Mobilizing an economic recovery under conditions of financial crisis

by Lyndon H. LaRouche, Jr.

The following is the text of a letter, written on Nov. 30, 1987, which has been widely circulated in West Germany and is now released to the public by the LaRouche Democratic Campaign.

I step off the stage of the U.S. presidential campaign, to address you as a representative of a growing bipartisan movement in the U.S.A., the which has been set into motion by the events of that awesome stock market panic called "Black Monday." The distinction to be made, is that the inauguration of the next U.S. President occurs in January 1989; it is during the 12 months before that inauguration that well-defined economic-recovery measures must begin, if we are to prevent the continuing financial collapse from leading directly into the worst economic depression in modern history.

I have caused to be attached to this letter a copy of an item I have written for the English-language intelligence newsweekly *Executive Intelligence Review* ["The World Financial Collapse in Progress: When the Gods of Olympos Fall There Is Danger, But Hope," released for limited circulation on Nov. 28, 1987, and available from EIR News Service]. This attached item provides the general background for what I have to present to you in this letter, including adequate indications of my exceptional qualifications to speak on the subject of recent and current U.S. monetary and economic policies, both domestic and foreign.

The inclusion of that attached item permits me to confine my remarks here to three subjects: 1) certain discrepancies among the economic situations in various of the OECD nations, 2) addressing frankly some unspeakable truths respecting the quality of national governments and political parties in Western Europe and North America, and 3) some appropriate technical-economic observations, supplementing the general description provided in the attached pre-publication draft.

Excepting Britain and Italy, until the recent developments in European agriculture and metals industries, the structure of the economy of industrialized Western Europe had been destroyed less rapidly over the recent 10 years than that of the United States and Canada. European OECD nations have a total active industrial potential greater than that of the United States; the percentage of the adult labor force of employment-age employed in production of physical output at modern levels is significantly higher than in the United States. Especially as a result of the more reckless bubble-building by U.S. money-market financial institutions in New York City and elsewhere, the debt-ratio in the United States is worse than in Western Europe as a whole.

Now, in consequence of such politically directed developments as the successive "Davignon rounds," and the precipitous collapse of European agriculture, Western Europe as a whole is tending to overtake the levels and rates of decay previously more typical of the U.S.A., Canada, Britain, and Italy.

In quality, governments, political parties, and economic management, are of much poorer quality generally today, than 10 years earlier, and vastly poorer than 20 years ago. Through various forms of attrition, as the generation of the 1968 student insurgencies have "marched through the institutions," and as the OECD's radical educational reform program of 1963 has destroyed the quality of the preexisting educational systems, the quality of political and managerial cadres has fallen, on the average, about as rapidly as the structure of the physical economy has been eroded.

The transition toward that utopia called "post-industrial society," has been accompanied by an acceleration of the post-1966 shift from an agro-industrial entrepreneurial economy, to a rentier economy. This has been reflected as shifts in the criteria of economic management and investment, and in axiomatic shifts in habits of thinking, not only among management cadres, but in the popular *Zeitgeist*. Society has become increasingly irrational in its habits of judgment, at all levels. A rational calculation of the physical conditions of life, production, and national security, has been superseded by emphasis on an irrational fascination with rather arbitrary choices of nominal values, an irrationality increasingly proximate to the witchcraft superstitions of illiterate savages.

This weakening of the quality of direction of society has been featured most prominently in the rapid, post-1966 decay in the quality of leadership provided by government and leading political parties. This trend has been in part relatively spontaneous, in the sense that it reflected the increasing tendency toward functional illiteracy and irrationalist world-outlooks in the population generally. It is not to be overlooked that this lowering of the quality of governments and political parties has been intended, since approximately 1963 decisions within transatlantic establishments, to this effect. The desire of the majority of such establishments has been to degrade the role of elected government in policy-shaping, to eliminate strong political leadership such as that of Konrad Adenauer and Charles de Gaulle, in favor of a blending of mediocrity and administrative technocracy.

So, we are now plunged into the greatest financial collapse in modern history, while the majority of the leadership of our nations is intellectually of poorer quality than even 10 years earlier, and vastly poorer than 20 years earlier. It is not unfair to say that today's governments are honestly incapable, intellectually, of understanding what would have been more or less clearly recognized by leading institutions even 10 years earlier. We should not indulge ourselves by blaming incumbent leadership for their horrifying lack of capacity; they are the hapless victims of a process of selection which chose to eliminate from election to higher posts men and women lacking in the desired qualities of mediocrity. Nor, can we blame them personally, if they were selected for their quality of adaptability to recent *Zeitgeist* trends toward irrationality.

The essential political fact to be learned from this, is that there are relatively few calamities in history which could be called rightly "crises" in theirown right. What usually defines a crisis is not the problem with which that crisis is associated; rather, the word "crisis" becomes justified when the leading institutions of society are confronted with a problem which has readily available objective remedies, but under the condition that leading institutions have lost the capacity to adopt such appropriate remedies. Barring the eruption of earthquakes, tidal waves, pandemics, and those wars over which the institutions of a nation have had no efficient means of control, the word "crisis" signifies a breakdown of the capacity of institutions to respond to what would be otherwise merely important problems.

The essential task before us all, on both sides of the Atlantic most emphatically, is to transform the current "crisis" into merely an important problem to be overcome.

For example, in the United States today, that which warrants the term "crisis," is not the ongoing financial collapse itself; but, rather that the Reagan administration and leaders of the Congress are responding to this situation with almost the same words and actions as did the Hoover administration and U.S. Congress of 1929-32. The 1929 crash need not have led into the deep economic depression of the 1930s; rational remedies, overthrowing the policies of the Coolidge and Hoover administrations, existed. What the Hoover administration did, was to react to the ongoing financial collapse, by ruining the economy in the effort to defend the policies which had caused the crash. That is exactly the way in which the Reagan administration and Congress are acting today, and most of the governments of other OECD nations, too. It is this stubborn folly, of stubbornly defending the so-called "free trade" policies which have caused the calamity, which constitutes the "crisis."

By "crisis," we should signify not only the ongoing international financial collapse. We mean also the strategic crisis, the AIDS pandemic, and so on. We ought to signify by "crisis," the desperate clinging, by governments and other leading policy-shaping institutions, to the policies which either have caused, or have greatly aggravated the principal calamities of this interval of history.

In the broadest terms, the general solution required, is to resume that philosophical world-outlook, on matters of economy and other questions, which prevailed 20 years ago. We should not go as far as to re-adopt intact the policies of 20 years ago; there were numerous follies in those policies. Rather, we should make the changes in policies which we would have tended to make, 20 years ago, had we foreseen then, with sufficient clarity and sense of urgency, the process of decline of our economy and our civilization up to the present time.

In economics as such, the axiomatic feature of combined mediocrity and incompetence is the spread of an ideology which replaces traditional employment emphasis on physical output per capita and per square kilometer, by emphasis on the merely nominal value added of rentier forms of financial appreciation. Policy-shaping in economic matters is so construed today, that were all the industries of Germany to cease production, but maintain the same levels of value added from employment in administration, sales, and unskilled services, current national income-accounting would argue, as it does in the United States, that the economy is either stable, or even growing.

Thus, prior to "Black Monday," President Reagan described an uninterrupted, 1982-87 erosion and collapse of the productive sector of the U.S. economy as "59 months of uninterrupted growth." Worse, even after the October collapse, the same President described the state of affairs as "60 months of uninterrupted recovery." Worse, the policies of the U.S. government today are based on acting out that delusion, taking patch-work measures, copied from the 1929-32 repertoire of the Hoover administration, and destroying the national defense, all in the effort to save the non-existent "recovery" which has caused this calamity. That is the meaning of the word "crisis."

The state of the economies

In broad terms, the calamitous condition of our economies should be described in two distinct, although interacting terms of reference. We must distinguish the physical structure of the economy, or what Leibniz defined as "physical economy," from the superimposed institutions of political-economy.

By "physical economy," we mean the average productive powers of labor, measured in terms of production and efficient distribution of physical output. This signifies the structural composition of the total employment of the national

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A steel mill along the Rhine River in the Federal Republic of Germany. Now, the factories are shutting down.

labor force, the level of technology represented by that employment, and the per capita physical output, measured in terms of a standard market-basket consistent with the level of technology which the labor force is required to assimilate efficiently.

The outstanding problems on this account are chiefly three.

First, consider the composition of employment in the United States as a standard for comparison. In 1946, more than 60% of the total labor force was employed as operatives in either agriculture, industry, or basic economic infrastructure, signifying that less that 40% were either unemployed, or employed in such "overhead expense" categories as administration, finance, sales, and services. Today, the level of employment of operatives is dropping below 20%, signifying that 80% of the labor force is assigned to the "overhead expense" categories of unemployment, administration, finance, sales, and services.

Second, the erosion of basic economic infrastructure: fresh-water management, general transportation, communications, production and distribution of prime energy-supplies, and urban residential-industrial infrastructure otherwise. Only communications holds up. Otherwise, relative to the state of repair of U.S. basic economic infrastructure in 1970, there is today a deficit which would cost approximately $4 trillion in investment to repair.

I expand on a point referenced in the accompanying item. Compare the energy-densities for the economies of Japan, the Federal Republic of Germany, and the U.S.A. approximately 1970. At that point the levels of technology and productivity among the three nations were comparable. The energy-density per capita is highest in the U.S.A., next-highest in the Federal Republic, and lowest, among the three, in Japan. However, the energy-density per square kilometer in Japan is very much higher than that of the Federal Republic, and the Federal Republic's higher than the U.S.A.'s. Examining this and other cases more closely, we see, statistically, that the rate of energy-density for the three nations is approximately identical circa 1970, if we measure energy-density in per capita units of population-density.

In a computer study done by *EIR* during the early 1980s, it was shown that up to 1966, postwar investments in capital improvements in infrastructure correlated closely with rates of increase of productivity. The rate of change was almost identical for the two curves, by a lag-factor of approximately 12-18 months. During the 1966-70 period, the net rate of capital improvements in infrastructure, relative to erosion, dropped to zero, as project-levels held over from the pre-1966 period declined. The rate of increase of productivity followed this decline. Since 1970, the rate of net erosion of infrastructure has correlated with the decline in physical productivity for the labor force taken as a whole. This statistical correlation is the most exact in all economic time-series.

What are the reasons for this astonishing statistical agreement? Some of the reasons are exposed by intelligent inspection; the more profound reasons are intelligible ones, but to be found in the realm of nonlinear studies of economic processes. The evidence supplied by intelligent inspection suffices to illustrate the point.

Two among the prime constraints of a physical-economic (nonlinear) function for economic growth are energy-density and energy-flux density. The notion of this role of energy-density was well established by Leibniz's work on the effect of heat-powered machinery in increasing the productive powers of labor. Energy-density pertains most emphatically to the effective energy-density per square centimeter applied to target-areas of production. By changing the units employed, from scalar, caloric values, to a Riemannian-Beltrami electrodynamics' view of the quantum-functions of self-focusing of coherent radiation, relative to frequency, the two notions, energy-density and energy-flux density, can be combined as one.

By inspection, it is not difficult to recognize that there is no absolute distinction between capital-intensity, as associated with the notion of investments in machinery, and the broader notion of capital-intensity, which includes basic economic infrastructure and capital investments in productive processes under a single functional classification. In both agriculture and industry, most obviously, the total capital improvement to be associated with such a single category of capital-intensity, is a partial function of the development of land-area. Hence, the greater the land-area requiring capital improvement, per capita occupying that land-area, the greater the partial capital-intensity costs of basic economic infrastructure.

Since we can translate all output into terms of the energy costs associated with both producers' goods and households' goods consumption of employees, a really satisfactory function for physical-economic processes is an appropriate choice of energy function.

The six primary constraints for an adequate functional representation of a physical-economic process are: 1) the general constraint, that the quality of per capita market-baskets of households' goods must increase in correlation with advances in technology and productivity, otherwise the labor force is unable to assimilate technological progress efficiently; 2) an increase of the energy-density per per-capita unit of population-density; 3) an increase of the energy-flux density of modes of production; 4) subject to constraints on the increase of the percentage of employment of the labor force in "overhead expense" categories: the increase of the ratio of employment of urban operatives to rural ones; 5) with the same restriction on employment classifications, the increase of the ratio of employment of operatives in capital improvements, relative to employment in output of households' goods; 6) advance in technology, as Leibniz defined "technology" as a function of least action.

From that standpoint, the energy-density function in terms of per capita units of population-density, is more or less readily understood. The reason I have emphasized this point as much as I have here, is that amateur economists of the International Monetary Fund's and World Bank's bureaucracies, among others, have argued that capital improvements in basic economic infrastructure must have a priority ranging from very low, to zero or even negative net growth. It is important to stress, therefore, that curtailing such categories of capital improvements has the effect of preventing economic growth in production of all goods, in the most diabolically efficient way.

The third feature of the erosion of physical economy over the recent 20 years, has been the collapse of technologically progressive, capital-intensive investment in industrial production. One effect of this has been not only to block progress in productivity, but to lower productivity. The other principal effect is to contract all industrial output, for reasons I have described adequately in the attached item.

What has occurred over these 20 years has been, in net effect, to shift percentages of employment of the labor force in capital-goods production into the services and related categories of overhead-expense employment. This trend has set into motion a secondary tendency, to shift percentages of the labor force from employment in all categories of operatives' occupations, also into overhead-expense sectors.

As I have indicated in the accompanying item, not all overhead-expense categories are truly nonproductive. By productive, I mean that which maintains and increases the per capita quality and quantity of per capita physical output. In this sense, we use the term "productive employment" to signify operatives employed in either the production of physical goods, or in operations, maintenance, and capital improvements in basic economic infrastructure. Yet, some categories of overhead employment have a highly significant benefit for the productivity of the operatives. These include direct production management as such. It includes also education and medical services to households. The connection is, I believe, sufficiently obvious, that I need say no more in defense of that point.

For example, in addition to a relatively fixed per capita requirement for employment of educators and medical professionals, Western industrial society requires a minimum of approximately 5% of the labor force employed as scientists, engineers, technicians, and so forth in research and development. Assuming a healthy machine-tool sector, and a healthy rate of capital-intensity's net growth, 5% of the labor force employed in R&D is sufficient to provide an average growth in productivity of operatives of between 5 and 10% per year. I propose, I have indicated, that we adopt the target of increasing this from 5%, to 10% of the total labor force so employed.

In this connection, we must reverse the post-industrial trends in composition of employment, reducing the percentages allotted for administration, finance, sales, and services (other than professional and related technical services), by shifting the relevant percentages of employment back into, chiefly, employment of operatives. I propose a target of not less than 40% of the labor force employed as operatives, not counting those employed in research and development functions, and reducing the percentage of the labor force employed in overhead categories other than research and development, education, and medical, to not more than 35%, and preferably 30%.

How this is to be accomplished comes under the heading of the second general topic, political-economy. I believe that I have covered the significance of this term sufficiently in the accompanying item. I shall add only the following relevant observations.

From the standpoint of physical economy, the design of the monetary and related political superstructure of an economy should be axiomatically entrepreneurial. Basic economic infrastructure is a function of the state, either as economic ventures of governmental agencies, or through regulation of privately owned public utilities. This includes the social infrastructure of basic education; it includes ensuring that the institutional side of general medical services is sufficient capacity for public need. Otherwise, production and trade should be entrepreneurial, unless special circumstances require temporary state intervention to fill a need which the private sector is either unable or unwilling to supply.

Bernd Mackeprang

Steelworkers demonstrate in Rheinhausen against the planned closing of the Krupp steel plant, December 1987. The banner reads, "Krupp must keep on making steel."

The reason for this was rather clearly understood by the middle of the 16th century. The mercantilist current in England, including Thomas Gresham, fostered the use of the power of the royal government to issue patents, under whose terms inventors and their business partners enjoy a limited period of monopoly on the production and sale of useful inventions. Western civilization's strength is our special view of the development and employment of the creative powers of reason of the individual personality; to encourage this, and to give it the greatest latitude possible or tolerable, is an intrinsic part of our civilization's superior genius for generating and assimilating the benefits of scientific and technological progress.

The state intervenes only to create orderly markets, as the boundaries within which private entrepreneurship occurs. This pertains to foreign trade, and to establish limits of fair price and related conditions on domestic commerce, including the conditions of labor. The maximum latitude within the limits beyond which there are abuses, is the correct policy.

These features of political-economy which I have identified should be seen as more or less axiomatic. No design of the monetary, taxation, and related policies introduced by government should violate those axioms. Also, the state must exert its sovereign right to assert its monopoly over the creation and issuance of currency, to regulate an orderly and stable banking system, and to regulate foreign trade and tariffs. The function of the state is to cause the creation of money, as lending power, at low interest-rates, for those applications of credit which are categorically in the national interest, especially for fostering technologically progressive development of infrastructure, and private agriculture and industry. The state should also shape its policies of taxation to foster investment in those sectors which are most beneficial to the nation.

Within those constraints, the other features of political-economy are variable. The object, as I have indicated in the accompanying item, is to adjust the variable features of a monetary and fiscal system of policies in such ways as correct for effects to be abhorred, and to promote effects much to be desired.

In the matter of determining the composition of employment of the labor force as a whole. The state's economic role in basic economic infrastructure determines a significant part of this composition. The rest is primarily controlled by the relative flows of credit to various sectors of investment, and by the shaping of policies of taxation with a view to their relevant effects on investment. The best mechanism for regulating the relative flows of credit, lies in the cheapness of state-created credit, relative to private sources of credit. By restricting the application of state-created credit in ways which promote achievement of a national consensus on matters of goals of composition of employment, output, and investment, and by addition of investment tax-credit incentives, the desired influence is achieved without further need of direct legislative action in the matter.

In the modern history of Germany, the work of Friedrich List is essentially up-to-date as a discussion of principles of national economy. I avow myself in sympathy with that great German-American, and pronounce his insights to be appropriate guides to economic thinking for today. The technology and other circumstance have been altered; the underlying principles remain the same. What I propose as a remedy, is what List himself identified as the American System of political-economy, the which once served both the United States and Germany very well.

The policy conflict

The relevant conflict at the levels of government, enterprise, banking, and so forth, is the conflict between an entrepreneurial form of agro-industrial national economy, on the one side, and an increasingly supranational rentier form of economy, on the other. This conflict appears in the guise of the present financial collapse, in the form of the following two choices: If we choose to continue the rentier policies, particularly those of the recent 20 years, civilization slides into the worst and perhaps longest depression in modern history; if we shift from a rentier bias, back to preference for entrepreneurial national-economy, even a stunningly deep collapse of financial markets does not trigger a lasting depression.

The crisis of 1929-32 was nothing more than the inevitable consequence of the international monetary and related agreements reached at Versailles. In the transatlantic community of the 1920s, excepting a brief boom in the major creditor-nation, the United States, there was no actual economic recovery. The international authorities stumbled from crisis to crisis, seeking to defend the Versailles system, with the perennial issue of the unpayable German war-reparations debt the central issue. Once the Young Plan failed, as it was doomed to do, the general collapse of the Versailles financial bubble, built up over the 1920s, was inevitable.

Had the Versailles system been scrapped at any point during the 1920s, and had the U.S. government used its great power to force adoption of a new monetary order consistent with the principles of the American System of political-economy, a rapid recovery of the German economy could have occurred, and with that, a general economic prosperity.

It was not too late to do this during the 1929-32 period. Hoover and his Congress, together with Treasury Secretary Mellon, together with the other Entente powers controlling the Versailles system, refused to consider such an alternative. London and New York, including the *New York Times,* even backed Nazi Economics Minister Hjalmar Schacht's proposal to stage the legal coup d'état of Hitler, as part of the effort to save the policies which had caused the financial bubble and its collapse. As a result of this folly by Hoover and others during 1929-32, there was a second World War.

Today, we are in a condition like that of 1929-32, but much worse. Not only have the governments, so far, reacted as they did during 1929-32. There is even, once again, serious talk of introducing fascist governments as a means for continuing the defense of bankrupt rentier policies.

There is a growing commitment to a plan to resume the policies of Schacht and the Brüning government. For nearly 20 years, at least, Keynesian and other idiots have insisted that had Weimar instituted Schacht's policies democratically, Schacht and his London and New York bankers would not have been forced to put Adolf Hitler into power! Now, there is a movement to react to the new financial crisis with policies of "democratic fascism," assigned to do what the Keynesian defenders of Schacht had proposed that the Weimar Republic should have done, democratically. There is already, in the United States, a powerful bipartisan faction in the Congress, indoctrinated along such lines, and drifting in such directions of policy-thinking for the period following the 1989 U.S. presidential inauguration.

Some people seem never to learn anything from experience.

However, the conflict between rentier and entrepreneurial policies, as deadly as it has been over the centuries, is not the crisis. The disastrous condition of the leadership of governments and political parties is. It is the natural tendency of the majority of the popular constituencies, under conditions such as these, to demand sweeping changes in policies, away from the policies which have caused the crisis, to policies explicitly designed to promote an economic recovery. It is the refusal, or even the simple failure of governments to respond to that popular demand, which creates the preconditions for entry of dictatorships or kindred acts of desperation. So, the habituated mediocrity of national leaderships is the hard kernel of this present crisis.

It is necessary and consoling to rail against the ineptitudes of governments and parties stricken with mediocrity, but complaining will not solve the problem. Some credible force must emerge to place effective proposals on the table. This force does not yet exist as a well-organized force, but only a potential one. Its political potential, throughout Western nations, is enormous, but is so far only potential. This force is based on local political leaders closer to the realities of the economic situation than most national governments or national party leaderships. It is also based on constituency forces of agriculture, industry, and others.

It is the nature of crises such as these, that solutions are provided, if they are provided at all, by aid of some unusual awakening of the national will for constructive good. To move these governments and national party leaderships in the right direction and in time, nothing less than such a manifest awakening will suffice. Those from local political leaderships and key constituencies, who recognize the peril of our civilization, must bring themselves together, and, we must hope, in several or all of our nations. We must assemble our forces of moral political influence, in just fear of the awesome political and other horrors which may be bestowed upon us, if the needed change is not effected soon, but also in just and hopeful confidence in the remedies available.

I hope that my remarks will contribute to making those remedies clearer.