Why LaRouche says we are heading for a crash

by Marcia Merry Baker and John Hoefle

Figure 1, a "typical collapse function," was presented by Lyndon LaRouche in a keynote speech at a conference in Germany on Dec. 10, 1995, to summarize the process of disintegration of the world economy. LaRouche said at that time, in a presentation entitled "We Are at the End of an Epoch," that, "for reasons I'll indicate to you, generally speaking and overall, *there has been no economic growth on this planet, since the end of the 1960s.* None; if you measure the right magnitudes." LaRouche said that "the American people produce *half as much* as they did 25 years ago, and consume about half as much, for various reasons. . . . That is a pattern around the world. There has been a secular tendency toward a 2-3% annual contraction in economy around the world, with some variations in that, over the past quarter-century. The system is collapsing" (see *EIR,* Jan. 1, 1996).

LaRouche described the three curves—not mathematical calculations—which characterize the disintegration process, beginning with the bottom curve, showing a decline in productivity in physical terms; the middle curve, showing an increase in monetary valuation and inflation; and the upper curve, showing hyperbolic growth in financial aggregates of all kinds, such as speculation in currencies, stock markets, derivatives, and so on.

Today, 12 months later, the processes described by the curves, in all but a few locations, have intensified, to the point of constituting a shock front threatening to destroy what economic means of existence remain, unless emergency measures are organized to intervene.

As 1996 ended, aspects of this situation were so obvious, that warnings were being sounded almost daily on the imminence of the "Big One"—a crash of the stock markets, or U.S. securities markets, or one or more of several national banking sectors (see the timeline of economic commentary—warnings and virtual reality—which follows, for such comments). The "virtual reality" section includes the pronouncements from those demented souls who still deny the ongoing collapse, and make reference to nonexistent economic growth.

What is profit?

But, what can be done to rescue the situation in 1997? One essential point to understand, is the defining qualities of a genuinely profitable economy of a successful nation-state. In this *EIR* economic survey, we feature two articles on this subject: "Machine-Tool Design: the Brains of Profit," by Lyndon H. LaRouche, Jr.; and the companion study, by our Wiesbaden economics correspondent Lothar Komp, "The Crucial Role of the *Mittelstand* in the Economy of Postwar Germany."

As LaRouche states at the outset, the crucial point is, "that for any national economy taken as a unified whole, scientific and classical-artistic progress, combined, are the only source of sustainable profit, nothing else. The machine-tool sector illustrates the role of science in this. For the imperilled economy of the United States, and, of many other nations, today, the lesson told is a desperately urgent one, even if it appears to address only technological progress as such."

In contrast to this scientific definition of "profit"—and Komp's report elaborates these secrets of the postwar German economic "miracle"—the currently most popular truisms about economic success, are based on lunatic measures of increasing rates of "free trade," "global integration," "outsourcing," national export-import "openness," "ecological sustainability," "market-based competition," and so forth. To underline this point, we here provide selected magnitudes and events in 1996 relating to each of the three collapse function curves, beginning with financial aggregates.

FIGURE 1
A typical collapse function

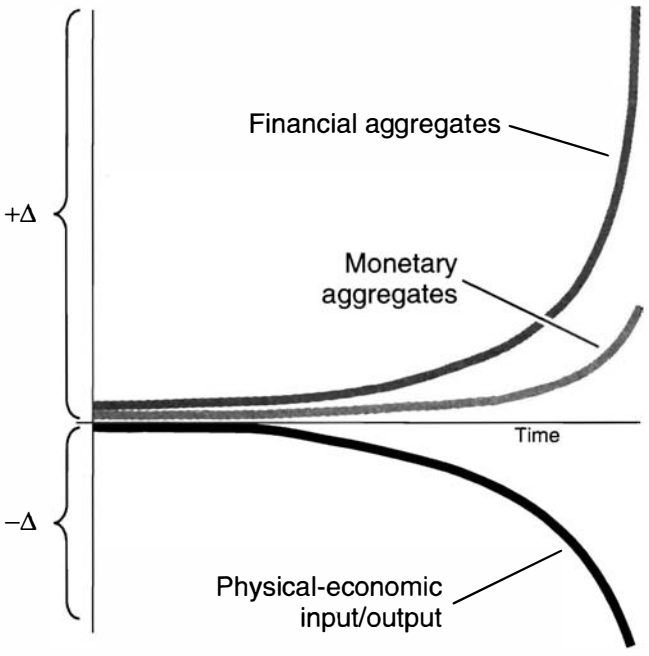
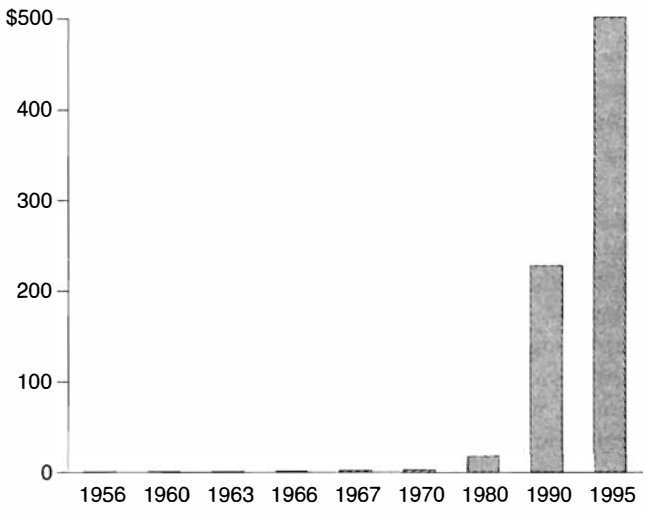


FIGURE 2
Annual financial turnover in the United States
(trillions $)



Hyperbolic growth of financial aggregates

The process which is leading the global financial system inexorably to collapse, is one in which financial and monetary aggregates are growing at hyperbolic rates, while productive economic activity declines. To feed the speculative bubble, productive activity is cannibalized; infrastructure repairs and improvements are neglected; health care, education, and scientific work are allowed to deteriorate, while the funds which should go into these sectors are instead pumped into the financial bubble. Such a system, the equivalent of eating your own flesh to stave off starvation, cannot be maintained; sooner or later, it must collapse.

To postpone that collapse, the international financial oligarchy has transformed the global economy into a giant casino, dominated by derivatives instruments. While precise figures are hard to obtain, *EIR* estimates that the level of international financial turnover has likely surpassed $1 quadrillion ($1,000 trillion), with perhaps as much as $5 trillion in paper values traded every business day, the equivalent of trading the gross domestic product of the United States every two business days, with a couple of trillion dollars left over.

In the United States, we estimate that the level of financial turnover in 1996 has reached at least $500 trillion (see **Figure 2**), in sum total of nominal valuation of all types of financial instruments traded. To keep that bubble going, the U.S. economy, and the population, have been subjected to massive looting, through such techniques as reduced wage levels, corporate downsizing, the moving of productive jobs overseas, cheating farmers, raiding of pension funds, and outright criminal activity.

Look at corporate downsizing in the United States, for example. By the end of 1996, some 500,000 Americans will have been laid off in the course of the year by corporations, compared to 440,000 layoffs in 1995, according to figures from Challenger, Gray and Christmas. Companies are laying off hundreds of thousands of employees, and shipping large numbers of productive jobs to countries where they can get away with underpaying labor, to boost their corporate stock prices, to meet the demands of Wall Street.

A recent example is Sunbeam Corp., the maker of household appliances. In November, Sunbeam announced that it would cut its 12,000-person workforce in half. Sunbeam's chairman, Al Dunlap, a notorious corporate hit man and protégé of British intelligence-linked Sir James Goldsmith, was brought in by the Wall Street funds which control Sunbeam, to gut the company in the same way he destroyed Scott Paper Co. At Scott Paper, Dunlap cut 11,000 jobs and sold the company; Dunlap received $100 million for two years' work as hatchetman.

Pension funds are another target of the financial sharks. At the end of 1995, U.S. corporations had underfunded their pension plans by $64 billion, according to the Pension Benefit Guaranty Corp. Much of that deficit came from companies controlled by corporate raiders, such as Carl Icahn, Charles Hurwitz, and Laurence Tisch.

The sharks are also eyeing Social Security and other public pension plans, and have launched a campaign to force Social Security trust funds into the stock market.

One effect of this unbridled looting in the United States, is a record level of bankruptcies. In August, the Administrative Office of the U.S. Courts reported that, for the first time in history, the number of bankruptcies in the United States had passed 1 million; for the 12-month period ended June 30, 1996, there were 1,042,110 bankruptcy petitions filed, including 297,162 between April 1 and June 30, the highest quarterly level ever. For calendar year 1995, a reported 926,601 bankruptcy petitions were filed, including 51,959 business and 874,642 non-business filings.

While individuals and companies were going bankrupt at record rates, derivatives continued to cut a swath through the public sector. In 1996, a group of Pennsylvania school districts were hit with a $2 million loss on derivatives, long after the lesson of Orange County, California, which was forced into bankruptcy in December 1994 because of derivatives losses, should have been learned. The schools joined the list of government agencies suing their investment advisers and salesmen.

All the while, U.S. banks are officially posting record profits. The derivatives holdings of the big banks continued to increase, rising $3.2 trillion in the first nine months of 1996, a rate which, if continued, will give the banks $21.5 trillion in derivatives by the end of 1996, a 25% increase over the year before.

Banking mergers were also prominent in 1996. Chase Manhattan merged with Chemical Bank, the largest merger in U.S. banking history, resulting in the growth of Chase to $305 billion in assets, knocking Citicorp out of the top spot. Chase and Chemical had some $5 trillion in derivatives between them. Wells Fargo made a successful hostile takeover of First Interstate, and NationsBank announced its acquisition of Boatmen's.

The federal government completed its takeover of Bankers Trust in 1996, with former Treasury official Frank Newman taking over as chairman of the bank, and former Federal Reserve Chairman Paul Volcker joining the board.

The Dow Jones de-Industrial Average

The big success story of 1996, from the standpoint of financial markets, was the incredible rise of the Dow Jones Industrial (more accurately, the de-Industrial) Average, from some 5,100 points at the end of 1995, to a peak of 6,548 on Nov. 25, a rise of 27% for the year (see **Figure 3**). At the end of November, the capitalization of the companies listed on the New York Stock Exchange was $7.4 trillion, an increase of 23% over the $6.0 trillion capitalization at the end of 1995.

The hyperbolic growth of the Dow, while widely touted as proof of economic progress, was an ominous sign, however, even to professional economists. On Dec. 5, Federal Reserve Chairman Alan Greenspan issued a public warning about the "irrational exuberance" of the stock market. That warning was quickly followed by leaks that the Fed wanted a "controlled deflation" of the stock market by as much as 25%, or 1,600 points, in order to prevent a crash.

"What Greenspan is proposing will not work," LaRouche warned on Dec. 7. He compared the effort to "the guy who, after he's gone off the bridge into the chasm, decides that it's time to do something to save the automobile, and perhaps himself, too, by putting his feet on the brakes."

What is coming, LaRouche said, is a series of escalating market shocks, such as the collapse of the French banking system, and international stock and bond markets, leading up to "the Big One, the general reverse-leverage implosion of the derivatives bubble," which, "in about three days, would *vaporize* every financial institution, or nearly every financial institution, in *nearly* every nation on this planet. Which would mean: forget your credit cards, forget your bank account, forget everything." The result would be that, "in major cities across the United States, probably 80% of the population would be exposed, within a matter of a couple of weeks following such a vaporization, to actual mass starvation, nothing to eat."

Input-output collapse

The bottom curve in Figure 1 schematically represents production decline in physical terms. During 1996, there were continuing declines in ratios of infrastructure provision (e.g., water and power per household, per unit area, and unit of production), in cycles of inputs and outputs of essential services (health, education, and so on), and in goods provisions for populations around the world—while millions of people are either without jobs, or misemployed.

Widespread food shortages are one obvious "marker" of this process of decline. On Oct. 13-17, in Rome, the World Food Summit was convened by the UN Food and Agriculture Organization, on "food security." The official estimate of the summit is that 800 million people (at least 15% of the world's 5.7 billion population) are now without adequate daily food.

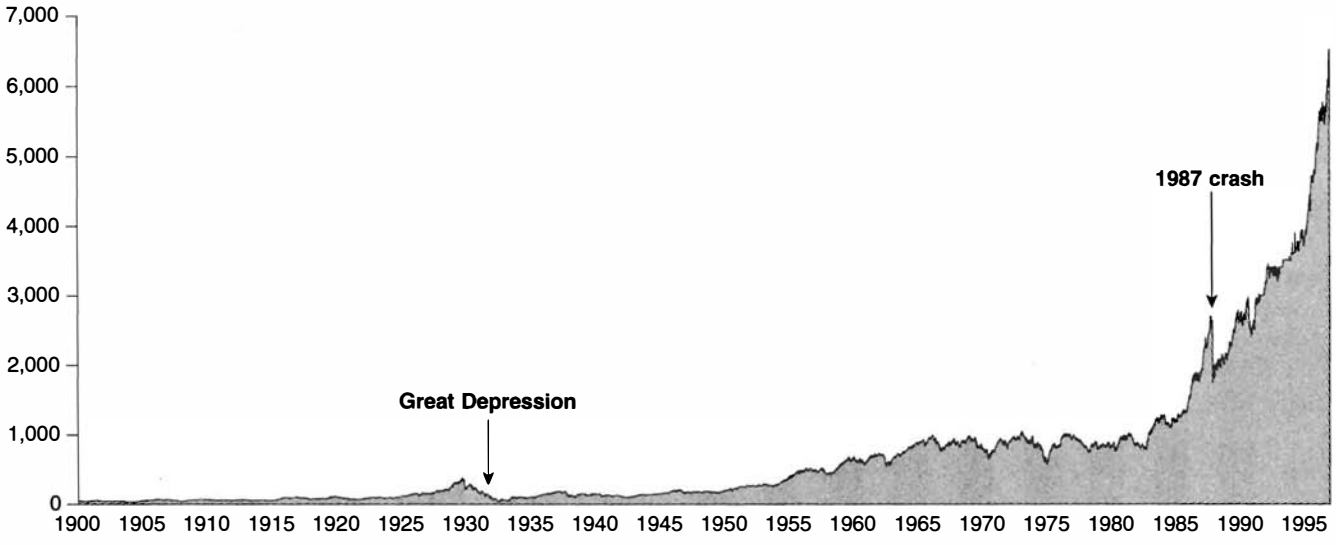
World annual grain output (all types) has leveled off at under 2 billion tons a year, while 3-5 billion tons are needed to provide decent nutrition. Therefore, in per-capita terms, 1996 marks the fifth straight year of decline in grain output. Dairy, meat, and other food commodities are far below per-capita needs.

These decreases directly reflect corresponding declines in ratios per hectare of essential farm inputs (chemicals, machinery, water), and infrastructure. Look at fertilizer, for example. In 1990, world annual fertilizer use, in nutrient tons (nitrogen, phosphate, potash), stood at 143.6 million tons, and then fell over the next five years, down to 123.6 million tons a year. In many locations, such as practically the entire continent of Africa, the 1990 levels of fertilizer use were far below requirements. However, the sharpest declines in agriculture so far in the 1990s, have been in Russia and the members of the Community of Independent States.

The Russian grain harvest in 1996 was only 67 million metric tons (official figure), far below the 80-100 million tons average of the 1980s, even under the Soviet command economy. As of 1996, on average, 35% of the current foodstuffs consumed in Russia are imported.

FIGURE 3

Dow Jones Industrial Average weekly closings, 1900-96



At a Moscow press conference on Dec. 10, Agriculture Minister Viktor Khlystun said, "The amounts of fertilizer applied have decreased from 84 to 18 kilograms per hectare. This is an appalling figure, because the extraction of mineral nutrient substances per year amounts to 26-28 kg at least, even when crop yields are low, whereas normally the figures are much higher. Therefore, we are simply exhausting the soil at present." There is a crisis disparity between the price levels farmers must pay, and what they receive. Khlystun said, "In 1996 alone, in addition to the situation that has formed over the preceding years, the prices changed as follows: prices of agricultural machinery and equipment, spare parts, mineral fertilizers from January to November 1996 went up by 60%, while prices of agricultural produce during the same period (the procurement prices as an aggregate indicator) went down by 0.8%."

What these agricultural figures reflect is the disintegration of national economies the world over.

Economic breakdown is no 'accident'

In the United States, the consequences of economic decline were evident in the frequency and severity of dramatic "accidents" in 1996—all predictable in terms of the systemic breakdown in vital sectors:

- Air transport. On May 11, ValuJet Flight 592 crashed in Florida, killing all onboard. ValuJet is a "Wall Street wonder," formed in 1993, and run as a cost-cutting/big profit operation. In early 1996, ValuJet's fleet of 51 airplanes (bought used) averaged 26.4 years of age—more than double the fleet age of America's three largest carriers (American, Delta, and United). In 1970, the average age of airliners was four years; by early 1996, the average age had tripled to 14 years.
- Rail transport. On Feb. 9, two New Jersey Transit commuter trains collided, leaving 3 people dead and 162 injured. Accidents continued throughout the year. Since 1980, some 60% of the U.S. rail workforce has been axed. Track mileage has been cut drastically.
- Water. In July, people in the nation's capital were ordered to boil their water, because, after years of lack of maintenance, bacteria flared up in Washington, D.C. water pipes, merely under conditions of summer temperatures.

U.S. economic breakdown

The decrepitude evident in these infrastructure breakdowns characterizes the overall condition of every sector of the dysfunctional U.S. economy. **Figures 4** and **5** summarize a crucial metric of the collapse—the shrinkage of the productive labor force, compared to the non-productive labor force.

Figure 4 shows, in millions of people, the size of the U.S. workforce, broken down into two sections, those in "productive" employment (manufacturing, farming, construction, infrastructure, and essential services such as education, health care, and science), and those in "non-productive," overhead employment (sales, legal, real estate, entertainment, and so on). You can see in Figure 4 how, beginning around 1970, the numbers of people working in "non-productive overhead" jobs grew far faster than those in "productive."

By spring 1996, America's workforce had grown overall to about 133.7 million (much of this growth reflecting women entering the workforce in the 1970s and 1980s), but the productive-infrastructure component of that was down to 26%; in the 1960s, it was close to 40%. Figure 5 shows how the percentage of the workforce involved in productive activity *fell by half* over the last 30 years.

FIGURE 4
Size of U.S. labor force, 1947-96
(millions)

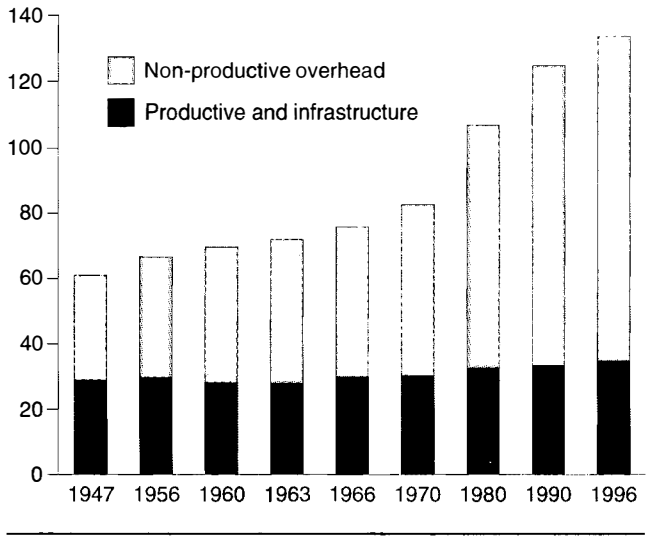
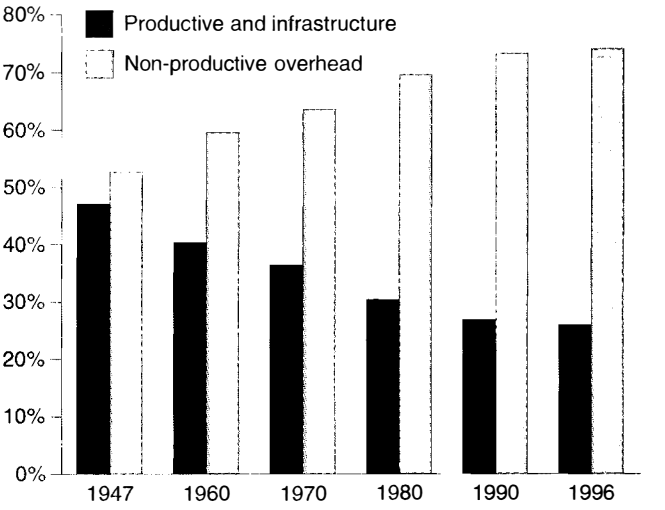


FIGURE 5
Productive compared to non-productive labor force, 1947-96
(percent of total labor force)



This means that the U.S. economy is producing and consuming at only about half the levels of the 1960s. Such as it is, the U.S. economy is import-dependent in all basic categories, from footwear to food, with terms of trade (controlled by international cartels) amounting to looting of trade partners. In manufacturing, it's called "outsourcing"; in food and agriculture commodities, it's called "global sourcing." The U.S. trade deficit set records levels in 1996. In September, the shortfall for goods alone (not services) set an all-time record of $16.1 billion.

The United States' food supply is now heavily dependent on imports, i.e., America can no longer feed itself. Half of U.S. imports come from poor nations. The U.S. position paper for the November Rome World Food Summit praised this process. The policy paper rationalized: "The United States is a major importer of food from developing countries, providing them with valuable foreign exchange. . . . For fiscal year 1996, U.S. agricultural imports are forecast at $30.5 billion. Taken as a group, developing countries have historically supplied just over half of total U.S. agricultural imports. In fiscal 1996, imports from developing countries are forecast at $16.4 billion or 54% of the total."

Even with this imperial import flow, which subsidizes the goods and services available for consumption in the United States, nevertheless, American families' paychecks have shrunk, relative to household consumption needs. In 1996, it took paychecks from three full-time jobs, to equal what one paycheck of a single manufacturing worker provided to a household in the 1950s. This means that as of 1996, the single wage-earner provider, whose paycheck could provide sufficient income for a family, became virtually extinct.

But this decline cannot continue indefinitely; social-economic breakdown is under way. About 700,000 Americans are now homeless. One in 10 Americans is getting food stamps—domestic food relief. On top of that, the demand for additional aid (free meals, food donations) rose an estimated 20% in 1996 alone.

Moreover, whole families are now showing up without shelter, food, or basic health care, in contrast to the situation 30 years ago, then the majority of homeless were single, out-of-work men.

What was the official U.S. policy response in 1996? As embodied in the so-called welfare "reform" law, enacted in August and now being implemented: condemn the people, don't change the economic policy. In February, 1 million Americans are due to be cut off food aid (no food stamps). U.S. "managed" health care is murdering people.

The so-called 1996 agricultural "Freedom to Farm" law (officially, the "Federal Agriculture Improvement and Reform Act of 1996") is phasing out all vestiges of support for farmers, and exposing them to food cartel "free market" rule. Family farm bankruptcies are now the result.

In Europe, there are parallel situations, under pressure of the Maastricht Treaty conditions; and, in other parts of the world, the consequences of the collapse of physical production are even more extreme.

What offers hope are the resistance movements and mass strikes gathering force as of the New Year, and the prospect of unleashing inspired "ingenuity," as described in the lesson of the German "miracle," to implement the economic recovery program that LaRouche has defined.