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Volcker caught in mammoth fraud

by David Goldman

In this Special Report we present excerpts of *EIR*'s Quarterly Economic Report for October 1983, released on Oct. 18. As promised, the report documents in full the "simpleminded statistical fraud" by the Federal Reserve, Bureau of Labor Statistics, Department of Agriculture, and other governmental bodies. Physical production will fall by 4 percent overall (including agriculture) during 1983 with respect to 1982, *EIR*'s staff concluded after reconstructing the actual state of industry sector-by-sector, using relatively reliable, non-governmental raw data in most cases.

The production collapse is the direct result of the high-interest-rate policies of Federal Reserve chairman Paul Volcker, which have cut off capital investment and choked world trade. Now Volcker's statisticians are trying to cover up the evidence of the crime.

Pre-circulation of the contents of this document has already produced shock waves in Washington, where the White House reportedly has asked the Commerce Department to cross-check the Fed's index.

We publish here the Executive Summary of the Quarterly Economic Report, as well as excerpts from three key sections of the report:

1) The general forecast (showing the actual state of the economy and its trajectory for next year);

2) The Fed's fraud in the industrial production index;

3) The Bureau of Labor Statistics' fraudulent misrepresentation of inflation.

Not included in these excerpts is the report's exhaustive comparison of the Federal Reserve's phony index with real data, and detailed reportage of the state of all key goods-producing sectors, including agriculture, as well as America's $120 billion per year manufactured-goods subsidy from the rest of the world. Also not included is an analysis by Lyndon H. LaRouche, Jr. on "Policy Improvements in LaRouche-Riemann Forecasting."

Excerpts from the Report's analysis of the global monetary crisis were printed in *EIR* last issue.

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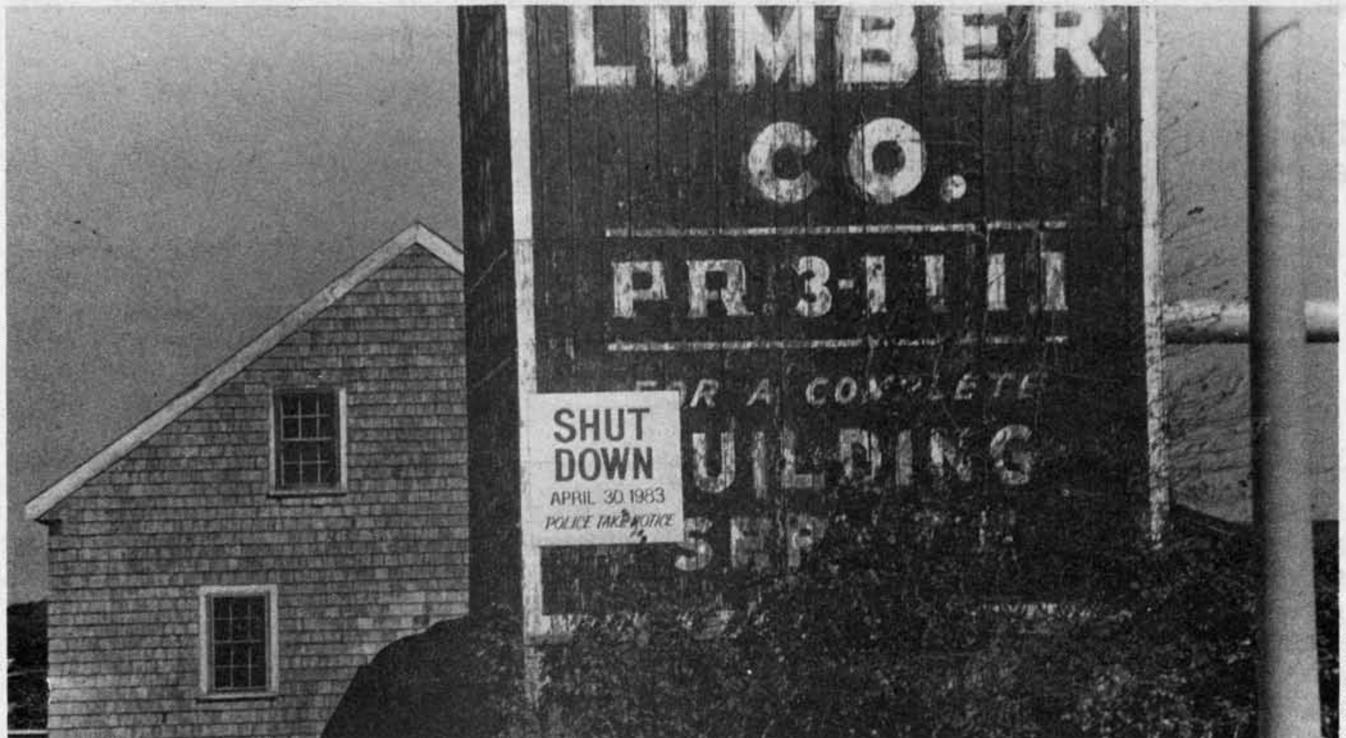


NSIPS/Connie Brown

Some of the evidence disproving Paul Volcker's recovery statistics.

Executive summary

You, like President Reagan, have been the victim of conscious and deliberate lying by the nation's most senior monetary officials concerning the state of the nation's economy. The Federal Reserve Industrial Production Index now stands 9 percent above last year's level, just at its all-time peak level. In fact, the physical output of the nation's factories, mines, and farms will have fallen by 4 percent during 1983; excluding the agricultural disaster, the decline will still be almost 3 percent. The difference is made up by simpleminded statistical fraud by Federal Reserve statisticians, who

- turned a decline in the value of steel output into a 36 percent rise;
- turned an 11 percent rise in tire output into an 18 percent rise;
- turned a flat trend in most categories of apparel production into a 12 percent rise;
- turned a 15 percent increase in laundry-appliance output into a 34 percent rise.

Apart from a temporary, heavily financed uptick in certain consumer sectors, the entire economy continued to fall, although not at the pace of the 1982 downslide; this will resume next year as the consumer bubble deflates. *EIR* has used on-the-ground surveys, direct collection of data from industrial sources, and other reliable means to reconstruct the true picture of the American economy as of the third quarter of 1983. Senior administration officials, as well as Commerce Department economists, have acknowledged that the picture presented in this report is accurate. Out of fear, they will not say publicly that Paul Volcker has no clothes.

The future potential of the economy, measured by the LaRouche-Riemann model's $S'/(C + V)$ (reinvested surplus divided by real production costs) will fall by an additional 6 percent this year—not including the continued devastation of the nation's basic infrastructure and labor force.

America now faces:

1) A world financial crisis worse than July-September 1931, postponed until the fourth quarter of this year by financial chicanery, promises of "economic recovery," and International Monetary Fund "conditionalities" which have made the ultimate problem much worse;

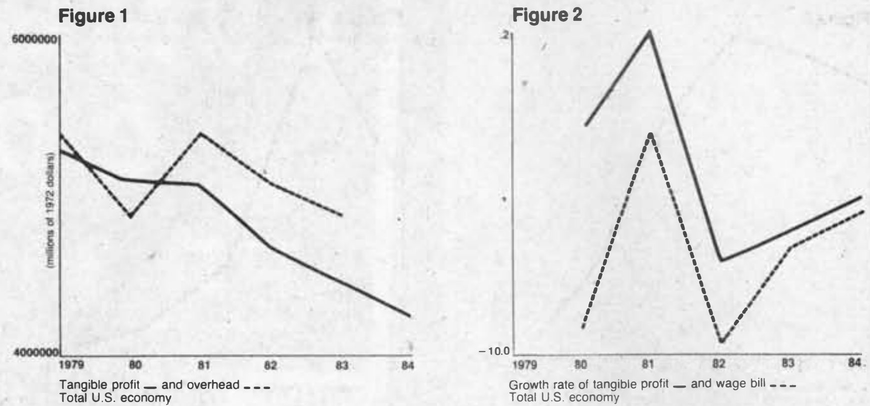
2) A devastated agricultural sector and the prospects of the first real food shortage in American history during 1985;

3) Continued destruction of labor force skills and downwards "recycling" of formerly employed industrial labor, when the American economy depends on a mere 18 percent of its labor force to produce the total volume of physical requirements of the economy;

4) Continued decapitalization, both real and financial, of the basic industrial sectors.

This is a moment for emergency action. The fog of the 1984 presidential campaign has already surrounded the White House. This does not mean that there are not a few astute persons in the Reagan administration. It means that such relatively few wiser voices are being drowned out by a chorus of bunglers which includes Henry A. Kissinger, Secretary of State George Shultz, Federal Reserve chairman Paul Volcker, and that confused paper-salesman from Merrill Lynch,

From EIR's economic forecast



Treasury Secretary Donald Regan. The misadvisers of the President have U.S. monetary policy caught between wishful delusions of non-existent economic recovery and the pit of general financial collapse.

The minimum requirements to avoid disaster are first, to undertake an emergency reorganization of developing nations' and related bankrupt debt, through a "federalized" Federal Reserve System, and to initiate a crash program on the World War II mobilization model to develop a coherent-radiation anti-missile capability (beam-weapon defense systems). Probably such a crash effort, acting as a science driver for both the military and civilian sectors of the economy, will enable the U.S. economy to repair the damage of post-1969 anti-industrial policies. Lesser measures would come too late.

The economic forecast

Physical output of the U.S. economy will fall by 4 percent between 1982 and 1983, LaRouche-Riemann analysis of the U.S. economy demonstrates. This startling result is obtained after stripping away the Federal Reserve's statistical fraud in the industrial production index.

Declines occurred in supposed boom sectors, including steel (the value of whose output fell after accounting for a shift in tonnage output to the cheapest categories of flat-rolled steel) and construction (where Commerce Department figures were artificially inflated by a rise in cheap, prefabricated multi-family dwellings). Apart from automobiles, chemicals, and a handful of small sectors, where a temporary uptick occurred, every sector of the economy declined. The most devastating decline occurred in agriculture, which shows a nearly 20 percent reduction in physical output between 1982 and 1983, due to both the PIK (Payment in Kind) program and drought.

The LaRouche-Riemann model is not employed for "crystal-ball" forecasts of future economic performance. The above results are an evaluation of present economic potential under present economic policy conditions, i.e., the direction in which the economy is moving under the Federal Reserve's fiscal and monetary austerity regime. In the real world, this trend will be interrupted in one of two directions, probably by early 1984. Either the President will prevent further economic disaster by initiating a general monetary reorganization and a crash program centered around beam-weapons defense, or the world monetary crisis will produce a sudden deterioration of the American and other industrial economies.

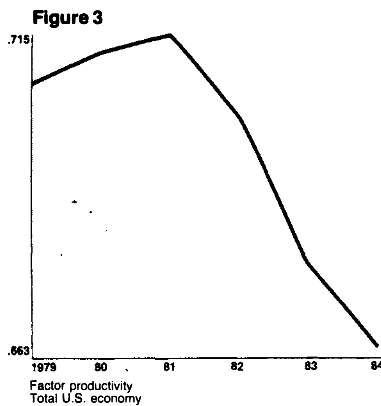


Figure 3
Factor productivity
Total U.S. economy

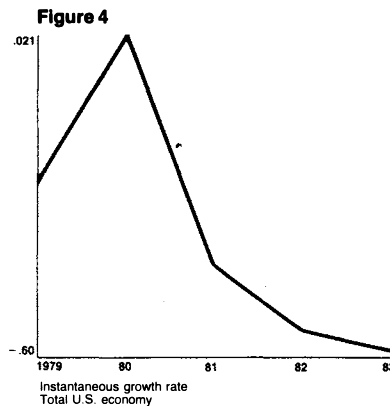


Figure 4
Instantaneous growth rate
Total U.S. economy

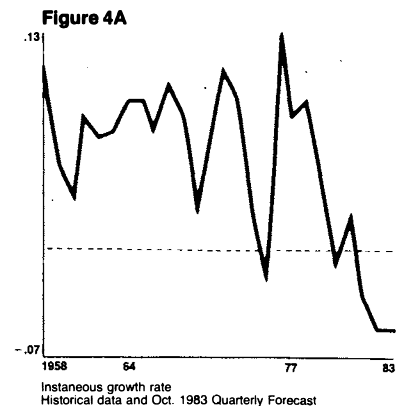


Figure 4A
Instaneous growth rate
Historical data and Oct. 1983 Quarterly Forecast

In our Quarterly Economic Report for March 1983, we identified the following possible trajectories for the American economy:

1) Continued decline of the U.S. economy at a 10 percent annual rate in terms of output of tangible goods, assuming continued lack of credit-availability to the productive sector, and inability and unwillingness on the part of goods-producing corporations to rebuild inventories, re-hire employees, skilled workers, and production line workers, and to replace plant and equipment.

2) Continued decline of the U. S. economy at a 3 to 5 percent annual rate in terms of output of tangible goods, under conditions of a general reflation which would revive auto and housing, but leave basic industry and capital goods industries unaffected. This scenario is not considered probable, and is included less as a forecast than as a demonstration that conventional reflation mechanisms will not work under prevailing circumstances.

The total decline of agro-industrial output of 4 percent this year is in the range of the 3 to 5 percent decline forecast last April, under the assumption that the Federal Reserve would continue to float the fraudulent "recovery." The LaRouche-Riemann model, in its quarterly forecasting application, has achieved the following results since 1979:

1) forecast the timing and size of the first-half 1980 industrial downturn;

2) specified the false-start recovery of the second half of 1980, and forecast a year in advance the "double-dip" decline beginning in the second half of 1981 in both timing and size;

3) forecast in mid-1981 the 7 percent agro-industrial downturn of 1982;

4) forecast the present year's developments, as noted above, once accurate data were substituted for utterly fraudulent Federal Reserve estimates.

Figure 1 shows the production of tangible profit and the overhead spending in the U.S. economy from 1979 to 1983-84. Tangible profit has fallen from a 1979 level of $521 billion to $468 billion 1972 dollars in 1982, and the fall will continue, to $440 in 1983 and around $420 in 1984. The continued decline is the overall result of the absence of any recovery, documented throughout this report. Overhead spending has also declined since 1979, but it has exceeded tangible profit in all years except 1980. In 1983, this gap will be a record $39 billion 1972 dollars. Note that no prediction of overhead spending is made for 1984, since this quantity is a residual after net investment.

Figure 2 shows the rates of growth or decline of tangible profit and of wages. A modest positive growth rate for tangible profit in 1980 was not matched by tangible wages. Overall, tangible wages were declining faster than profit, until the 1982 collapse. The forecast calls for a continued decline in both categories, slowing to around a −6 percent per annum rate in 1983 and −5 percent in 1984.

Figure 3 shows the overall measure of the productive efficiency of the economy, factor productivity, or the ratio of tangible profit to the total operating costs (wages plus intermediate goods plus plant and equipment replacement). The forecast shows a continuation of the decline in factor productivity experienced in 1982 throughout 1983 and 1984.

Figure 4 shows the ratio of net reinvestment to total operating cost. This represents the instantaneous growth rate of the economy as it compares the amount spent on net expansion of labor, capital, and intermediate goods, with the totals of these categories. The forecast indicates that the potential of the economy is not only continuing to decline, but that the decline is occurring at an accelerating rates, as the shrinkage of the operating base continues (See **Figure 4a**).

The fraud of Fed statistics

The following is the anatomy of a fraud which has influenced the policies of the White House, foreign governments, U.S. businessmen, labor leaders, and ordinary citizens. It has been in place many years and has spread to many areas

of government statistics.

However, the scale of fraud dominating the output of Federal statistical agencies grew drastically during the period of supposed "economic recovery" since November 1982. The fraudulent Industrial Production Index of the Federal Reserve Board has been used to create a non-existent "recovery" of the U.S. economy, convincing the President to follow the economic dictates of Federal Reserve Board Chairman Paul Adolph Volcker, to reappoint him to another seven-year term as chairman of that Board. The use of the bogus Fed Index was the basis for Secretary of State George Shultz's promises to the developing nations that the U.S. recovery would restore their economies—if they accepted the policies of the International Monetary Fund.

All available physical evidence showed that the economy continued to decline through 1983. Electricity consumption and all categories of transportation remained lower during the first half of 1983 than during the first half of 1982.

No economic recovery, much less one concentrated in the physical production categories listed by the Federal Reserve, is physically possible without strong growth in power consumption and transportation. If the goods were being produced, where were they?

By comparing production figures supplied to us by trade associations for the specific industries to the Fed Index figures, we were able to locate the extent and magnitude of the Fed's lying for about 10 percent of all industrial output. Collateral information, including employment data and information from industry sources, enabled us to reconstruct the actual state of physical output. Below we document in depth the fraud irrefutably proven for categories of output where complete data are available, as shown in **Figure 5**.

Our work has produced two related discoveries: The first is the short-term inflation of industrial figures from the second half of 1982 to the first half of 1983 to produce the "recovery" announced by Secretary of State Shultz in September 1982

Figure 5

Fed fraud at a glance

			1983			
		1982	**Jan.**	**Feb.**	**March**	**6 mos.**
Autos	Fed index	86.6	92.8	110.2	112.5	114.3
	Actual index	69.4	70.0	79.6	92.8	88.2
Tires	Fed index	137.9	149.8	158.3	159.1	153.7
	Actual index	109.4	114.0	110.3	127.1	116.8
Synthetic rubber	Fed index	84.9	82.2	99.6	106.0	103.5
	Actual index	94.3	95.9	95.0	105.1	100.5
Raw steel	Fed index	62.1	55.4	63.0	71.4	68.4
	Actual index	58.6	52.5	53.5	67.2	63.0
Steel mill prod.	Fed index	66.6	65.1	72.4	80.2	78.1
	Actual index	71.3	65.5	65.6	85.4	76.7
Laundry appliances	Fed index	110.5	133.4	136.4	139.2	140.2
	Actual index	96.1	106.7	103.3	120.3	110.6
Cook stoves	Fed index	102.2	138.4	137.3	140.5	147.2
	Actual Index	84.4	88.7	87.7	108.9	102.6
Refrigeration equipment	Fed index	97.3	109.4	106.4	108.0	114.0
	Actual index	98.1	96.2	89.4	107.3	107.4
Hosiery	Fed index	212.5	217.3	233.5	223.5	237.9
	Actual index	122.3	120.0	121.4	132.4	130.8
Plywood	Fed index	186.0	213.2	225.5	232.0	231.1
	Actual index	133.6	143.7	146.9	190.2	163.8
Lumber	Fed index	78.4	90.7	95.7	89.3	92.6
	Actual index	74.8	85.5	86.4	91.3	88.9
Fiber boxes	Fed index	143.9	149.7	198.9	154.3	153.5
	Actual index	144.6	147.5	137.4	161.8	152.3
Petroleum refining	Fed index	122.5	112.5	109.6	110.3	115.4
	Actual index	123.5	116.4	101.9	113.0	115.8
Auto gas	Fed index	128.5	121.9	118.4	119.4	124.9
	Actual index	128.3	124.2	108.9	121.6	123.8

Source: Federal Reserve Board; *EIR* estimates

Figure 6
How the BLS ignores inflation

	Cost to Consumer 1967	Cost to Consumer 1st Half 1983	No. of times cost rose	August 1983 consumer price index (1967-100)	Corrected consumer price index	Inflation BLS left out (%)
Transportation						
new car	$3,212	$10,700	3.331	202.1	333.1	131
old car	1,500	5,203	3.468	333.8	346.8	13.0
repairs	102	516	5.052	332.0	505.2	173.2
Home						
monthly installment (+ interest on 25-30 yr. mortgage)	121.74	814.17	6.668	357.6	668.8	311.2
Appliances						
monthly installment (+ interest on 2 yr. financing) refrigerator	145.37	354.86	2.442	200.3	244.2	43.9
freezer	124.13	271.95	2.192	200.3	219.2	18.8
stove	117.67	243.90	2.073	122.5	207.3	84.8
dishwasher	113.48	214.12	1.887	122.5	188.7	66.2
air conditioner	111.85	236.19	2.112	124.5	211.2	86.7
dryer	95.37	184.80	1.990	142.9	199.0	56.1
washing machine	125.13	238.98	1.910	142.9	199.0	48.1
Food						
oranges/dozen	0.95	2.66	2.880	298.6	280.0	(18.6)
lettuce/head	0.27	0.84	3.296	306.4	329.6	23.2
round steak/pound	1.11	3.67	3.303	257.4	330.3	72.9
white bread/pound	0.23	0.84	3.652	224.4	365.2	140.8
milk/half gallon	0.52	1.22	2.346	247.1	234.6	(12.5)
eggs/dozen	0.66	1.02	1.543	165.3	154.3	(11.0)

and the Fed itself in December—subsequently believed by the White House in April 1983, and announced by the national news media continuously since December 1982. The second finding is that the Fed Index has systematically inflated certain items of production, especially consumer goods, since at least 1967—when the current Index was established. These two interrelated statistical manipulations have made it possible to show that industrial activity is now back to 1979 levels despite the undeniable, and unmistakable ruin of our basic heavy industries in precisely that same time period. It is this fact that labor leaders, corporate executives, and ordinary citizens have captured in describing the industrial Midwest as the "Rustbowl."

How we discovered the fraud

In December 1982, as we prepared the Quarterly Economic Report, we determined that nothing in the present economic picture could sustain a recovery. Although pulled down by the Federal Reserve Board in July 1982, interest rates were at usurious levels for consumer credit and much producer credit, deregulation continued to cut the transportation industry to ribbons, the administration's farm program would gut farm output, industrial corporate sectors were either so laden with debt they would not purchase capital equipment, or were parts of conglomerate financial holding companies whose policy it was not to invest in capital equipment, and International Monetary Fund "conditionalities" were washing out U.S. exports especially to our trading partners in the Western Hemisphere.

Yet, starting in December 1982, the Federal Reserve began reporting across-the-board increases in industrial output. Our own industrial sources continued to report extremely depressed conditions. The Fed Index itself reported rises in output of production in about a dozen major industries while simultaneously reporting a drop in electrical consumption in those industries. There was clearly something wrong. One case stood out above the others: a reported ten percent increase in cement output with no corresponding increase in electrical consumption. This simply could not occur.

In August, we proceeded to gather industry data independent of the Fed, to compare against the Fed Index, as reported in the tables below; we also began to closely question the Fed itself as to how it derived its figures.

We established:

1) The Fed employs exactly four people—two economists, one statistical assistant, and one research assistant—

to compile all the data on the nation's output for the Fed Index.

2) The Fed claims to use real output data but in fact makes preliminary estimates of output from manhours worked or electricity used in each industry and then makes arbitrary adjustments by what it calls "production adjustment factors" (PAFs).

3) Those PAFs include, the "Inventory Adjustment Factor," the "Productivity Adjustment Factor," the "Quality Adjustment Factor," and others.

4) These factors are never made public and are contained only on the worksheets of those who compile the index.

5) When the Fed decides there is upturn in the "Business Cycle," it automatically engages the Productivity Adjustment Factor which increases the output per manhour—thus producing the very upturn in production to justify its determination that such an upturn is occurring.

6) The Fed borrows its fudge factors from other agencies, notably the Bureau of Labor Statistics "Quality Adjustment Factors," and the BLS in turn uses the Fed Index to compute its own Productivity Index. Given that the Fed sits on the interdepartment group on government statistics, the implication is that the statistics of some, most, or all Federal agencies are falsified.

Usury and inflation

It is lawful that the widest discrepancy between the Bureau of Labor Statistics estimate of inflation and what inflation really is should occur in the area of housing. Home prices reflect the effect of usury. Based on a Consumer Price Index number of 1967 = 100, the BLS estimates that the CPI number for home purchase and interest charges (averaged according to respective weights) is 357.6 in August of this year. However in 1967, a homeowner paid $121.74 per month payment on the mortgage for his new home. Today, due to skyrocketing mortgage interest charges, he pays $814.17, or

6.688 times the level of 1967. Based on the real costs of homeownership, which includes the actual interest charges a homeowner pays, the BLS Consumer Price Index number housing should be corrected to read 668.8—the actual amount the cost of homeownership rose, since this is what the BLS claims to be measuring. How much did the Consumer Price Index for homes underreport the real inflation level for homes? If one subtracts the fraudulent BLS number from the actual corrected number, one finds that the BLS refused to report 311.2 percent of the increase in home prices since 1967 **(Figure 6)**.

But the effects of the pestilence of usury on homeowner costs is too evident to be hidden. The usury can be directly measured in the cost of a home as the amount of interest overhead a homeowner must pay to pay off the mortgage and downpayment on a home. The interest component of the home cost is the difference between the purchase price of the home and the final price after the mortgage is paid off.

In 1949 the average purchase price of a new home was $12,000. The final cost, when interest is included was $17,811. The amount of interest paid was $5,811, which is 32.6 percent of the total cost. In 1967, the average purchase price of a new home was $24,600; the final cost was $47,293; and the interest paid was $22,693, or 48 percent of the total.

But under Volcker, usury has become the dominant governing force of the economy. In 1983, the average purchase price of a new home is $88,200; the final price, after the mortgage is paid off, is $261,714; and the interest amount is $173,514. *The interest cost is a staggering two-thirds of the total!*

To put this into perspective, consider the fact that today one pays 30 times the absolute amount of interest on a house that one paid in 1949.

Against this interest cost, all other costs pale. While Paul Volcker is screaming about the need to cut wages, one must conclude that he is certainly in need of institutional confinement when one considers the cost of a home. The entire construction labor costs of an average home are $13,000 or one-twentieth the cost of a home. Even if the construction workers were to declare that they would work for free, and their labor costs were deducted from home costs, most Americans could still not afford to buy a home.

While the BLS claims that it is taking into account interest charges, it doggedly insists on doing the opposite. Indeed, starting in 1983, the BLS changed the basis for the computation of the cost of home ownership. It eliminated the interest charge of housing altogether, and instead replaced the category of home ownership with something called "home ownership rental equivalent."

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