

Speculative bubble feeds off economy

by Richard Freeman

The United States is now staggering under a mountain of speculative financial instruments, that reached \$97 trillion during the first quarter of 1999. This speculative mass, which effectively represents what economist Lyndon LaRouche has identified as the financial aggregate, has risen at an increasing rate of growth over the past 30 years, and has grown hyperbolically especially since 1987, when Alan Greenspan became Federal Reserve Board chairman.

The growth of this speculative bubble reflects the implementation in America, by Federal Reserve Board chairmen Paul Volcker (1978-87) and Greenspan (1987-present), of the British oligarchy's post-industrial society policy, which withered America's manufacturing, agriculture, and infrastructure, while fostering an "information age" service economy, and speculation.

This post-industrial society policy represented a sharp break from America's past policy of development of capital-intensive, energy-intensive manufacturing and agriculture, and the development of the cognitive powers of the labor force.

The simultaneous growth of the speculative financial bubble and the contraction of the physical economy has occurred through a process that economist Lyndon LaRouche has heuristically presented in his "Triple Curve: A Typical Collapse Function" (**Figure 1**). The upper curve represents the financial aggregate, i.e., the speculative financial instruments, which is growing at a hyperbolic rate. The middle curve, representing the monetary aggregate, in effect, the money supply, which liquefies and props up the upper curve, is growing at a rapid rate. The two curves combined suck the life out of the bottom curve, representing the physical economy, which is contracting at the rate of approximately 1-2% per annum.

The category of U.S. speculative financial instruments, or the financial aggregate from the "Triple Curve," consists of the combined sum of total U.S. debt (U.S. Federal, state, and local government, business, and household debt), U.S. derivatives outstanding, and the valuation of all stocks traded on U.S. markets. *EIR* presented in-depth the size each of these three elements of the speculative financial instruments—debt, derivatives, and stocks—in its Oct. 29, 1999 issue

("How Volcker and Greenspan Created the Financial Bubble"), as well as the process by which the post-industrial society was implemented. **Table 1** shows the level of each of the three principal elements—debt, derivatives, and stocks—and the combined total (the derivatives outstanding for the period before 1985 are estimated).

Between 1987 and 1998, the years that Greenspan has served as Federal Reserve Board chairman, the financial aggregate grew by an increment of \$76.57 trillion, which is 82% of the total value of the financial aggregate at the end of 1998, of \$93.62 trillion. This is a hyperbolic rate of growth.

Speculation compared to GDP

Figure 2 shows the growth of the speculative financial instruments/financial aggregate compared to Gross Domestic Product, which officially constitutes the output of goods and services of an economy. (As a measure of economic growth, GDP is seriously flawed, because of the way that it is determined from the "national accounts" system. It does not measure the functioning of an economy, and for years has risen when the output of the physical economy has fallen. But despite this, it is useful for purposes of our comparison here.)

Two time periods, signifying important economic events, are marked: 1979, when Volcker imposed his policy of "controlled disintegration" as an extreme variant of the post-industrial society policy, and 1987, when Greenspan succeeded Volcker as Fed chairman. The upward shifts in the financial aggregate curve following each of these two events is noticeable.

Figure 3 shows the ratio of the speculative financial instruments/financial aggregate to GDP. Notice that the ratio

FIGURE 1

A typical collapse function

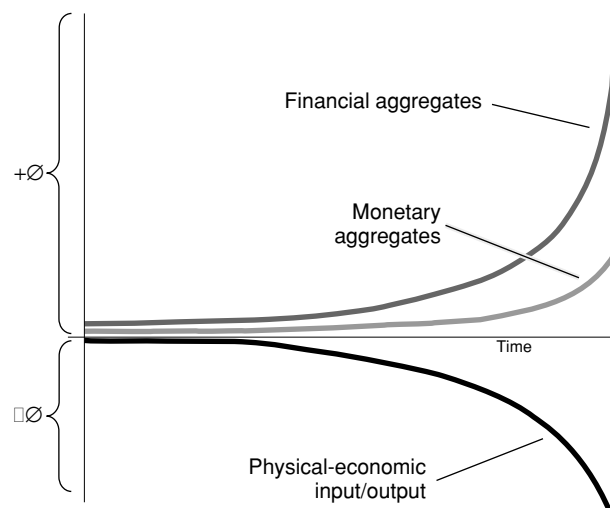


TABLE 1

**U.S. speculative financial instruments/
financial aggregate**

(trillions \$)

	Derivatives outstanding	Capitalization of all stocks	Total debt	Financial aggregate
1960	NA	0.42	0.83	1.25
1965	NA	0.73	1.17	1.90
1970	NA	0.84	1.70	2.54
1975	0.5	0.85	2.76	4.10
1979	1.0	1.16	4.48	6.64
1980	1.0	1.51	4.94	7.45
1985	2.4	2.32	8.96	13.71
1987	3.0	2.76	11.29	17.05
1990	9.3	3.54	14.57	27.42
1991	10.0	4.89	15.33	30.26
1992	12.0	5.46	16.23	33.67
1993	16.2	6.26	17.16	39.67
1994	23.6	6.24	18.44	48.26
1995	26.0	8.33	19.78	54.12
1996	30.5	10.06	21.29	61.86
1997	43.0	12.78	22.89	78.67
1998	53.0	15.44	25.16	93.62
1Q, 99	55.0	15.97	26.00	96.97

Sources: Federal Reserve Board of Governors, "Flow of Funds Accounts"; U.S. Office of Management and Budget; Federal Deposit Insurance Corp.; U.S. Comptroller of the Currency; Bank for International Settlements; *EIR*.

had stayed fairly stable, in a very narrow range, between 1960 and 1979; the latter is the year that Volcker began implementing the policy of controlled disintegration. Between 1979 and 1987 (when Volcker left office), the ratio of the financial aggregate to GDP rose from 2.6 to 3.6. Then, from 1987 until 1998, under Greenspan's direction of the buildup of the speculative bubble, the ratio soared from 3.6 to 10.7.

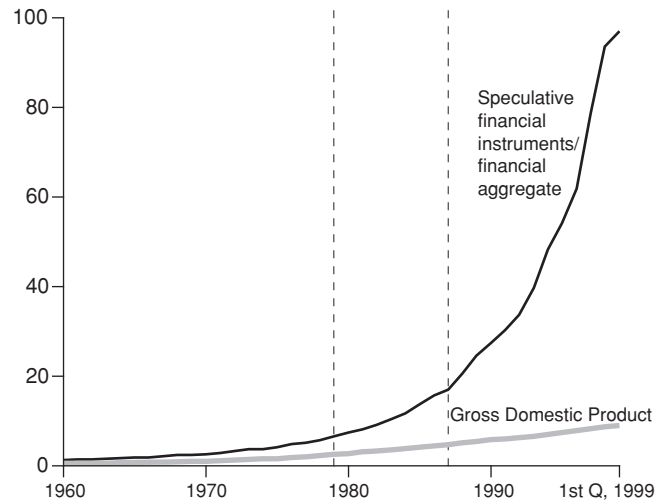
The picture is even worse than it appears. In 1998, although total GDP was \$8.76 trillion, according to Commerce Department figures, 67.5% of the GDP represented services, and only 32.5% of the GDP, or just \$2.85 trillion, represented goods production. Thus, for 1998, the ratio of the financial aggregate, at \$93.62 trillion, to the goods-producing portion of GDP, at \$2.85 trillion, was 33. That is, the financial aggregate of the speculative financial instruments was *33 times greater than the real-goods portion of GDP*. This is unprecedented in economic history.

The rates of return demanded by these speculative financial instruments are enormous. The physical economy, incapable of continuing real human existence and servicing the rates of return on the financial bubble, cannot survive. Defined by the process of the Triple Curve, this ensures physical-economic and financial disintegration.

FIGURE 2

**U.S. financial speculative
instruments/financial aggregate vs. U.S. GDP**

(trillions \$)

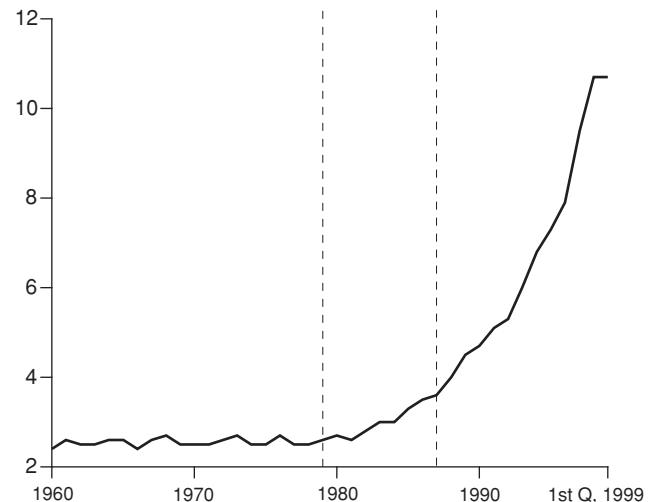


Sources: Federal Reserve Board of Governors, "Flow of Funds Accounts"; U.S. Office of Management and Budget; Federal Deposit Insurance Corp.; U.S. Comptroller of the Currency; Bank for International Settlements; U.S. Department of Commerce; *EIR*.

FIGURE 3

**The ratio of U.S. speculative
instruments/financial aggregate to U.S. GDP**

millions-line under figure head-Helvetica Reg 7/12



Sources: Federal Reserve Board of Governors, "Flow of Funds Accounts"; U.S. Office of Management and Budget; Federal Deposit Insurance Corp.; U.S. Comptroller of the Currency; Bank for International Settlements; U.S. Department of Commerce; *EIR*.