BIS Warns, Bankers and Economy Are Just Blowing Bubbles

by Paul Gallagher

While "economic recovery" propaganda in the United States and Europe reached truly hysterical levels in early March, the next phase of economic and financial collapse was becoming clearly visible. Those who knew enough to watch the unfolding fate of J.P. Morgan Chase Bank, for example—the United States' second-largest, with assets over $800 billion but falling—could see the next shoe of the Enron collapse preparing to drop. On March 14 the *Wall Street Journal* ruefully admitted "the possibility that the bank will be forced to seek a merger with another big Wall Street firm"—the acknowledgment that the huge bank's foundations are shaking as masses of debt and derivatives continue to implode throughout the rotten financial system.

The disaster stalking J.P. Morgan Chase and Wall Street in general, is the "great derivatives cluster-bust," which Lyndon LaRouche in early February saw rumbling out of the Enron collapse.

No amount of American households playing the mortgage-refinancing game to keep buying houses and consumer goods, can touch the basic driver of the collapse—the hopeless level of indebtedness and speculative funny-money on (and hidden off) the books of firms throughout the economy, and on the household books of those consumers themselves. That debt bubble is continuing to implode. The U.S. economy has been through five consecutive quarters of declining profits as a result. As of March, the collapse of the biggest firms in the telecom sector was continuing: Lucent Technologies announced a further shrinkage of investment occurring throughout the sector; fiber-optic giant Nortel's debt was cut to junk-bond rating by the agencies; a near-term bankruptcy of the big communications firm Worldcom is rumored; the biggest mobile phone maker, Nokia, announced a huge fall in sales. "The industry can't survive this way," as the CEO of Verizon put it.

On March 11, a realistic warning came from an unexpected source: the Bank for International Settlements, after its meeting of the world's central bankers in Basle, Switzerland. BIS general director Andrew Crockett said that the Japanese financial crisis today is much worse than most people think; and that what now threatens, from the U.S. Federal Reserve's attempt to overcome the collapse by money-printing, is a new Japanese-style bubble, this time on a worldwide scale. (At the end of 2001, the broad U.S. money supply was already increasing at a 22% annual rate.) In its March 2002 *Quarterly Review,* the BIS warned against the latest increases in the U.S. stock market, achieved through such money-printing. U.S. corporate profits have declined by 47% in the past year, says the bank, much worse than during the 1990-91 recession; consequently, "the price/earnings multiple for the S&P 500 briefly exceeded the levels it had reached at the peak of the equity price boom in April 2000."

Look at the Real Economy

Not just telecommunications, but the whole real, physical economy is continuing to shrink in the world's two largest economies. The European economies are following them down.

In Japan, the government announced on March 7 that capital investment fell 12% in the last quarter of 2001; new machinery orders by 22%; construction orders received by the nation's top 50 contractors, by 14%. The government also increased yet again, the official estimate of the rate at which the Japanese Gross Domestic Product is now shrinking.

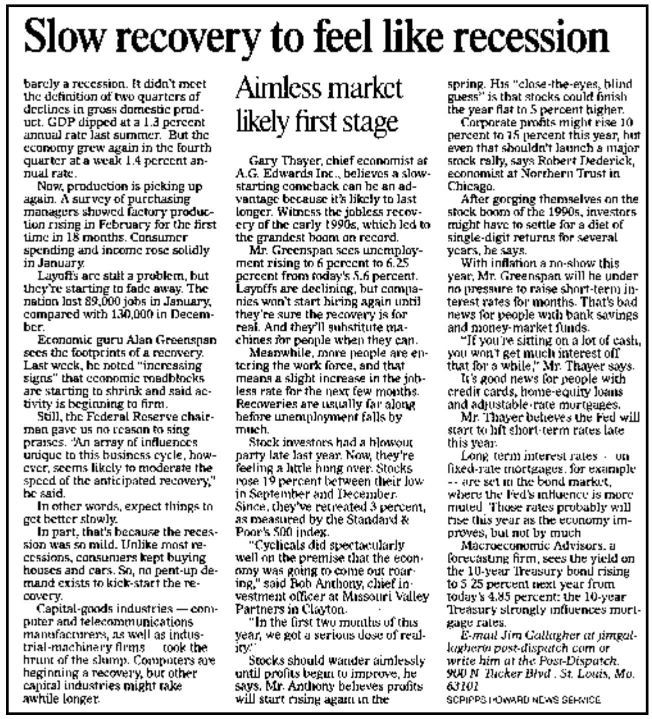
In the United States, despite the Department of Commerce's announcement of increased new orders for manufactured goods in January, Commerce's own report simultaneously showed the underlying reality. In comparison to one year ago, there is only one category of manufactured goods, where new orders are rising strongly, and that is—not surprisingly—"defense aircraft and parts," up 53.9% year-on-year. Automobile orders are up 6.6%. In almost all other categories, new orders are still sharply down compared to the year before. Iron and steel orders are down 5.9%; aluminum and nonferrous metals orders, 14.5%; industrial machinery orders, 15.4%; metalworking machinery 10.2%; turbines, generators, power transmission equipment, 33.9%; material-handling equipment 29.8%. Then in the fields of electronics and communications equipment, the picture gets even worse: orders for electronic computers, down 25.5%; for non-defense communications equipment, down 39.1%; and for electronic components, down 33.8%.

Just a couple of weeks earlier, on Feb. 21, the U.S. Department of Agriculture had released its *World Outlook Forum* publication, and had forecast that all American farmers combined will lose money on farming in 2002, which would be the first time this had ever been statistically recorded. The USDA forecasts the losses will average about $200 per farm, whereas the average farm gained $7,500 only four years ago. This means that U.S. farmers, as a whole, are supporting their agricultural "hobby" by other jobs—what will happen to the nation's food supply as they lose them?

Unemployment in the United States is obviously continuing to increase, even as the unemployed are, statistically, kicked out of the labor force, to back up the "recovery" delusions. The U.S. Labor Department records approximately 1 million workers as having "left the labor force," stopped looking for work, over the course of the past year. A report from the Labor Department on March 13, concerning the Washington, D.C. area, showed the amount of statistical massaging going on. The Department, which had been reporting throughout 2001 that the capital area was gaining jobs, in defiance of the national "recession," suddenly acknowledged that in fact, the area had *lost* 20,900 jobs during 2001.

Add to this, the fact that the United States' national railroad corporation, Amtrak, has announced that it will likely have to close down most of its long-distance rail service this year; and that large-scale layoff announcements are still coming from the retail, telecommunications, and auto and other industrial sectors. And at the same time, virtually all of the 50 states of the Union have been plunged into fiscal crisis by collapse of their tax revenues, and are savagely cutting away at public school funds, medical-care support for the indigent and elderly, transportation and construction spending, etc.

Thus Federal Reserve Chairman Alan Greenspan's pronouncement of "an expansion," as even his fellow central bankers of the Bank for International Settlements realize, is nothing but a bubble-blowing delusion. LaRouche has identified this delusion, widely accepted by "public opinion," as the greatest danger to an actual recovery policy.



Slow recovery to feel like recession

barely a recession. It didn't meet the definition of two quarters of declines in gross domestic product. GDP dipped at a 1.3 percent annual rate last summer. But the economy grew again in the fourth quarter at a weak 1.4 percent annual rate.

Now, production is picking up again. A survey of purchasing managers showed factory production rising in February for the first time in 18 months. Consumer spending and income rose solidly in January.

Layoffs are still a problem, but they're starting to fade away. The nation lost 89,000 jobs in January, compared with 130,000 in December.

Economic guru Alan Greenspan sees the footprints of a recovery. Last week, he noted "increasing signs" that economic roadblocks are starting to shrink and said activity is beginning to firm.

Still, the Federal Reserve chairman gave us no reason to sing praises. "An array of influences unique to this business cycle, however, seems likely to moderate the speed of the anticipated recovery," he said.

In other words, expect things to get better slowly.

In part, that's because the recession was so mild. Unlike most recessions, consumers kept buying houses and cars. So, no pent-up demand exists to kick-start the recovery.

Capital-goods industries — computer and telecommunications manufacturers, as well as industrial-machinery firms took the brunt of the slump. Computers are beginning a recovery, but other capital industries might take awhile longer.

Aimless market likely first stage

Gary Thayer, chief economist at A.G. Edwards Inc., believes a slow-starting comeback can be an advantage because it's likely to last longer. Witness the jobless recovery of the early 1990s, which led to the grandest boom on record.

Mr. Greenspan sees unemployment rising to 6 percent to 6.25 percent from today's 5.6 percent. Layoffs are declining, but companies won't start hiring again until they're sure the recovery is for real. And they'll substitute machines for people when they can.

Meanwhile, more people are entering the work force, and that means a slight increase in the jobless rate for the next few months. Recoveries are usually far along before unemployment falls by much.

Stock investors had a blowout party late last year. Now, they're feeling a little hung over. Stocks rose 19 percent between their low in September and December. Since, they've retreated 3 percent, as measured by the Standard & Poor's 500 index.

"Cyclicals did spectacularly well on the premise that the economy was going to come out roaring," said Bob Anthony, chief investment officer at Missouri Valley Partners in Clayton.

"In the first two months of this year, we got a serious dose of reality."

Stocks should wander aimlessly until profits begin to improve, he says. Mr. Anthony believes profits will start rising again in the spring. His "close-the-eyes, blind guess" is that stocks could finish the year flat to 5 percent higher.

Corporate profits might rise 10 percent to 15 percent this year, but even that shouldn't launch a major stock rally, says Robert Dederick, economist at Northern Trust in Chicago.

After gorging themselves on the stock boom of the 1990s, investors might have to settle for a diet of single-digit returns for several years, he says.

With inflation a no-show this year, Mr. Greenspan will be under no pressure to raise short-term interest rates for months. That's bad news for people with bank savings and money-market funds.

"If you're sitting on a lot of cash, you won't get much interest off that for a while," Mr. Thayer says.

It's good news for people with credit cards, home-equity loans and adjustable-rate mortgages.

Mr. Thayer believes the Fed will start to lift short-term rates late this year.

Long-term interest rates -- on fixed-rate mortgages, for example -- are set in the bond market, where the Fed's influence is more muted. Those rates probably will rise this year as the economy improves, but not by much.

Macroeconomic Advisors, a forecasting firm, sees the yield on the 10-year Treasury bond rising to 5.25 percent next year from today's 4.85 percent; the 10-year Treasury strongly influences mortgage rates.

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SCRIPPS HOWARD NEWS SERVICE

A schizophrenic headline in one of the dailies of the capital, the Washington Times, *shows the lunatic quality of wishful thinking which has produced the U.S. economic "recovery."*

'Free Trade' Myth Cracking

There were signs that President George W. Bush himself was dubious about Greenspan's announcement to Congress of "an expansion." Bush told the press that "number crunchers" didn't convince him that the economy was now fine; he added that there was still plenty of unemployment and suffering in the country.

Bush's move to announce tariff protection for the U.S. steel industry, which has almost completely collapsed into bankruptcy since 1998, was the first sign of a critical shift—highlighted by LaRouche in statements on the decision—from the "free trade" axiom of ingrained American public opinion of the last decades, toward "fair trade" and regulation. Other such signs are appearing. On March 5, the Senate began debating restoring the power of the Commodity Futures Trading Commission (CFTC) to regulate the trading of energy derivatives. The deliberate removal of that power in 1998, involving the sacking of the CFTC's chairman, opened the door to Enron's looting of the economy and then its ruin. Greenspan publicly opposes regulation of derivatives markets, even now.

At the same time, the Senate began debate on legislation to save and upgrade the Amtrak rail infrastructure with large-scale Federal funding.

Such shifts, confronting the dominant insanity of the "recovery" mantra, depend on the LaRouche forces in the United States, to bear fruit.