

Russian Economists Forecast: World Economic Crisis to Explode in Autumn

by Jonathan Tennenbaum and Konstantin Chermnykh

“Will the United States Manage To Bring on the Apocalypse?—The World Economic Crisis Should Begin in November of This Year,” is the title of an extraordinary article in the July 24 issue of *Ekspert*, a prominent Russian economics and business weekly. The authors, Oleg Grigoryev and Mikhail Khazin, were high-level economic advisers to the Russian government during 1994-98, who now work as independent experts. Khazin headed the credit department of the Ministry of Economics during 1995-97, then was deputy chief of economics in the Presidential Administration, 1997-98, maintaining close contact with upper circles of the government until today. Co-author Grigoryev worked for a time under well-known economist Sergei Glazyev, who now heads the Russian Parliament’s Committee on Economic Policy.

The glossy-cover *Ekspert* is a publication of the new Russian establishment, and is linked to Oneksimbank. A similarly titled article by the same authors, written in the form of a strategic memorandum and explicitly responding to the Russian government’s attempts to draft a ten-year economic policy plan, has been posted on a Russian website, linked to former Economics Minister Yevgeni Yasin. In that memo, Grigoryev and Khazin argue that any reasonable long-term policy for the Russian economy, “requires careful consideration of the international context,” but “at present, all existing programs actually *ignore* that context.”

The events of 1997-98, they say, should have taught that reality “brutally overturns” plans made without such consideration: “The crisis in Southeast Asia occurred in a manner completely unexpected for the authors of Russia’s economic strategy. . . . In the final analysis, it was also unexpected by the majority of Western analysts. The failure was, to fail to take into account the implications of the crisis for Russia, and to correct economic strategy accordingly. As a result, August 1998 hit Russia in the most devastating way.”

This time, especially if “the situation in the world economy looks relatively favorable from the standpoint of Russia’s development” (due to revenues from lucrative oil exports), the economists urge Russia not to “overlook developments that cannot be extrapolated from the present,” or “omit making preparations for necessary measures, in response to such eventualities.”

The significance of the Grigoryev-Khazin article in *Ekspert* may be appreciated upon reading through their entire

argument, which we excerpt here. The translation, subheads, and addition of emphasis are *EIR*’s.

The ‘New Economy’

“When, at the end of 1997,” Grigoryev and Khazin begin, “the authors of the present article prepared their first briefs for the President of the Russian Federation on the impending crisis in Russia, they pointed out a certain similarity between processes in Russia and the United States. At that time, however, there was no point in writing official reports to develop the theme of the coming crisis of the world financial system, because they would have just been laughed at. Today, this theme has become quite popular, and may be discussed in all seriousness.

“Unfortunately, when the overwhelming majority of sources talk about the world economy today, they look exclusively at the phenomenon of the so-called new economy, and they analyze it exclusively at an empirical level. The preference for an empirical approach is understandable: The short history of the new economy has allowed no time for constructing adequate models, so modern science cannot precisely define, whether the new economy has approached a critical line, has crossed it, or may yet have more reserves for stabilization.

“One thing, however, is incomprehensible. The new economy is viewed in isolation, although it would seem to be more logical to analyze the interaction of the new, information sectors, with the traditional, industrial ones, and to utilize this analysis for forecasting the overall economic situation. This is what we have attempted to do in the present article—to describe the interaction of the new and the old sectors of the economy, and identify the mechanism of the eruption of a world economic crisis, which we believe may begin this Fall.”

The Russian article first analyzes the bubble of the “new economy,” as a critical factor in the rapidly oncoming U.S. economic catastrophe. Unlike previous technological revolutions, which had led to broad increases in productivity and living standards in the real economy, “the latest technological revolution, associated with the development of information technologies, did not develop in that way. As yet, there has been no observable impact by the new, information sector, on the traditional sector, with respect to any significant increase of labor productivity and rates of profit. We are speaking not of management and marketing technologies, which have

experienced a marked change, but of production technologies, which have not. The chief reason for this phenomenon, we believe to be the huge difference in the time it typically requires to bring innovations on line, in the new and in the traditional sectors of the economy. Any attempt to renovate industrial production, in line with the very latest ‘information technologies,’ becomes obsolete in the planning stage, since several new generations of computers and software appear already during that period. . . . As a result, there is no ‘material,’ technological linkage between the information and the traditional sectors of the economy; each develops on its own, and the gap between them continues to widen.”

People’s Needs Are Met by the ‘Old Economy’

Using the terminology of the Russian Kondratyev school of economics, about phases of technological development of the economy, Grigoryev and Khazin write, “Besides the lack of penetration of the old economy by the new, which is necessary for the formation of a coherent technological phase, the new economy also has failed to edge out the traditional sector in terms of *consumption*. The basic needs of real people are still met by the traditional economy. Moreover, a significant number of those who use the information sector’s products could get by without them, without suffering particular ill effects. Therefore, the new economy had to seek different applications. This has had two interesting effects.

“First, the new economy itself became the major purchaser of the services of the new economy. A *gigantic virtual bubble*’ began to inflate, the size of which greatly exceeded the dimensions of the umbilical cord which connected it with the old, or real economy. The second effect, is that the primary commodity provided by the new economy is the *sale of new mechanisms of sale* for the products of the old economy. As a result, the greater part of investment in the new economy goes for new, Internet-based *marketing technologies*.

“The current value of commodities . . . cannot be changed significantly by the use of intermediary services, however advanced they might be. Therefore, almost all new economy companies are valued on the basis of their future profits. . . . This model for the determination of value has been adopted and is maintained on the basis of a general consensus. This is because, insofar as the network for the sale of such companies is developing, and future profits depend on their exponential growth, all investors can register superprofits. This model became the base of the new economy’s enormous growth, . . . allowing it to provide rates of profit *an order of magnitude higher* than what would correspond to the real state of the new economy.

“This situation, however, undermines the new economy itself, which too much resembles a financial pyramid scheme, the stability of which largely depends on strictly *psychological factors*.”

The authors note that the U.S. economy would have fallen into a deep crisis long ago, were it not for the dominant world

role of the dollar and “globalization.” They continue:

“The collapse of the world socialist system, and the grab by the United States and its allies for the markets that had been controlled by the U.S.S.R., extended the growth phase of the U.S. economy for several years. This reserve was exhausted rather quickly, however, so that by the early 1990s, there was every reason to expect a crisis. But, the new economy flourished just in time to attract any excess financial resources, making possible a repetition of the phenomenon of 1920s—rapid growth, with practically no inflation—and to postpone the stage of overheating for approximately ten more years. Now, this time is up.”

The Trigger

“The rapid growth of the new economy in the mid-1990s led to a significant increase in the income expectations both of individuals (households) and of institutions. Consequently, the cost of credit for industry rose significantly. As a result, industry turned more and more toward resource-conserving regimes of activity, and its rate of development through its own, internal resources slowed. Costs rose. It became more difficult to attract young, skilled specialists, because they headed for the more financially lucrative sectors of the new economy. . . . Since the major criterion for the work of U.S. managers has long been the share value of their companies,

GENOCIDE RUSSIA AND THE NEW WORLD ORDER



Russia in the 1990s: “The rate of annual population loss has been more than double the rate of loss during the period of Stalinist repression and mass famine in the first half of the 1930s . . . There has been nothing like this in the thousand-year history of Russia.”
—Sergei Glazyev

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Economist Dr. Sergei Glazyev was Minister of Foreign Economic Relations in Boris Yeltsin’s first cabinet, and was the only member of the government to resign in protest of the abolition of Parliament in 1993.

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these problems could be ‘hidden in the accounts ledgers’ for a certain time. . . .

“The profitability of industry decreased ever more steeply, on a global scale, which led to a significant rise of the minimum level of production, necessary for generating a profit. The ratio of companies’ internal capital to borrowed capital, steadily decreased. For purposes of economizing on resources, there was a wave of mergers of companies operating in similar areas; international monopolistic concerns were established in practically all markets. . . .

“We view the persistent and steady decline of profitability of the old, real economy, primarily industry, as the trigger of the future global economic crisis.”

Turning to the events of 1997 on the financial markets of Southeast Asia, Grigoryev and Khazin emphasize that “these markets served as a safety valve for the U.S. economy, and with their collapse, *the only remaining possibility to postpone the crisis in the United States itself, was to employ non-economic mechanisms, like the aggression in Yugoslavia.*”

The Symptoms in the U.S.A.

Concerning the internal dynamic of the U.S. economy, the Russian economists write:

“The enormous growth of the virtual economy ‘bubble’ had to cause an accelerated (by comparison with the growth of industry) increase of consumption. The lengthy period of growth and success of the new economy resulted in a decrease of U.S. citizens’ savings rate. They began to spend more, while also increasing their *debt obligations*.”

“With rising interest rates, this process had to provoke *inflation*. The first signs of inflation appeared in 1998, when the U.S. had a budget surplus for the first time in many decades. But, for a long time the inflationary processes were not reflected in prices on the [goods] markets, thanks to the skilled and competent efforts of the Federal Reserve System.

“By the end of 1999, however, *the Federal Reserve could no longer contain inflation*. The critical point was reached in March-April 2000, when *the annual rate of inflation in the United States, drew even with the average profitability level of industrial production*. . . . The Federal Reserve’s attempts to combat inflation by raising interest rates, undermined the financial situation in industry even more.

“The qualitative deterioration of industry provided evidence of *the absence of any objective basis for the growth of the Dow Jones index*. This index, which had been steadily rising for many years, has stalled out since the beginning of the year 2000, in the 10-11,000 range. *The profitability of stock-market investment has sharply declined*, simultaneous with intensified speculative activity by its professional participants, which has increased the amplitude and frequency of its fluctuations. Since then, the magnitude of each latest decline has come to depend on a combination of various trivial and accidental factors, while the fluctuations of the stock index have become an important indicator, of how close the United States is to the onset of the collapse.”

The Politics of the Crash

The Russian authors emphasize, that the approaching “psychological disturbances,” related to the U.S. Presidential elections, will significantly magnify the fragility of the system.

“The U.S. Presidential elections, in November of this year, define two possible scenarios. The first one plays out in the event that the U.S. financial oligarchy keeps control over the two major parties. In this case, nothing will happen before the elections; *but immediately thereafter, the truth about the real state of affairs, will necessarily appear in the mass media by early November*, when the balances from two quarters of the business year begin to be published, likely triggering the dumping of shares of industrial companies.

“We note, that *the oligarchs are preparing for the crisis*. In the Fall of 1999, a U.S. law [the Glass-Steagall Act] forbidding combination of any two of the three forms of business (banking, brokerage, and insurance), was repealed. This law had been adopted after the crisis of 1929, in order to protect the interests of small investors and to prevent excessive speculation with other people’s money. The repeal of this law will allow the owners and top managers of financial institutions to save their personal fortunes after the onset of the crisis (just like in Russia, in the Fall of 1998).

“The second scenario would unfold, if the leadership of the U.S. Republican Party were to behave relatively independently. In that case, it might push to accelerate the crisis—firstly, in order to guarantee victory in the election, and, secondly, to force the Clinton Administration to take the first and most unpopular measures after the crisis broke out. This second scenario is suggested by the recent statement of Federal Reserve Chairman Alan Greenspan, about the onset of a crisis in the next few weeks, or, more precisely, in late August.

“The rapid collapse of the stock market will wipe out assets estimated at \$10 trillion (the April crisis on the NASDAQ ‘cost’ about \$2 trillion). This will sharply accelerate *inflation*. . . .

“There will be mass bankruptcies of financial institutions, whose assets largely consist of securities of mutual funds, insurance companies, venture capital, and pension funds. The trillions of dollars of liquidity, which investors manage to pull out of the hardest-hit sectors of the economy, will be invested *in any available long-term assets*. This will cause a sharp rise in the prices of gold, other precious metals, real estate, and other kinds of durable property.

“For most banks, securities are not a significant part of their assets, but securities are used for liquidity management. Moreover, a substantial quantity of their loans are guaranteed by securities, owned by the borrowers. The bankruptcy of some financial institutions and serious problems of others, will significantly undermine the American and global economies.

“Our very preliminary calculations suggest that world average consumption levels will fall by a factor of 1.5 to 3. . . .

“The governing bodies of the international corporations

will be incapable of reacting quickly to the rapidly changing conjunctural situation. Consequently, they will begin to shut down production, which will bring serious protests from the national authorities, who do not want an increase of unemployment, at a point when social programs have been scaled back. This will lead to the collapse of the World Trade Organization [WTO] system and the re-establishment of traditional mechanisms for the protection of national markets. This process will also be driven by the loss of the U.S. dollar's function as an international currency, a niche into which the euro [European single currency] will be unable to move with any speed.

"In order to support national industries, which will be suffering from the credit shortage under severe crisis conditions in world financial institutions, many countries will switch to national credits for domestic industry. This effort will fan inflation, but increase the competitiveness of domestic industries on world markets.

"We believe that the interaction of mechanisms for the protection of national markets will define the development of the global economy in the first post-crisis years.

"The crisis will profoundly change the correlation of forces in the global economic arena. The weakening of the U.S. economy (aggravated by powerful social upheavals) will hit those regions, which derive a significant part of their income from sales in the United States — above all Japan, China, and Southeast Asia. Serious stagnation will take place in

[western] Europe, too, but it may secure powerful investment potential by expanding the role of the euro. In part, this will be directed toward Latin America.

"After the destruction of the WTO system and re-establishment of protectionist mechanisms, the situation in the world economy will be very reminiscent of the early 1930s. A small quantity of major international monopoly concerns, a multi-currency system, high unemployment, rising social tensions, inflation and stagnation — these features will define the picture of the world economy at the start of this new century."

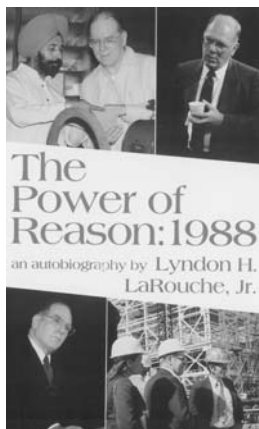
The authors anticipate that the collapse of world stock markets will be "a rather abstract event" for Russia, with the exception of the loss of individual savings — not the first time this has happened in the recent period. They believe that large amounts of loose money, desperately seeking sound investment prospects, are likely to select the natural resources of Russia, in the form of long-term (30-50 year) concessions for their development.

In conclusion, the authors insist that the perspective given in their forecast could be acted upon by the Russian leadership, given the factor of *little available time*, only in cooperation with an economically strong Western partner. In view of "historical Russian business traditions, Russia's relations with Western countries during recent decades, and the existing volume of investment," Grigoryev and Khazin propose that this partner should be Germany.

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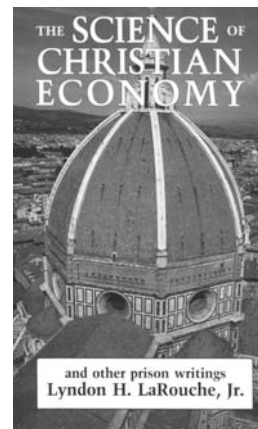
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