Debt burden decimates real U.S. production

by Richard Freeman

The National Association for Manufacturing Technology, formerly known as the National Machine Tool Builders Association, has announced that orders for U.S.-made **machine tools,** at $226 million for August, were down 33% from the level of August 1988. The "spin-masters" of the media and the machine tool association tried to make the data look good by noting that machine tool orders had at least risen from the previous month of July's level.

Machine tools are the machines that produce other machines, the most critical sector of the economy, upon which economic expansion and capital formation are based. Hence, while the machine tool sector is minuscule—at $3.0 billion in annual sales it is but .06% of Gross National Product—its contraction gives a direct reading of how the usurious debt bubble leeches out life from the economy.

As *EIR* reported in our Sept. 8 issue, the total debt of U.S. business swelled nearly fivefold in 16 years, from about $1 trillion in 1973 to $4.85 trillion in the first quarter of 1989. Though official figures cannot be obtained, a best estimate is that *the annual interest service charge on this debt rose,* for business, from close to $85 billion in 1973 to $450 billion in the first quarter of 1989.

The U.S. Department of Commerce does publish a figure, from its internal sources, that nets out the difference between what business pays out on its borrowings over what it earns on its holdings. This "net interest" in 1973 was $22.5 billion; by 1987, the last year for which figures are published, it had grown to $98.6 billion. What is startling is the comparison of the net interest a corporation paid and its retained earnings or retained profits. In 1973, business retained earnings were 158% the size of net interest; in 1987, only 28%. Thus in 1973, there were $1.58 in retained profits for each dollar a business paid in net interest; in 1987, only 28¢ in retained profits were available to cover every dollar cost in net interest. The resulting cash squeeze shows up partly in the slash in real capital formation.

The **oilfield service** industry, which is a gauge of all U.S. energy production, has also been devastated. Out of 106 publicly held oilfield service firms operating in 1981, at the height of the oil-drilling boom, 42 have been liquidated, sold, or have discontinued oilfield service-related operations. Matthew R. Simmons, president of the Houston consulting firm, Simmons and Co. International, said that 1989 "will go down in the record books as the worst ever for the oilfield service industry—worse than '86 or '87." J. Steven Larkin, executive vice president of the Houston-based Petroleum Equipment Suppliers Association, expects bad times to continue. "Everybody agrees that at some point this market will turn around. But I'll bet you can't find anybody that will hazard a guess when that point will be." Larkin said that 60% or more of the oilfield service industry's sales originate overseas, as the drilling rig count for the U.S. continues to hover around 900, compared to the average of close to 2,500 rigs working each day from 1977 to 1986.

Declining trade

The industrial contraction skewered **trade.** Imports of industrial supplies and capital goods fell sharply in both June and July. As a result, total imports shrank by 2.5% in July, to $38.3 billion, after a 3.1% drop in June. Outgoing shipments of manufactured goods also declined in July, combining with lower agricultural exports to lower U.S. exports to $30.7 billion in July. The U.S. trade deficit "fell" to $7.6 billion in July. The government crowed over this "smaller" amount, a deficit still larger than most countries run in a year. But not only will this deficit not stay long below $10 billion a month, this "trade turnaround" comes from falling industrial activity.

Finally, the labor force cannot buy basic necessities, like houses and cars. **Housing** statistics released in September showed that housing starts, after rising 7.4% in June and 1.3% in July, fell back 5% in August to 1.35 million starts on an annualized basis. For the first eight months of 1988, new home production is 11% below 1988 levels—which are 10% below 1987's. Real unemployment in the construction industry lingers at 20-25%. **Auto** dealers discounted heavily to get rid of 1989 models. In August, autos sold at a 8.3 million annualized rate. But in September, the minute the discounts were taken off, sales fell to a 7 million annualized level. Production usually closely follows sales.

For the whole U.S. economy, inventories of unsold goods are piling up. In July, the ratio of inventories to sales rose to 1.54, a 2 and a half year high, before easing off in August. Even this depressed level of consumer production wholly depends on credit. **Consumer borrowing,** represented by consumer installment credit, rose $2-5 billion per month between February and June. In July, consumers paid off $280 million more than they borrowed, and the shock wave of collapse in the physical economy amplified. In August, a brief respite occurred; consumers borrowed again, but the economy still went downward.

But as consumer borrowing buys less and less, and as credit costs more and more, consumers will borrow less. At this point, several retail stores, already on the verge of bankruptcy, shut down, more construction companies fold, and the shock front in the physical economy takes over to the extent that the U.S. economy closes in on itself.

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