LaRouche 'Typical Collapse Function' Confirmed by U.S. Economy, 1996-2001

by EIR Economics Staff

Lyndon LaRouche's Dec. 2, 1995 conference address in Germany, "We Are at the End of an Epoch," first introduced his "Typical Collapse Function," or "Triple Curve" idea, to make the point that if monetary and financial processes shown were allowed to continue, the major nations of the world would undergo outright collapse of their physical economies. The Triple Curve (see p. 5) gave an econometric form to LaRouche's "ninth long-range forecast" made in 1994, in which he warned that a global financial bankruptcy and collapse would be under way by the time President Bill Clinton left office, unless Clinton and other leaders dramatically changed economic policies.

The economic data of the American economy from that time to the current crisis completely vindicate LaRouche's Triple Curve schematic. Graphs of the relevant U.S. economic statistics (however inadequate the available data), document and verify LaRouche's forecast of what would ensue, if policies were not changed. In the figures below, we provide indicative representations of key components of this collapse process.

LaRouche stressed in 1995, both at the German conference, and at an earlier Rome colloquy, where he first introduced the "Triple Curve" diagram, that the world economy at the time, was already in serious decline. "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." Referring to the fact that "the American people produce *half as much* as they did 25 years ago, and consume about half as much, for various reasons," he stressed: "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" (*EIR,* Jan. 1, 1996).

He described the interplay of the three curves—not mathematical calculations, but directionalities which characterize the collapse process. The bottom curve is the productivity and functioning of the physical economy, upon which all human existence depends; the middle curve shows increase in monetary aggregates (approximately represented by money supply measures); and the upper curve shows growth—which can become hyperbolic growth—in financial aggregates of all kinds: run-up of debts and other obligations, speculation in currencies, stock markets, futures (derivatives), etc. As in the case of a "typical collapse function," the interaction of the upper two curves sucks the underlying physical economy dry.

Here we review several elements of each of these curves, making reference to certain key government policy responses year-by-year, which furthered the collapse process, to the breakdown point we face today. The final figures shown are snapshots of the actual *collapse process now under way in the United States.*

Financial Aggregates Zoom Out of Control

Figures 1-3 show aspects of the volume and trends of certain financial aggregates—the LaRouche diagram's "top curve"—for recent decades, highlighting (shaded area) the six years following the 1995 LaRouche warning.

In **Figure 1,** "U.S. Credit Market Debt" is shown, which includes all types of borrowings (corporate, household, consumer revolving credit, etc.) kept as a category by the Federal Reserve statistics, but excluding certain types of government debt. The time period is 1952 through the third quarter of 2001.

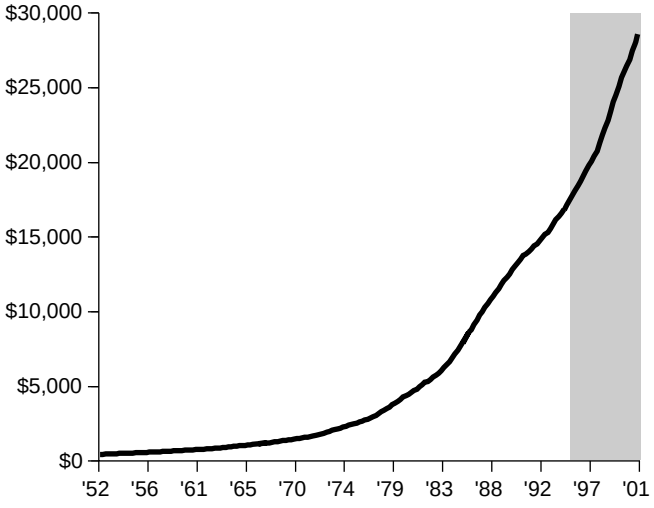
It is clear that the rate of rise through the mid-1960s was minor. But the rate of increase took off in the 1970s and 1980s. This time-phase change, is a pattern seen across other key readings on the American economy, as it shifted into the "post-industrial" decline.

In the years following LaRouche's forecast—1996 is noted on the graphic—the rate of U.S. indebtedness continued to grow, and at an even steeper rate. Today, it is at the level where whole categories of debt-holders are unable to service their obligations, from personal credit card accounts, to steel mills. Insolvencies are evident in the record incidence of bankruptcies and defaults. In November 2001, U.S. consumer borrowing increased by $19.8 billion, an annual growth rate of 14.8%. The monthly dollar increase was the biggest since the Federal Reserve started keeping its records in January 1943. Though no downturn may yet be visible in the volume

FIGURE 1

Financial Aggregates: U.S. Credit Market Debt, 1952-2001 (3Q)

($ billions)

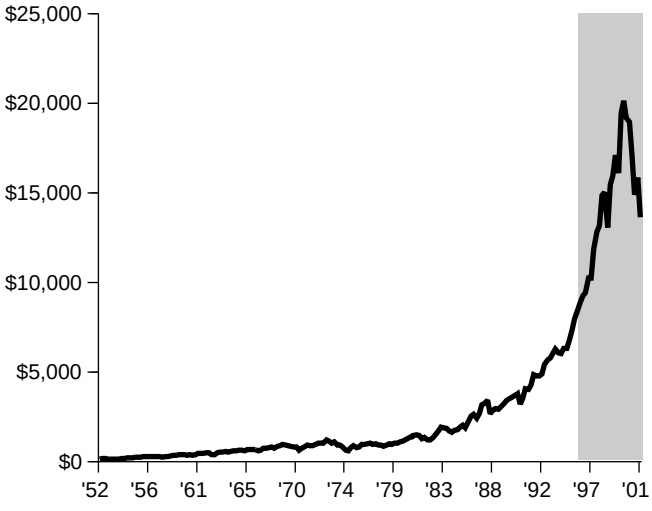


Source: Federal Reserve Flow of Funds

FIGURE 2

Financial Aggregates: U.S. Corporate Equity, 1952-2001 (3Q)

($ Billions)

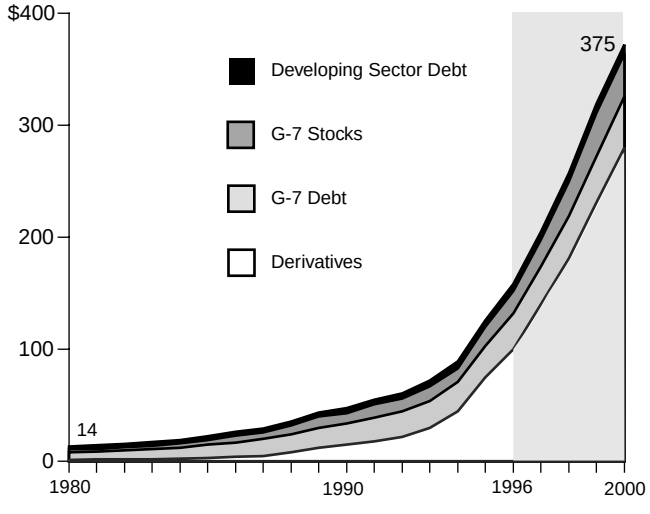


Source: Federal Reserve Flow of Funds

FIGURE 3

World Financial Aggregates, 1980-2000

(Trillions $)



Sources: Federal Reserve Board of Governors, "Flow of Funds Accounts"; OMB, "Budget of the U.S., Fiscal Year 2001, Historical Tables"; Bank for International Settlements; World Bank; *EIR*.

of debt outstanding in the Fed's figures, that statistic will change almost instantly in a crash.

Figure 2 shows "Corporate Equity," the financial category of valuation of stocks, for the same time period, 1952 to 2001's third quarter. First, notice that the same slow rate of increase is apparent from the 1950s through the mid-1960s. Then, in the 1970s, there was more volatility in equity values; and a real take-off occurs in the late 1970s. By the time of LaRouche's warning—1996 is again indicated—the "bubble"-rate of rise in stock values was well under way. Then, with the New Economy info-tech frenzy, stocks soared to an amazing peak as of early 2000. By Spring, the dot-com meltdown began, and since then the "Old Economy" stocks have been plunging as well.

- The Nasdaq capitalization (the number of shares of stock times per share value) was $6.7 trillion in March 2000; then stood at $2.9 trillion in December 2001.
- The New York Stock Exchange capitalization was $12.9 trillion in August 2000, and $11.7 trillion in December 2001.
- U.S. Corporate equity overall that was $20.1 trillion in the second quarter of 2000, was $13.7 trillion in the third quarter of 2001.

Figure 3 shows four categories of financial aggregates for the world, from 1980 to 2000. The same run-up since 1996 is notable. Stock values for the G-7 are shown continuing to rise from 1996-2000 (Group of Seven, being the United States, Canada, Italy, France, Germany, Japan, United Kingdom), and also G-7 debt. Growing relatively less is the "Developing Country" debt. Rising dramatically, and accounting

for most of the "financials" bubble in the world, are *derivatives.* These contracts are futures bets of all kinds (hedges, swaps, or so-called risk-management instruments), which, as a category, did not even exist prior to the 1980s.

What about 2001? While not shown graphically, the current or near-future condition of much of the global skyrocketting indebtedness, is made clear by recent events in one location: Argentina. As of December 2001, the biggest national debt default in history took place there. Similar situations are pending in Turkey, Poland, and the "Big One"—in Japan. The debts are unpayable.

'Wall of Money'

What has propped up the unprecedented heights of indebtedness, stock values, and other financials? Looting of the physical-economic base of the economy, as shown in graphs further below, and a "wall of money" policy of hyperinflation, as shown in **Figures 4** and **5** (which refer to the middle of the three curves on the Triple Curve diagram).

But at a certain point in the 1999-2000 period—which we graph in more detail further on—no matter how much money is injected, the financial bubbles cannot be kept aloft! The rate of rate of growth of monetary aggregates becomes higher than the rate of rate of growth for financial aggregates. In graphical terms, this is the "inevitable crossover" point of the middle, monetary curve, breaking up through the top, financial curve.

In 1997, as the breakdown of the global financial/monetary system expressed itself in the mis-named "Asian" crisis, LaRouche warned against continuing International Monetary Fund (IMF) policies, and, in particular, against pursuing the "printing press" approach to money supply.

On Feb. 17 that year, international parliamentarians joined with him to launch a mobilization to "annihilate the IMF," and he outlined a threefold program for what course should be taken by national leaders at the time. He called for collaboration to convene a New Bretton Woods conference to devise sound financial and monetary measures for restored national economies, utilizing the best of "what worked" during the 1946-66 first Bretton Woods period. Secondly, he called for an international mobilization for global infrastructure development—led by building the "Eurasian Land-Bridge" projects; and thirdly, for a commitment to fostering nation-state economies, with machine-tool sector development, to create conditions for self-generated economic growth.

As the year progressed, and IMF-policed assaults on Asian and other economies intensified, LaRouche repeated his warnings. Specifically attacking the resort to money-pumping, he likened such a policy to the hyperinflation in Weimar Germany in 1922-23, and he commissioned an *EIR* research feature on it (Richard Freeman, "Hyperinflation in Weimar Germany," *EIR,* Jan. 30, 1998).

Speaking on Jan. 17, 1998, at an international conference in Alexandria, Virginia, LaRouche warned: "We're on the edge of coups throughout Asia and Southeast Asia, as a result of IMF policy. In the meantime, the policy which the United States government, including the Clinton Administration presently, by default, is conducting, is a hyperinflationary policy, which will blow up the value of money into nothingness, quicker than John Glenn can get into space, through an attempt to maintain financial aggregates by pumping in money fast enough to keep the aggregates going, under so-called bailout techniques, IMF bailout.

"What does the IMF say? The IMF says: *Cut* your production. *Accelerate the cutting* of per-capita output. *Increase greatly* the monetary output in order to cover, and prime up, and pump up the financial aggregates, which are already skyrocketting." LaRouche noted that it took Weimar Germany 18 months to two years for the German Reichsmark to disintegrate, and the same would happen on a world scale at some point ahead, unless measures were taken to stop the hyperinflation and the IMF monetarist insanity.

However, as 1998 drew to a close, the money-pumping policy was even more frantic. This came in response to a series of financial crises. In August that year, soon after the Russian government defaulted on short-term bonds, the huge Connecticut-based hedge fund, Long Term Capital Management (LTCM), was caught out wrong on billions of dollars of speculative bets, and failed in September. The chain-reaction impact of LTCM threatened a meltdown of the financial system. In response, instead of taking public-interest-serving measures, the Federal Reserve, U.S. government officials, and London/Wall Street interests collaborated in a "bailout of the bankers," one part of which was a massive increase in money supply.

This liquidity-pumping accelerated again in 1999 in response to the so-called "Brazil crisis" and the "Argentina crisis" of that year. At that time, the strategy was actually given the name, "the wall of money policy," by its own advocates—most prominently, by mega-speculator George Soros at Davos in February 1999. Worldwide, this was intensified under the hoax of "contingency" preparation for the asserted Y2K computer changeover period. Under these massive money infusions and related policies, the Nasdaq stock index skyrocketted.

LaRouche warned again and again of the hyperinflationary insanity. In early 2000, as hyperinflation hit oil and gasoline prices, he said on March 8, following the Super Tuesday 16-state primary elections, "There is a *global* hyperinflationary spiral in the process of taking off." Referring to the gas pump prices, he said, "This is simply, predominantly—it is not some 'market this, and market that'—it's a hyperinflationary process, which has taken off."

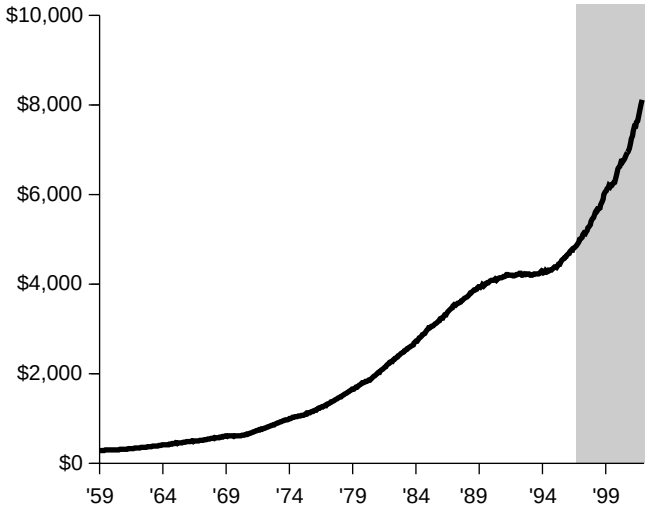
Extraordinary Collapse Function

In the Spring of 2000, LaRouche issued his updated version of the 1995 Typical Collapse Function (see previous article), to depict, as he said on June 3, 2000, in a paper on

FIGURE 4

Monetary Aggregates: U.S. Money Supply (M3), 1959-2001

($ Billions)

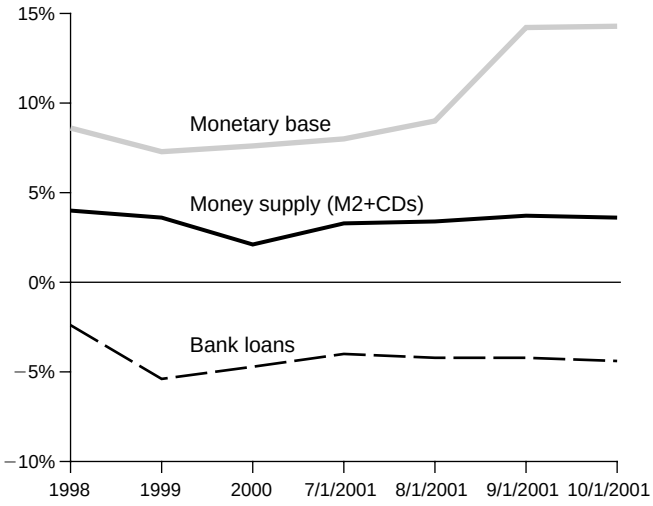


Source: Federal Reserve

FIGURE 5

The More Japan Prints Money, The Less Banks Loan To The Economy

(Percent Change)



Source: Bank of Japan.

world monetary reform, that there is "a point at which the rate of monetary expansion rises more rapidly than the rate of financial expansion [it is feeding]. The latter is the condition into which Germany had entered over the interval March-October 1923."

Figure 4 gives the value of money supply in the United States, called M3, from 1970 through 2001. Clearly rising throughout, the rate of rise after 1996 is spectacular. Last year, Federal Reserve Chairman Alan Greenspan made an unprecedented series of 11 interest-rate cuts. For 2001 as a whole, the fundamental measure of U.S. money supply known as MZM grew at an extraordinary 23% rate; the broader M3 measure grew by 12.8%. We face today exactly the chaos that the hyper-liquidity policy brought to Germany, but this time on an international scale.

Figure 5 gives monetary trends in Japan, the nation for which interest rates were effectively at the zero level for a prolonged period of time in recent years. Today Japan—the second largest and economy and financial system in the world, is facing a financial meltdown. With an impossible load of many trillions in indebtedness, and Japanese banks holding approximately $1.5 trillion of bad loans, "walls of money" printed by the Bank of Japan no longer work to sustain debt, bad or good.

The graph, giving 1998 through September 2001, shows three things. The "monetary base" of the nation (the Bank of Japan's loan mechanisms for providing liquidity) has increased at the rate of 9% a year, and then in October, it went up a drastic 14.3%. Meanwhile, the money supply (the cash and certificates of deposit which consumers and businesses are putting into circulation by going about their business), is staying flat, at the 3% to 4% rate of increase a year. And bank loans are negative! The Bank of Japan's liquidity pumping is no longer functioning.

Properly speaking, this situation is not truly a "Japan" or a "yen" crisis, but the prelude to the crash of the *dollar system* itself.

Figures 6 and **7** show the dramatic fall since the 1970s, in two key aspects of the real, physical economy in the United States: manufacturing workers employed (1979 to 2001), and machine-tool production (in units and in dollars, 1974 to 2001). The manufacturing workforce declined significantly from 1970s levels. Since LaRouche's 1995 forecast/warning, the decline has been catastrophic. It is estimated that from Summer 2000 to Summer 2001, the hardest-hit category of the 1.2 million layoffs, was the manufacturing sector.

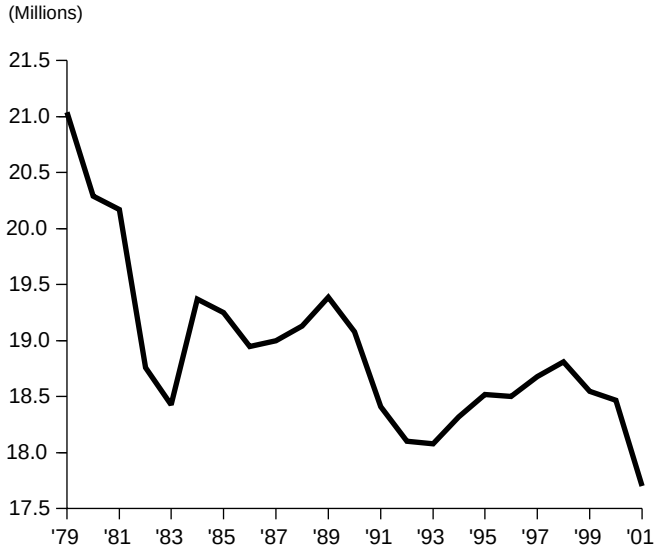
Machine tools—the heart of an industrial economy—dropped in U.S. production by over half in the last 30 years, and at present, the fall in output is headed toward shutdown.

Instability Becomes Collapse

Shown next in **Figure 8,** are key components of the LaRouche-specified Triple Curve components for the United States economy. In order to show the combined development of the three types of curves, they are indexed back to their levels of 1996—the time of the circulation of LaRouche's

FIGURE 6

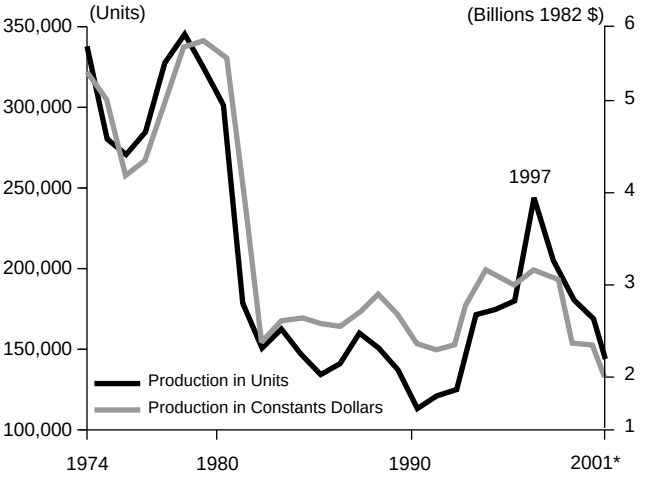
The Physical Economy: U.S. Manufacturing Worker Employment



Source: U.S. Department of Labor.

FIGURE 7

Physical Economy: U.S. Machine Tools

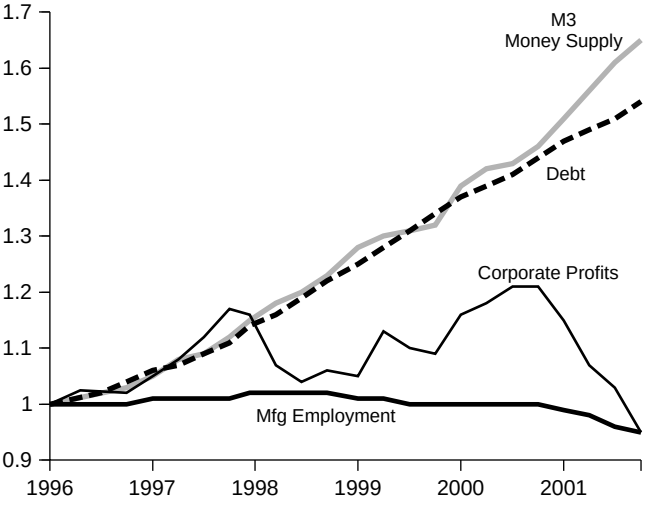


* projected, based on first three quarters of 2001.

Sources: Association for Manufacturing Technology; U.S. Department of Commerce; *EIR.*

FIGURE 8

The U.S. Economy's Collapse Function Since 1996



Source: EIRNS.

original Collapse Function diagram. Just as he said, what is associated with perpetuating the upper curve of the financial bubble—depicted by the rising debt curve (debt, as defined in Figure 1), are a soaring money supply (M3, as in Figure 2), and the decline in the physical economy, shown in the manufacturing employment falling.

What also jumps out from these data-based curves is verification of the second version of the LaRouche Triple Curve diagram in 2000. In this second stage—which might be called an extraordinary collapse function—the "crossover" LaRouche forecast as a result of the "wall of money" policy has indeed occurred. The central monetary (M3) curve has broken up through and beyond the financial-aggregates curve (debt) which it was sustaining. This "crossover" effect occurred in the 2000 as LaRouche had warned it would. The rate of money emission has increased at hyperinflationary rates, but with less and less effect on "supporting" the financial curve.

Meantime, the decline in manufacturing workers accelerates, as the instability of the system has sent the actual physical economy into collapse. A fourth line on the graph relates to that, showing that corporate profits are now plunging. Corporations cannot service their debt, do not have income levels required to continue to do business, and no amount of easy-money from Fed Chairman Greenspan's hyperinflation machine is helping.

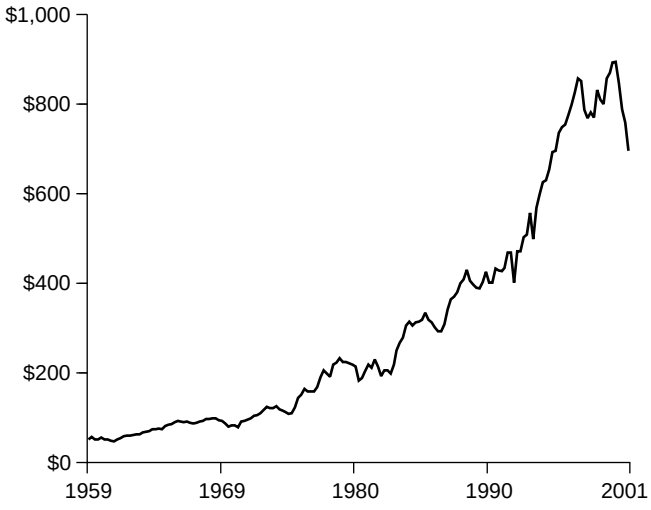
Figures 9-11 show three aspects of the economic/financial collapse now in progress. In **Figure 9,** the level of U.S. corporate profits is shown from 1959 through 2001's third quarter. They now are approaching a hyperbolic rate of fall.

Associated with this process, are the number of annual bankruptcies of U.S. public companies, 1985 to 2001, shown in **Figure 10.** Some of these big-name Chapter 11 filings, such as Bethlehem Steel (October 2001), are still in operation,

FIGURE 9

The Physical Economy: U.S. Corporate Profits, 1959-2001 (3Q)

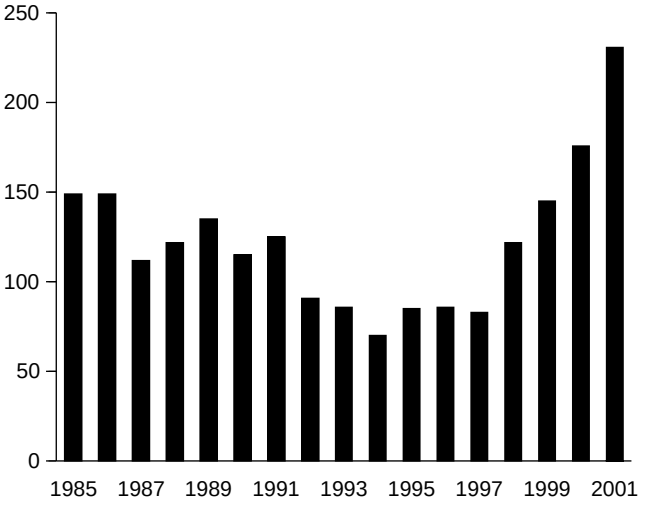
($ billions)



Source: Federal Reserve

FIGURE 10

Bankruptcies Of Public Companies, 1985-2001

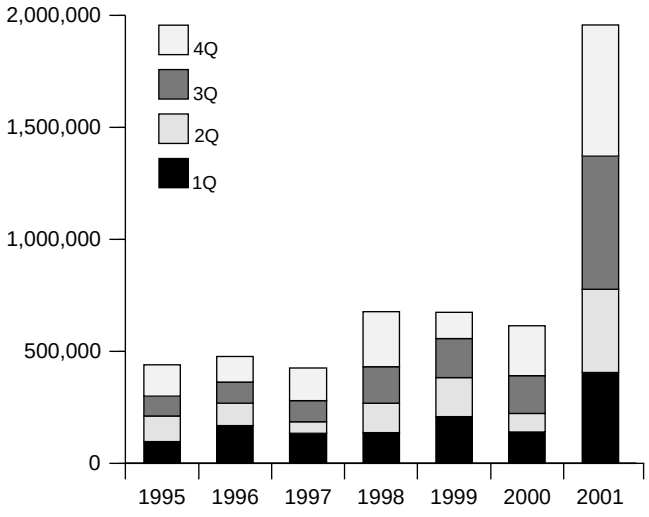


Source: BankruptcyData.com

FIGURE 11

The Physical Economy: Mayor U.S. Layoff Announcements, 1995-2001

(Numbers of Companies)



Source: Challenger Gray & Christmas

but others represent closures and liquidations, on a scale now eroding the remaining economic capacity of the nation.

The final illustration of this shutdown process, in **Figure 11,** portrays the numbers of major U.S. layoff announcements each year, from 1995 through 2001. While all the announced cuts have not necessarily been implemented, and while some repetition occurs, the catastrophic trend is clear.

The biggest job-cut year ever, 2001, had almost as many layoffs announced as in the three previous years combined. Moreover, the bar column which is divided into the four quarters of 2001, shows clearly that none of this can be blamed on the impact of "Sept. 11" as the key factor. By that point, a record number of job cuts were already promulgated. We are on the brink of all-out breakdown.

Thus, the 1995 LaRouche Triple Curve is entirely proven by the U.S. economy's evolution into today's collapse crisis. But it is not, nor was it intended to be, a blueprint. It described processes which ought to have been reversed, but were not, because key leaders chose not to heed LaRouche's warnings.

LaRouche's evaluation, as of two years ago, is still a call to action. Speaking Jan. 11, 2000, on a live video webcast from Boston, he summed up the collapsing system: "And it's coming down fast now. No one can say, predict, what day is the market going to collapse. It's collapsing already, in one sense or the other. It's caught between deflationary threats, hyperinflationary threats, wars spreading all over the world, a new war every month or so, which doesn't seem to quit. A new scandal, a new destabilization. We're in a crisis worse than that of the 1930s. We're in a crisis of the type, which, in terms of worldwide strategic implications, is the kind of thing that gave us Adolf Hitler in World War II."