

The Economic State Of The Union -- 2008

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Manufacturing and Technology News

In just the past seven years, U.S. household debt almost doubled and federal debt soared by near two-thirds, rocketing by a combined \$10.5 trillion. The total combined debt of households (\$14.4 trillion) and the federal government (\$9.2 trillion) is now 168 percent of GDP, far higher even than in the brief spike during World War II. All other levels and ratios of debt also have soared far beyond any past precedent.

Yet, this record-shattering explosion of debt stimulus created the weakest seven-year job growth (4.4 percent) and one of the weakest periods of real GDP growth (18.1 percent) since the Depression: less than 6 million new jobs (\$1.8 million of debt per job) and a mere \$4 trillion increase in GDP.

This period began with the collapse of Wall Street's stock market bubble from the late 1990s and ends now with the collapse of Wall Street's housing and other debt bubbles. That such massive mortgage and consumer borrowing, tax cuts and war spending produced such remarkably weak real economic results suggests the months and years ahead could be quite difficult.

Yet, along with the Fed rate cuts for cheaper debt, the only policies seriously considered by this year's crop of Wall Street-funded political candidates is more short-term household and federal debt "stimulus." Locked into a failed, 30-year-old ideology of deregulation and debt, there is still no option to compete with the remarkably effective industrial and trade policies pursued by China and others.

2008 will be the ninth consecutive year the U.S. economy grows slower than the world's growth while China grows more than three times faster. In the past seven years of sluggish growth, the United States accumulated manufacturing trade deficits (production shortfalls) of over \$3 trillion with full current account trade losses of \$4.3 trillion; more than the entire nominal growth of GDP.

At the same time, now in the third year of their remarkable eleventh Five-Year Development Plan, China's accumulated Current Account surplus soared by nearly \$1 trillion since 2001, near 13 percent of GDP in 2007. These surpluses are funding China's now \$1.5-trillion war chest of foreign currency reserves.

Record trade losses have accelerated the hollowing-out of the once dynamic U.S. economy. For the first time on record, in 2002 the United States lost its historic global trade surplus in advanced technology products (ATP). Worsening sharply, since 2004 the ATP deficit became larger than the U.S. trade surplus for intellectual property services, royalties and fees. That is, for

the past four years the United States has a worsening combined deficit in technology goods and services. Technology no longer pays any part of the U.S. import bills for oil, cars, electronics and clothing, etc. China now accounts for half the U.S. manufacturing trade deficit and more than the entire deficit in technology.

Reflecting the production shortfall from the trade deficits, BLS data show output growth since 2001 is among the weakest since the Depression and the gain in total hours worked (just 0.5 percent) is, by far, the weakest. This is why productivity growth has appeared misleadingly healthy; productivity is a measure of output per hour of labor.

Another powerful measure of the hollowing out in the economy is the radical shift in the job market. Of the 5.92 million total new jobs in the last seven years, only 4.32 million were in the private sector while 1.66 million were in state/local governments, mostly for public education, health and prisons. The federal government cut jobs in the Postal Service.

More than all of the new jobs added by the private sector since 2001 are in private education and health care bureaucracies (3.34 million new jobs) and in bars and restaurants (1.53 million new jobs.) Uniquely, all net new jobs added fall in the non-supervisory/ production category -- half a million supervisory jobs were lost. Manufacturing lost 3.28 million jobs (19.1 percent) and now provides fewer jobs than in July 1942 -- seven months after the attack on Pearl Harbor.

Despite concerns about illegal immigration, since 2001 the labor force has grown more slowly (7.4 percent) than during any seven-year period since 1955 and participation rate of those in the labor force -- those working or looking for work -- also fell sharply -- from 67 percent to 66 percent. This is the reason that the unemployment rate, now 5.0 percent, is not much higher.

The average weekly wage for non-supervisory jobs buys 2.0 percent more now than seven years ago and the average real salary and benefits for all workers is up by 9.0 percent. These real increases are down from the bubble period of the late 1990s but they are far better than the declines of the previous 20 years. Unfortunately, these recent increases in "average" wages appear to be a product of the latest financial bubbles: the widening use of stock options and very large bonuses in compensation, particularly on Wall Street.

Median real wages have continued to decline, including by 1.4 percent over the past year. Median household real incomes fell 2.0 percent from 2000 to 2006 (latest data available) and even the average income fell 0.5 percent with inequality now the worst on records back to the 1960s. The total current savings of ALL households over the past three years is virtually nothing; by far the worst since 1933.

The foolishness of powerful, self-interested claims of a "new paradigm" is again exposed. The fantasy is that soaring debt and the loss of production through trade deficits are good things and the lack of current savings irrelevant. As a long forgotten advertisement once proclaimed: "If you don't have yourself an oil well, get one!" We can all live well from royalties and asset appreciation.

Soaring debt and debt schemes did drive up many asset prices, creating a borrowed illusion of general prosperity along with enormous actual wealth and power for a few. But now, unprecedented debt and soaring inventories of unsold homes are driving down the inflated prices for homes and other assets. For at least the next several years, most households will now be forced to cut spending and earn, not borrow, their living standard.

Another short-term debt stimulus may take the edge off the difficult economic conditions of the next few months. But trading away our once unique economic strengths while borrowing against the future has failed. Making even minimum interest payments on these massive, soaring debts will be increasingly difficult as the success of thoughtful industrial and trade policies in China and elsewhere continues.

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