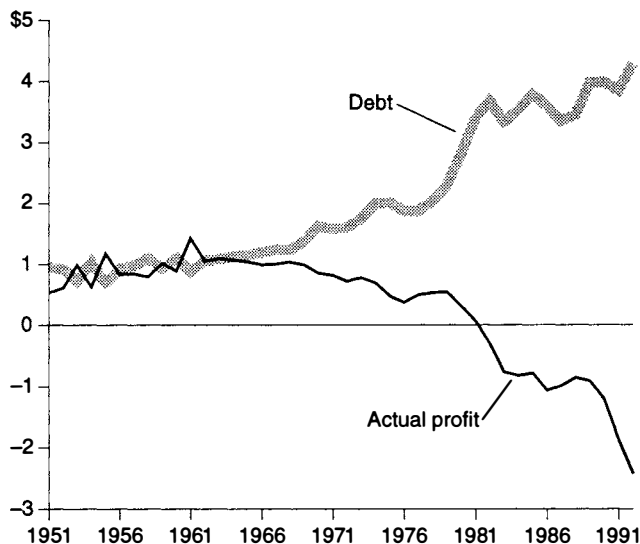


FIGURE 8

Pumping the bubble only makes it worse

(debt or actual profit for every dollar of reported profit)



Source: EIR.

by pumping it up, only made things worse. The greater the so-called profit from the bubble, the more money the real economy loses.

Currently, for every dollar of so-called profit, we lose \$2.50 and incur \$4 in debt, for a total loss of \$6.50 per dollar. That's like going down to the store and buying dollars for \$7.50 apiece, and then taking that dollar, and calling it profit. Furthermore, the guy we're borrowing the money from to buy these dollars, doesn't have any money either: He's stealing it from somebody else. That "somebody else" is the rest of the world. We're stealing money from Ibero-America, from Africa, from Asia, from the former East bloc countries, looting their populations and our own, to keep the bubble afloat.

The solution to this crisis begins with recognizing the disease, the decay and inevitable disintegration of the existing central-bank monetary system, LaRouche said recently. Nothing can be done, and nothing should be done, to save the system. You have to tell the patient to give up the diseased organ; otherwise the patient will die.

"What we have to do, very simply," LaRouche said, "is to seize the U.S. Federal Constitution, and the work of Treasury Secretary Alexander Hamilton, the work of Henry Carey, of Friedrich List, and Abraham Lincoln, with both hands, and say, 'This was good; let us eliminate that which replaced it, which is now dying, and let us bring it back into operation.'"

LaRouche's method of physical economy

by Dennis Small

The following is the second part of Small's presentation, continuing from p. 23.

So, how did LaRouche know the Mexican crisis and the derivatives crisis were coming, when all the established authorities insisted otherwise? It's a question of method: not of what people think, but the way they think. In other words, if someone is always wrong, it is probably because they are thinking wrong; if they are usually right, it is because they are thinking right.

Let's start with some people who are always wrong: the winners of the Nobel Prize in Economics. In fact, one of the criteria for even being considered for the Nobel Prize, with the single exception of France's Maurice Allais in 1988, is to have an economic theory with no demonstrable relationship to actual physical economic reality. That puts you in the running. But then to make it to runner-up status, you have to use your delusional theory to make consistently erroneous forecasts. However, to actually win the Nobel Prize, you then have to go on to apply your policies to at least one country resulting in that nation's economic disintegration. Then you win the big one.

Take the case of 1970 Nobel winner Paul Samuelson. He is the guy who came up with the idea that depressions could never again happen, thanks to "built-in stabilizers" which automatically take care of everything. Samuelson is kind of the "What, Me Worry?" of economists.

In his 1955 textbook, which has been used for decades to rinse generations of professional economists, he pronounced: "The modern fiscal system has great inherent automatic stabilizing properties. All through the day and night, whether or not the President is in the White House, the fiscal system is helping keep our economy stable. If in 1980 a recession gets under way while Congress is out of session, powerful automatic forces will go instantly into action to counteract it before there are any committee meetings or the exercise of special intelligence of any form."

Most Nobel winners have followed Samuelson's dictum of doing without "the exercise of intelligence of any form." In 1974, the guru of the fascist Conservative Revolution, Friedrich von Hayek, won the award. Two years later, the University of Chicago's Milton Friedman won it. His view

can be summarized as the belief that the only thing that matters is money supply—production is entirely irrelevant. Friedman has led the campaign for drug legalization, and holds the British crown colony of Hongkong as his model.

In 1990, Harry Markowitz and Merton Miller won the Nobel Prize for developing something called “portfolio theory,” which argues that futures contracts, just like other “products,” are valuable to those who buy them, and so they should not be regulated by the government. In 1992, Gary Becker was favored for, according to the Nobel committee, “having extended the domain of economic theory to aspects of human behavior which had previously been dealt with—if at all—by other social science disciplines such as sociology, demography, and criminology.” Becker, like Friedman, is for legalizing drugs and for eliminating the minimum wage.

But things get wilder as the years go by. In 1993, Robert Vogel won the Nobel economics prize for his 1974 book defending U.S. slavery as economically progressive. And last year, John Nash, John Harasanyi, and Reinhard Selten received the honor for their pioneering work in the field of game theory, i.e., the theoretical justification for the world derivatives crap game.

Bad ideas, bad methodology.

LaRouche’s method of physical economy traces back to Leibniz. It rejects as useless any monetary measurement of the economy, such as Gross National Product (GNP) and balance of payments, none of which can distinguish between the value of a million dollars invested in a steel plant and the same million invested in the construction of casinos and warehouses in Las Vegas or Acapulco. Instead, in order to determine which kinds of productive activity increase the technological power of each member of the workforce with respect to nature, the LaRouche method measures the physical production of consumer goods, of the means of production, and of basic infrastructure, which is useful for the reproductive economic process, and also measures its effects on the productivity of the labor force. All of this is measured by densities per capita, per household (the basic unit of social reproduction), and per square kilometer of total land and/or land in use.

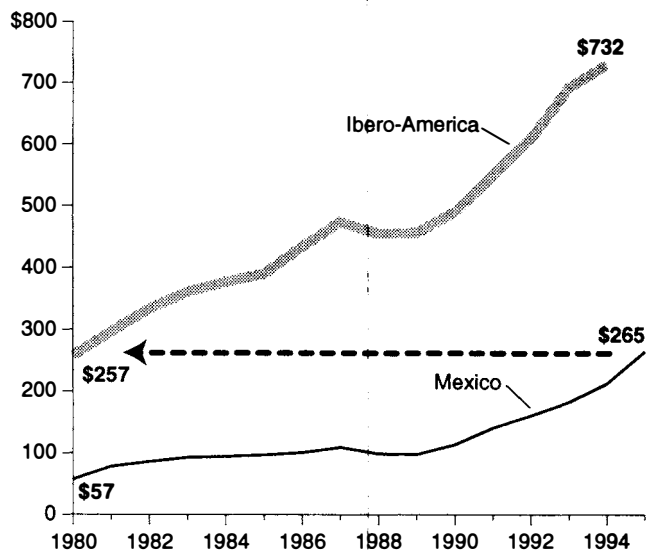
Economic success is most clearly expressed by the exponential increase in the relative potential population density of society.

The fundamental source of such continuous improvements in social reproduction, LaRouche has emphasized, is human creativity—that quality which distinguishes man from, and makes him superior to, all other animal species. With this in mind, a properly growing physical economy must meet the following four criteria or constraints:

1) The per capita and per household consumption of the workforce must rise.

2) The consumption of producers goods must also increase, and at a more rapid rate than that of consumer goods—that is, production must become increasingly capi-

FIGURE 1
Mexico and Ibero-America debt compared
(billions \$)



Sources: World Bank, EIR.

tal-intensive.

3) Energy density per household and per square kilometer must also increase, as must the energy flux density of the power sources employed—i.e., they must become more efficient as well as more dense. This is closely correlated with leaps in applied technologies.

4) The “free energy of the system” must increase relative to the total energy of the system. That means that even as the economy requires ever higher consumer and producers goods market baskets, the total output of the economic cycle must rise more rapidly still, making increased proportions of total output available for reinvestment and expansion. This latter requires constant technological progress, and therefore human creativity. In other words, there is no “steady state” economy: There is either growth, or there is decay and collapse.

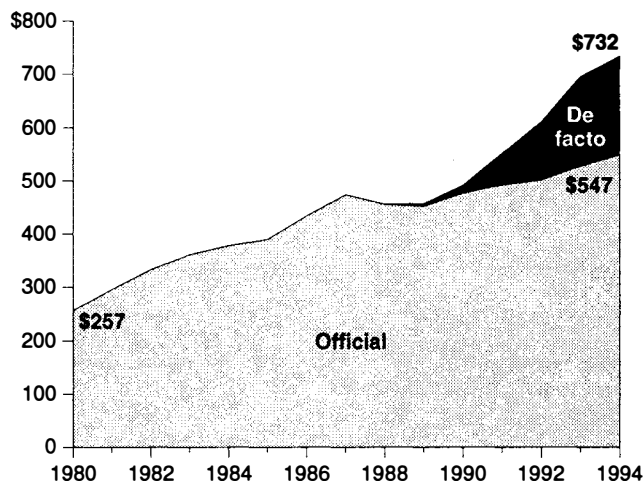
Let’s briefly apply this approach to Mexico and Ibero-America as a whole, and see how they have fared. As we explained earlier, the last 15 years have witnessed a sharp rise in the speculative bubble called Mexico’s real foreign debt, which rose from \$57 billion in 1980 to a projected 265 billion in 1995—a nearly fivefold increase. As you can see, this is more than the foreign debt of all Ibero-America back in 1980, which was then \$257 billion (Figure 1).

Ibero-America’s official foreign debt, in turn, rose from \$257 billion in 1980 to \$547 billion in 1994 (Figure 2). But there are an additional \$185 billion in other foreign obligations—the hot money bubble of bonds and stocks that has erupted since 1989—which bring the total real foreign debt

FIGURE 2

Ibero-America's real foreign debt

(billions \$)



Sources: World Bank, EIR.

up to \$732 billion, nearly three-quarters of a trillion dollars. So Ibero-America's real foreign debt nearly tripled over this time period.

I want to emphasize that this amount of debt is not a problem in itself, so long as the rate of growth of the physical economy underlying it is more than keeping pace with it. In fact, I would propose that the nations of Ibero-America have no need to repudiate this debt outright; they should recommit themselves to paying it . . . after a 20-30 year debt moratorium or cessation of payments, during which time they would studiously reject British free market economics, and instead channel all their resources into real physical economic growth. With regional integration, great development projects, and emphasis on twenty-first century technologies, Ibero-America can easily attain 10% per annum growth rates of tangible output, which over the course of two decades would mean a sixfold rise in output, and over three decades would mean a sixteenfold jump. And all of that is without taking into account the non-linear leaps that technological revolutions would bring about. So, the problem is not the debt; the problem is the growth of usurious debt combined with a collapsing physical economy.

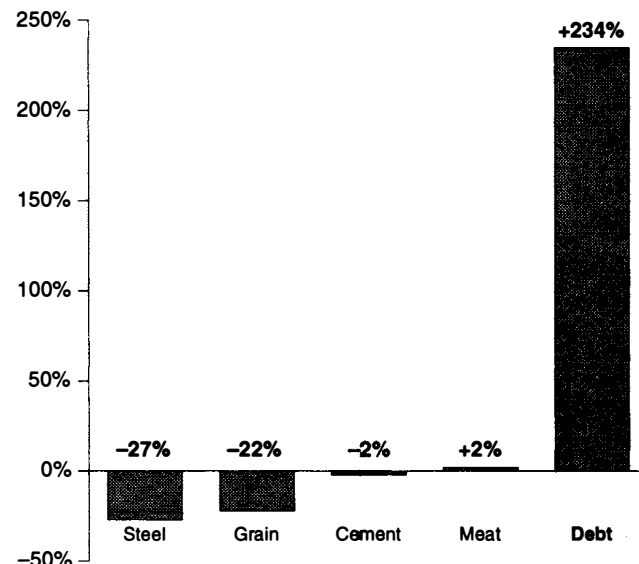
So, how did Mexico and Ibero-America fare in this regard over the past couple of decades? Look back at Figure 3 on p. 17. It shows the production of consumer and producer goods in Mexico, measured exclusively in physical economic units per capita and per household. While the debt was soaring over the '80s and '90s, real physical output was collapsing.

As Figure 3 shows (this page), between 1981 and 1993 steel production per household fell by 27% in Mexico, grain

FIGURE 3

Mexico: growth of foreign debt versus production, 1981-93

(percent change)



Sources: World Bank, ECLAC (United Nations), INEGI (Mexico).

by 22%, and cement by 2%. Meat production per capita rose by a paltry 2%. The official foreign debt, however, soared by 234%.

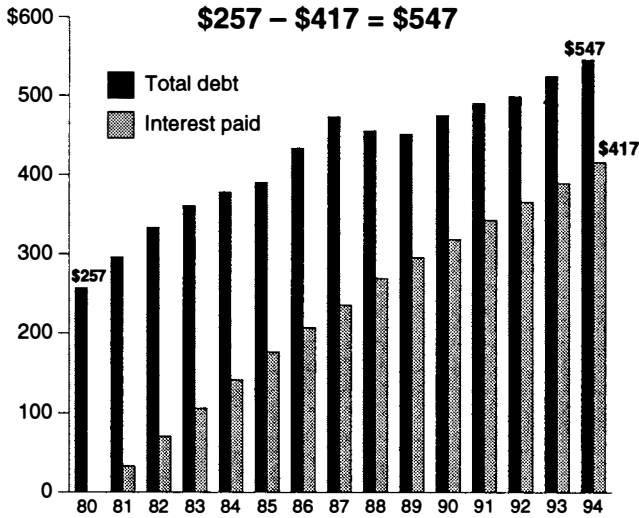
Are you still wondering how LaRouche knew that the Mexican model was going to explode? Perhaps we had better look at Ibero-America as a whole to see if the same thing is going on there.

In Figure 4 we are looking at the growth of Ibero-America's official foreign debt from 1980 to 1994 and the cumulative interest paid over that same period. For example, Ibero-America's debt in 1980 was \$257 billion. Over the course of the next 14 years, they paid \$417 billion in interest payments alone, i.e., excluding amortization of principal. And yet at the end of that period, they owed more than at the beginning: \$547 billion. In other words, as you can see as clear as day, $\$257 - \$417 = \$547$. That's what I call "bankers' arithmetic."

(It is true that some portion of the increased debt actually meant a flow of new resources into the region. But in general, this was more than offset by additional outflows in the form of amortization payments and illegal capital flight. So the "bankers' arithmetic" calculation is a simplified, but accurate, reflection of the net capital flows.)

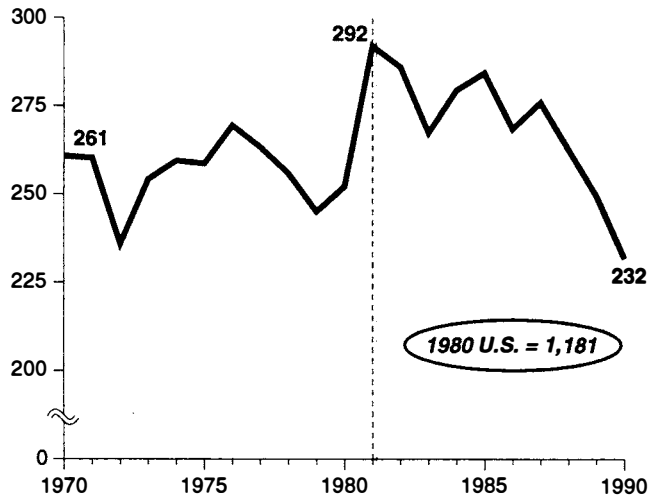
Not surprisingly, this debt looting process has taken its toll in the physical economy. To help calculate that impact, EIR has just developed preliminary market basket indices of production of consumer goods and producer goods, which are similar to those developed earlier for Mexico—although

FIGURE 4
Ibero-American foreign debt, and interest paid
 (billions \$)



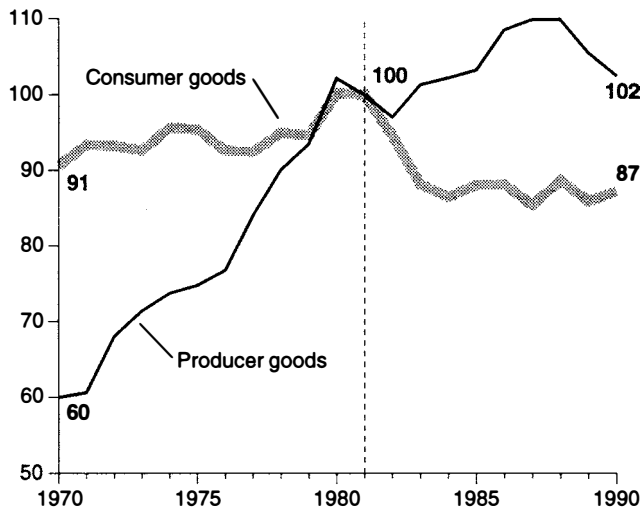
Source: World Bank.

FIGURE 6
Grain production in Ibero-America
 (kilograms per capita)



Sources: ECLAC (United Nations), FAO, U.S. Department of Agriculture.

FIGURE 5
Ibero-America: producer and consumer goods production
 (index 1981=100)



Source: ECLAC (United Nations).

containing fewer products (8-10) so far (Figure 5). The results are conclusive: As with Mexico, Ibero-America saw a period of modest growth in both indices during the 1970s, but then stagnation and outright decline, after the 1981 turning point. Compare the growth of debt obligations and pay-

ments in Figure 4. Do you see the problem?

Just how bad are things in Ibero-America?

As Figure 6 shows, grain production per capita, which is the centerpiece of any economy's ability to feed its population, rose by a meager 12% from 1970 to 1981. But between then and 1990, it plummeted by 21%, and although more recent numbers were not readily available, it is likely that it has declined further from 1990 to 1994. The 1990 level for Ibero-America was 232 kilograms per capita, which compares with 1,181 kilograms per capita in the United States in 1980.

The picture for steel is no better (Figure 7). Ibero-America's per household output in 1990 was no higher than what had been achieved 10 years earlier. Compare this 391 kilograms per household, with 1,406 in the United States in 1980.

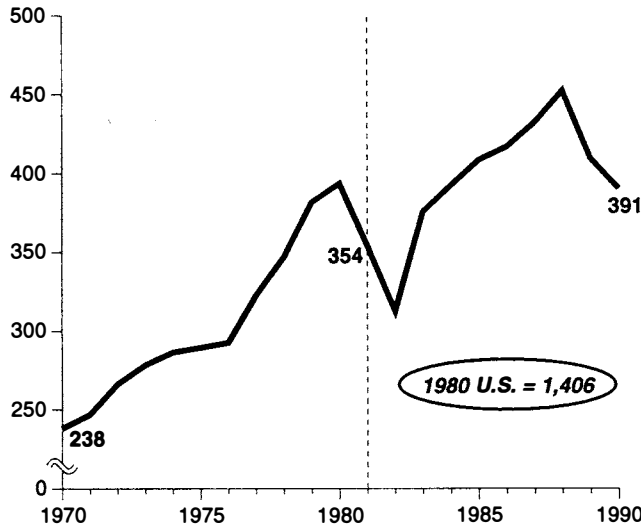
The long and the short of it, is that the policies of the IMF and the international oligarchy are Africanizing Ibero-America—they are rapidly reducing the region to conditions in which its physical economic reproduction will break down entirely, as has already occurred in large parts of Africa.

I want to conclude this section of the panel by making a forecast. First of all, the \$50 billion package for Mexico may have bought some time, but it will in all likelihood not even get Mexico through 1995 in one piece. Mexico has about \$63 billion in foreign obligations coming due with certainty over the course of 1995, which will overflow the \$50 billion bailout. But there are an additional \$45 billion in other foreign obligations (certain *Tesobonos*, foreign investment in the stock market, etc.) which could also potentially be called in

FIGURE 7

Steel production in Ibero-America

(kilograms per household)

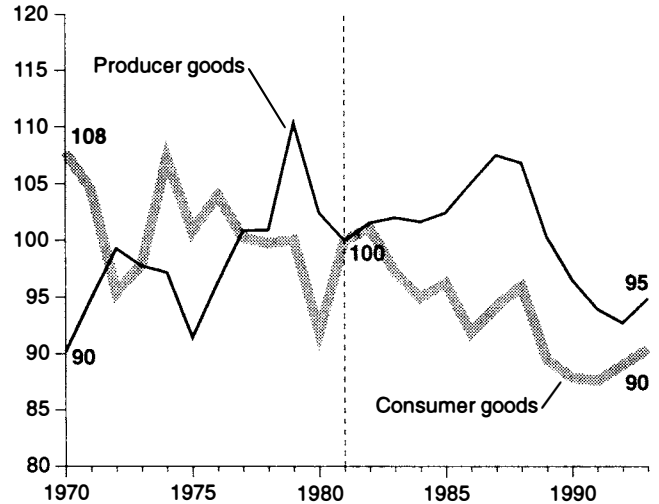


Sources: ECLAC (United Nations), U.S. Department of Commerce.

FIGURE 8

Argentina: producer and consumer goods

(index 1981=100)



Sources: ECLAC (United Nations), INDEC (Argentina).

1995. If that happens, we are looking at \$108 billion in obligations—twice the size of the giant package assembled. Not surprisingly, financial insiders in Mexico are already saying that the country will need another \$50 billion by August of this year—unless policies are radically reversed.

But my forecast is that Mexico is not really the problem: Argentina is.

Producer and consumer goods indices for Argentina show a worse pattern than for Mexico or Ibero-America as a whole (Figure 8). (Here the producer goods index is composed of a half-dozen basic commodities; the consumer goods index is limited to five food items only.) What I mean by that, is that in Argentina there has been negative growth for *two* decades, note one: There was a collapse in the 1980s, like Mexico and the rest of Ibero-America, but unlike the rest, Argentina was decaying throughout the course of the 1970s as well.

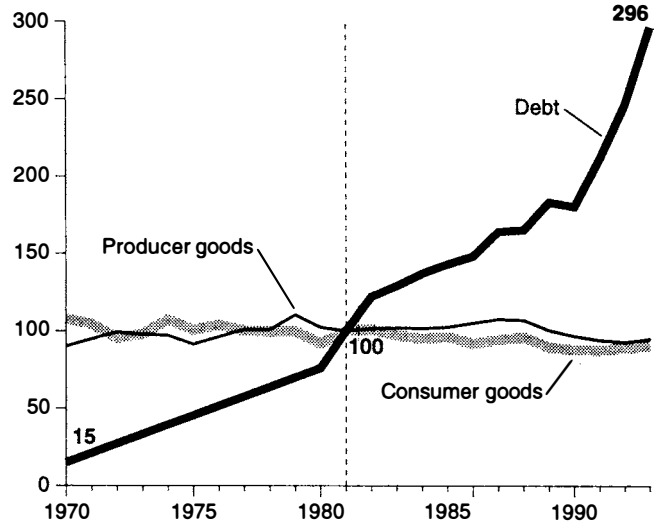
Argentina has endured 25 years of physical economic stagnation and decay, while all the while its debt bubble has been growing astronomically. In Figure 9, we have graphed indices that show how debt has grown by 296% since 1981, while real production per capita and per household has collapsed.

Figure 10 shows that steel production per household in Argentina has fallen by 7%; grain by 27%; cement dropped by a third; and meat production in Argentina, once one of the world powerhouses of meat production and consumption, has plummeted by a shocking 35%. Yet all the while the debt has risen, and risen. The policies of the current Menem

FIGURE 9

Argentina: foreign debt versus consumer and producer goods production

(index 1981=100)



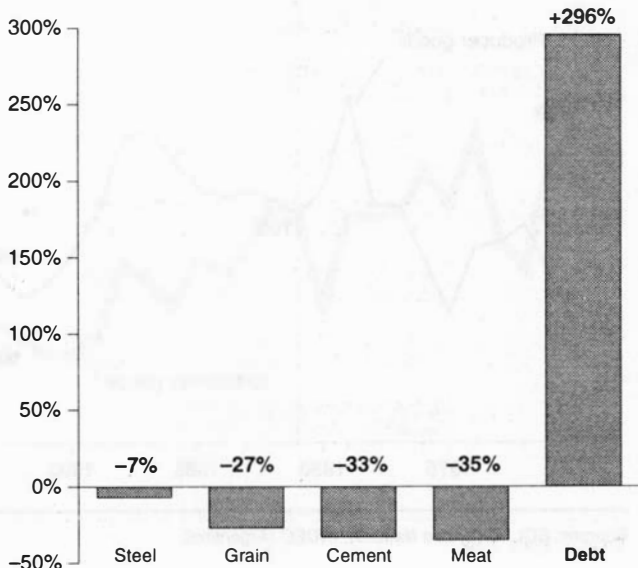
Sources: World Bank, ECLAC (United Nations), INDEC (Argentina).

government, and particularly those of President Menem's Harvard-trained economics minister, Domingo Cavallo, have worsened this already grave crisis, and are about to result in a total blowout of the Argentine banking system.

FIGURE 10

Argentina: growth of foreign debt versus production, 1981-93

(percent change)



Sources: World Bank, ECLAC (United Nations), INDEC (Argentina).

Cavallo and Menem are doing in Argentina almost exactly what Salinas and Finance Minister Aspe did in Mexico, only worse. Cavallo, indeed, seems well on his way to winning a Nobel Prize in Economics.

Some in Argentina understand that this is what is going on, and are trying to do something about it. Prominent among these is the former President of Argentina, Dr. Arturo Frondizi. Many of you know that Dr. Frondizi has also played a leading role internationally in the campaign to first free LaRouche, and now to fully exonerate him and his associates. But perhaps you are not aware of the fact that he and Lyndon LaRouche have known each other personally since 1984.

Dr. Frondizi was invited to attend this conference, but sent his regrets that he was not able to travel. But it is a great honor and pleasure for me to introduce Mr. Carlos González, who is Dr. Arturo Frondizi's political secretary, and who is with us here today in representation of President Frondizi [see *EIR*, March 3, 1994].

The world debt bubble

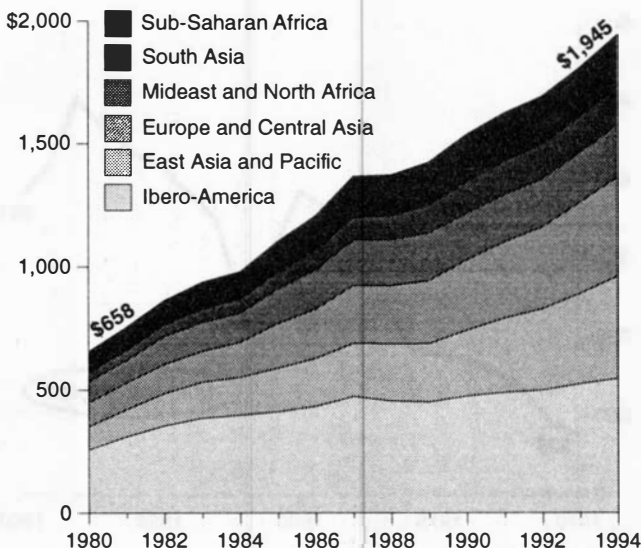
It will perhaps shock you to learn that the foreign debt bubble in Ibero-America is actually the *slowest*-growing among all major regions of the world. So, in one sense, the problems we have been looking at so far pale in comparison with those of Africa, or the former East bloc countries.

Figure 11 employs the official statistics published by

FIGURE 11

World foreign debt, by region

(billions \$)



Source: World Bank.

the World Bank, in their just-issued edition for 1994. It covers the growth of all developing sector debt from 1980 to 1994.

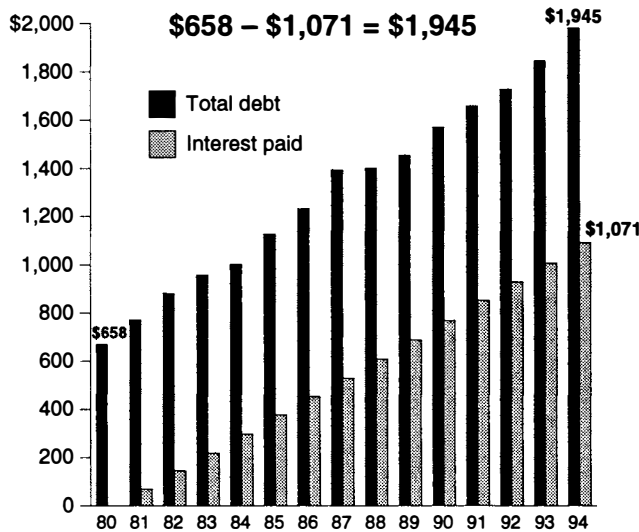
First, let's consider the total numbers (Figure 12). Total world debt tripled from \$658 billion to 1 trillion, 945 billion dollars in 1994—nearly \$2 trillion. Over that period, the developing sector paid their creditors over \$1 trillion in interest payments—\$1.71 trillion to be precise. Mind you, these are interest payments alone; they do not include any amortization or payment of principal that also occurred. So once again, we have a situation where \$658 billion was owed; \$1,071 billion was paid, which is way more than what was owed; and yet at the end of the period they ended up owing \$1,945 billion, or three times what they owed at the beginning. $\$658 - \$1,071 = \$1,945$. Bankers' arithmetic!

If we do the same calculations for each of the regions of the world, we have these results:

- East Asia and the Pacific owed \$95 billion in 1980 and paid \$200 billion. They ended up in 1994 owing \$415 billion.
- In the Middle East and North Africa, the debt owed was \$86 billion and \$113 billion was paid. They ended up in 1994 owing \$213 billion.
- South Asia owed \$38 billion, paying out \$61 billion. They ended up in 1994 owing \$156 billion.
- Sub-Saharan Africa owed \$84 billion and paid \$93 billion. They ended up in 1994 owing \$211 billion.

In the 14 years in question, every single region paid in interest a total amount that was more than their original for-

FIGURE 12
World foreign debt, and interest paid
 (billions \$)



Source: World Bank.

ign debt in 1980; and yet in each case, the debt had doubled, tripled, or—in the case of East Asia and the Pacific—quadrupled by 1994. This particular region includes China, whose debt grew from a mere \$5 billion in 1980, to \$84 billion by 1993, one of the most rapid growth rates anywhere in the world.

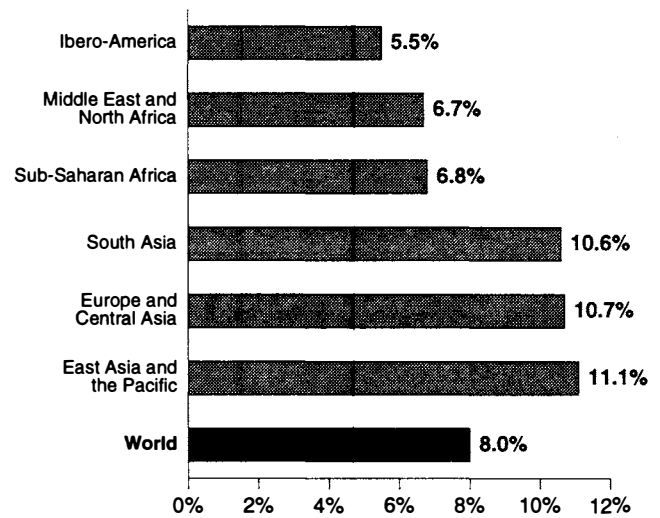
Figure 13 ranks the regions of the world in terms of the average annual rates of growth of their foreign debt, over the period 1980-94. The world average is 8.0% and, as I told you, Ibero-America is the slowest-growing of all, at 5.5%. The Middle East and North Africa are next, at 6.7%, followed by sub-Saharan Africa at 6.8%. Then we take a jump to over 10%, with South Asia coming in at 10.6%, Europe and Central Asia at 10.7%, and East Asia and the Pacific leading the pack at 11.1%.

Let's look in a bit more detail at Europe and Central Asia, whose debt leaped from a mere \$97 billion in 1980 to \$403 billion in 1994, despite the fact that they paid twice their original debt in interest payments (**Figure 14**). What countries are we talking about here? I will read you some names from the official World Bank list, with their corresponding foreign debts as of 1993: Bulgaria \$12.3 billion; Czech Republic \$8.7 billion; Hungary \$24.8 billion; Poland \$45.3 billion; Portugal \$37 billion; Russia \$83.1 billion; Turkmenistan \$9.0 billion.

Get my point?

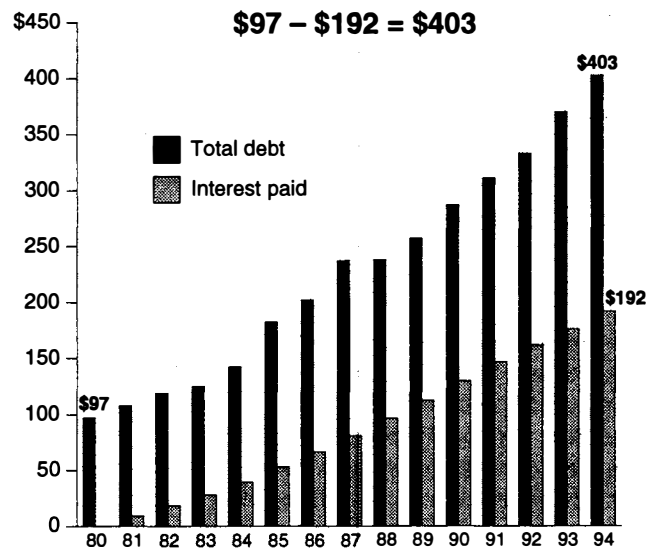
It may be possible for the oligarchy to Africanize Ibero-America—that is a question of political power and what they are able to get away with. But what will happen as they

FIGURE 13
Annual growth of debt, by region, 1980-94
 (percent annual change)



Source: World Bank.

FIGURE 14
Europe and Central Asia debt, and interest paid
 (billions \$)



Source: World Bank.

attempt to “Ibero-Americanize” Poland, Hungary, and, above all, Russia? The total foreign debt of Mexico and Russia may be comparable, but the size of their arsenal of strategic nuclear warheads is not, if you see what I mean.