Domestic Credit by Leif Johnson

The GNP inflator

How the Commerce Department manages to produce statistical leaps while industrial output continues to sag.

Analysts in the United States have traced the most recent rumors of Yuri Andropov's ill health to reports that Andropov injured himself by laughing too hard at the batch of "economic recovery" figures released by the U.S. government on Oct. 21. The court jesters at the Commerce Department claimed that the U.S. economy experienced a whopping 7.9 percent increase in the Gross National Product for the third quarter of 1983, while inflation was held to a mere 3.4 percent.

And once again acclaim for "the upswing" could be heard the length of Pennsylvania Avenue. White House press spokesman Larry Speakes hailed the GNP figures as proving "an impressive pattern of non-inflationary growth. We now expect the economy to continue at a sustainable rate of growth in the months ahead."

Commerce Secretary Malcolm Baldrige chimed in: "The economy has entered an expansion phase, although a few specific industries are lagging behind the overall pace of the economy."

EIR is in a position to explain why even Russian economists are shrewd enough to see through the hoax.

First, consider the plain fact that the value of steel output is lower than a year before, industrial power consumption is down, machine tool orders are one-fifth of 1979 levels, all basic metalworking continues to drop, and this is becoming the all-time record year for U.S. bankruptcies."

The method behind the provision of entertainment to Yuri Andropov is as follows. Gross National Product (GNP) is simply the sum of transactions in the economy, including manufacturing sales, retail sales, service sales, and other payments. GNP says "product" but in fact does not measure any product. It measures the dollar value of transactions in the economy, regardless of the nature of those transactions.

For example, as Economics Editor David Goldman and I have documented (see *EIR*, Aug. 9, 1983), the GNP compilers add in the amount of interest paid in the economy. Interest payments are not a "product"; in fact, when interest rates are at usurious levels as at present, these payments are a net drain on real product. But the way the GNP is calculated, the rise in interest payments hides the drop in real product. When interest rates go up, as at present, the GNP goes up, other elements remaining equal.

This is why GNP continues to rise during economic slumps or falls only mildly in the worst of downturns.

The way the Commerce Department constructs the GNP, if interest rates went up to 25 percent and everybody traded used cars and clothing, and if absolutely noting was produced, the GNP would rise.

Of course, people would complain that the GNP was just reflecting price increases and not more production. Therefore, the Commerce Department deflates the GNP statistics for price increases—but the trick here is to underestimate the real rate of inflation.

We show in the current *EIR* Quarterly Economic Report that the Bureau of Labor Statistics' Consumer Price Index has understated inflation of some consumer durables by as much as half over the past dozen years.

For example, the cost of an automobile has risen slightly more than threefold since 1967, according to the Motor Vehicle Manufacturers Asociation. Yet the Bureau of Labor Statistics claims that the price of an auto has only doubled since 1967.

Since Commerce uses the BLS's Consumer and Producer Price Indices to deflate the GNP, the GNP figure is inadequately deflated, i.e., grossly overvalued.

Thus the GNP is not only not a measure of product, but a measure of financial transactions in the economy, but those transactions are not properly adjusted for inflation.

In remarks made to the Joint Economic Committee of Congress on Oct. 20, Paul Volcker, chairman of an institution that has been in the forefront of the "recovery"-mongering, made an interesting comment. Volcker told the committee that "foreign competition, a slack labor market, and spare factory capacity give the United States a rare opportunity to build in greater stability."

What kind of stability is built on depressed industrial conditions? It is the stabilization of interest income at the expense of industrial production—exactly the internal transfer in the economy that the GNP is design to hide by counting interest and rental income as "product."

Volcker added, "There are strong grounds to believe that underlying inflation is lower—and can continue to move lower—than is generally perceived." Although the Fed is not directly involved in producing the inflation numbers, Volcker was either saying that the BLS will more energetically falsify the inflation figures or that the economy will continue downward.