the study but too many people had been laid off from his staff to take on the project, he told IPS.

GOVERNORS TO GRID THEIR AUSTERITY PLANS

The National Governors Conference is reported to be gathering reports on the new state austerity budgets as they come out and will put together a comprehensive review by early next month.

A researcher for the governors' group said today that preliminary indications are that the northeastern and north central states will follow a near-identical austerity route, singling out welfare, education and health costs for the axe.

The New York State Budget released by Gov. Hugh Carey this week targets these outlays. The $10.76 billion "no growth" budget calls for cutbacks of $110 million in education, $132 million in welfare and several tens of millions in health costs.

THE NEW YORK CRISIS ... AGAIN

As was predicted last week in this newsletter, New York city and state suddenly find themselves in the throes of a "new" fiscal crunch. The parameters of the crisis are the same as the last time around -- an inability to borrow additional capital and the inability to guarantee repayment of billions of existing debt.

At a meeting Jan. 23 of the city's banker-appointed government, the Emergency Financial Control Board (EFCB) New York Governor Hugh Carey told city officials that "new information"required that the city's current three year austerity plan be revised -- more severe cuts were necessary. While the newspapers cited figures showing that the city would lose $200 million in expected revenue according to the new State and Federal budget and another $89 million due to tax revenue shortfalls, the "information" that was prompting the Governor's action was being whispered in his ears by the New York banking community.

These bankers, both the big Rockefeller banks and the investment houses that have in the last week emerged as the Rockefeller's factional opponents, are extremely nervous about the more than $20 billion in "soft" New York paper that they carry on their books as assets. Unless both the city and the state show an ever increasing commitment to repay this debt by administering new and severe budget cutbacks at all levels, these bankers reason, a time will come when all the patchwork schemes aimed at covering up the insovency of these institutions and the worthlessness of their securities will cease to be functional. As most investors realize -- though refuse to say too loudly -- the billions in New York paper is already worthless. However, as long as the debt service payments are met, then no one will dare call the bluff. But if the time ever comes when the bluff is called, then the Rockefeller banks and the investment houses will go broke together -- hence their alliance on the New York question.

This week Carey finally concretized the "pain" that he called for in his State of the State message, submitting a zero growth budget that slashed hundreds of millions from state education, welfare, and health payments.

Later in the week, New York's Mayor Abe Beame, who is also under pressure from the city's creditors to step up his austerity program, told the city council in his State of the City message that the outlook for the city's future was "bleak." We can no longer afford such luxuries as the City University, several municipal hospitals, thousands of city workers and serices, the Mayor stated. These cuts will be "painful," Beame said, but there is no other way.

During the height of last summer's fiscal crisis, David Rockefeller had in a letter dictated to and released by one of his vice Presidents at Chase Manhattan warned that the city "might not survive" what it was going to be asked to do. Beame said this week, that the city "will survive" but "you won't be able to recognize it."

Over the last eight months the bankers have chopped up the city into little pieces, hocked its services to pay off their debt -- all in the name of "fiscal responsibility," when MAC couldn't do the job, they consolidated for a new onslaught under the EFCB. Now although they won't admit it publicly, the least hysterical of these bankers have come to understand that they have solved nothing. With the aid of the$2.5billion Federal loan, they have only postponed the collapse of their New York paper. Scream as they may for austerity, their day of reckoning is fast approaching.

At some point the city and state have to re-enter the now moribund bond market -- or default. A Standard and Poors official said this week that the city may be able to enter the bond market again - "maybe twenty years from now." The state, he indicated was in better shape -- it could go back into the market maybe by April or May for "a couple of hundred million .. to test the water, its very'iffy' you know."

But the state is slated to go into the market for a whopping $4 billion starting April, "if it doesn't sell," one bond trader indicated, "then we will be in real trouble." The plans are to reduce the offering by slashing the state and city budget in progressive stages. But there is no way that the budget can be slashed enough to market only "a few hundred million."

And in the back of these bankers minds is the nagging thought that they might not even get that far. The level of austerity they are demanding is so incredible that some legislator or city official may get the idea to extend the moratorium enacted by the state on $1.6 billion in city notes, rather than "play ball" with the austerity proposals. If such a proposal comes up during the current session of the legislature, it just might pass.

$200 million in state agency notes come due Feb. 15 while $2.5 billion in state notes are slated to be redeemed between April and June. Each of these become inflection points for debt moratorium "talk" and a possible bill.

While some hysterical Wall Street people scream "it can't happen here," a few realize that it already has , as a State Supreme Court declared last month, its all quite legal.