EIR Economics

We were right; they were wrong

by John Hoefle

The economics establishment never likes to admit it is wrong, and it hates even more to admit that *EIR* is right. But the record is clear. The LaRouche-Riemann econometric model, with its solid grounding in economic science, has consistently beat the establishment's tea leaves and other forms of superstitious prognostications. Once again, we were right and they were wrong.

In the *EIR Quarterly Economic Report* for the fourth quarter of 1985, *EIR* wrote: "Unless present policies are reversed, the underlying economic collapse of the United States, estimated at a rate of 2.5% per annum, will accelerate during 1986, to perhaps pass over the line into the deflationary part of the depression process. Vulnerabilities that have accumulated under the evil and misguided policies that produced the so-called 'Recovery of 1983-84' create the potential for a further 15-30% rachet collapse in living standards, from the levels of the 1960s and early 1970s, and for a further estimated 9-15% reduction in the physical economy.

"There are, of course, measures available to *postpone* the approaching disaster. Such has been done before, by monetary and related authorities, at each turning point in the post-1967 destruction of the Bretton Woods monetary system. Each time, such postponement has made the next round of crisis that much worse."

EIR's warning was ignored by the policymakers, who continued to insist that the nation was enjoying steady, uninterrupted economic growth. The "recovery" was in full swing, the "experts" pontificated. President Reagan, and now President Bush, counted off the "straight months of economic recovery," one by one, amid much fanfare and hype.

Meanwhile, the economy continued to collapse.

The line abruptly shifted in late November of this year. The press, in a quick about-face, began to write about the troubles on Wall Street, and even about the possibility that a "recession" was under way. Various economists and financial specialists were trotted out to announce that suddenly, somehow, the robust United States economy was in trouble.

None of this was news to the average American, who has seen his standard of living plummet during the so-called recovery, and has long since learned to ignore the incompetent pronouncements of the so-called experts. But the fact that the line changed so radically is significant, because it exposes the underlying desperation and panic of the financial community.

The most important of the new revelations came from the *New York Times*, in its Nov. 20 business section. In an article entitled "Data Are Signaling Bad Slump," the *Times* reveals, "With the release of each week's data, the message is growing clear: The United States is suffering from a severe downturn, perhaps the worst of the last seven years. This month brings the seventh anniversary of the economic expansion that began after the 1982 recession, an unusually long period of prosperity that nevertheless was nearly interrupted by two earlier downturns, in 1984 and 1986. The current one began to show itself in late summer."

"What was that?" the reader might ask. "Downturns in 1984 and 1986? Funny you never mentioned them before. All you talked about in 1984 and 1986 was the great recovery." In its typically understated and indirect way, the *Times* revealed a great truth: The emperor's recovery has no clothes.

The *Times* tries to downplay this stunning admission as if it were nothing new, claiming that the 1984 downturn "was confined mostly to the manufacturing sector . . . while the 1986 downturn resulted largely from plunging oil prices." In fact, the paper claims, the 1986 slowdown was so subtle that "no one knew the economy had contracted for a while in 1986; that was not discovered until July 1988, when the Commerce Department updated its earlier data." Nevertheless, the premier mouthpiece of the Eastern Establishment has indeed confessed. Pandora's box is open, and no amount of sophistry can close it.

The only thing the *Times* forgot to admit was, "*EIR* was right, and the *New York Times* was wrong." Or perhaps more accurately, "*EIR* told the truth, and the *New York Times* lied." Readers of *EIR* should not hold their breath waiting for the *Times* to make either of those admissions, however.

Why we were right

The proper approach to the science of economics begins with the understanding that the role of economics is to maximize the continuing process of the survival of society as a whole. Economics is not about money, as the so-called "experts" would have you think. It is about what mankind must to do to ensure that current and future generations can survive, and thrive, overcoming the challenges that face them, creating an ever-increasing standard of living for all mankind.

In order for society to thrive, it must have in place mechanisms to ensure that a process of continued and interdependent generation, transmission, and efficient assimilation of scientific and technological progress is maintained, such that the transformation of land and the productive powers of labor are maximized. Such a process means that the amount of average land-area required to sustain an average person is constantly being reduced, while thermodynamic throughput and energy intensity are increased through capital goods investment. Thus, the realized standard of physical consumption of the average person is augmented. The result is an increase in the potential population-density of the society, which is the standard by which the productivity of economies are measured.

The process is self-expanding and nonlinear. A rise in technical progress creates the conditions for an increase in potential population-density, fostering the conditions under which such advances can be put into general use by the population. That potential increase, if realized, then leads to a further increase in potential population-density, and thus increases the likelihood that the speed of technological progress will increase.

Conversely, a break in the process causes the reverse effect, with a slowing of the rate of technological progress, and a resulting decrease in potential population-density, causing the standard of living to inexorably rachet downward. This conceptual, moral framework is the basis for any competent economic work. It is from this standpoint that policies must be made, and evaluated.

Why they were wrong

The self-proclaimed experts of the economic establishment have rejected this viewpoint, insisting that such issues as morality and the welfare of mankind have no place in economics. They view economics in the narrowest possible way, as a matter of money and markets, in which the behavior of the markets is paramount, and the needs of mankind are subservient. They ignore the real world, and immerse themselves in the artificial world of high finance, where such concepts as "right" and "wrong" give way to the more bestial "profit" and "loss."

Profit and loss have become the standards by which the economy is popularly measured, with all profit contributing to the artificial statistic known as the Gross National Product. When the GNP is rising, the experts proclaim, the economy is healthy. It makes no difference, the experts maintain, whether the profits come from heavy industry or houses of ill repute.

The various "schools" of economics differ somewhat in their specific approaches to the economy, but they all share the same basic flaws. Their grand, computerized models are of no more value than the gypsy's tea leaves, and no more accurate.

Where we go from here

The United States has entered into a deflationary spiral of economic collapse. The collapse of the junk bond "industry" set into motion an unraveling of the financial system which is threatening to ruin everything in its path. The huge bubble of debt built up over the years of the Reagan-Bush recovery is absolutely unpayable, and it is crushing the banks and investment houses. The major Wall Street investment banking houses are desperately laying off personnel and looking for financial saviors. The money center banks have suffered devastating drops in the values of their stocks since the Friday the 13th crash in October, some losing as much as one-third of their value. Real estate values around the country are collapsing, wiping out huge chunks of investment and threatening to blow out regional banks. The retail sector is verging on bankruptcy. Industrial firms are closing right and left, laying off employees. Pensions are in jeopardy, from both looming industrial bankruptcies and from failed investments.

The response of Wall Street's financial elite has been to inflate the debt bubble even more. Suggestions have been made that consumer debt be allowed to double, and that all homeowners take out second mortgages or home equity loans to pump more money into the system. The Federal Reserve has decided that banks should be allowed to double the amount of their assets and loans for the same amount of equity capital, overruling the capital standards proposed by the FDIC.

The call has gone out to postpone the inevitable collapse a bit longer by engaging in a flurry of hyperinflation, thereby looting the public one last time. Such policies are economically insane and morally bankrupt, and absolutely cannot work.

Unless these policies are changed dramatically, and the principles of economic science applied, we will once again be in the tragic position of telling the economics establishment: "We were right, and you were wrong." Next time, however, it may be too late.