Some"fundamentals" of the "new economy" exposed

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The economic communiqué issued by the G-7 leaders at last month's Genoa summit noted that while the world economy had slowed faster than expected nevertheless the "fundamentals" were sound.

But as a pointed comment by *Guardian* economics correspondent Larry Elliott on July 23 drew out, this assertion has become something of a mantra for the leaders of the major capitalist powers, or at least the bureaucrats who draft their statements.

"In the summer of 1997," he wrote, "when the G-7 met in Denver, Thailand was the first country to be affected by the Asian financial crisis. The fundamentals of the world economy were sound. A year later in Birmingham, Russia was about to default on its debts as its experiment with turbo-liberalisation went disastrously wrong. The fundamentals of the world economy were sound. When the G-7 gathered in Cologne in 1999, stock market speculation in the United States meant Amazon.com was valued more highly than General Motors. It was not a problem because the fundamentals of the world economy were sound. Nor was it a problem a year later, when investors had to rethink and decided that Amazon.com was really just a mail order company that made no profits, because—you guessed it—the fundamentals of the world economy were sound."

These continued assertions invite the obvious question: what are the fundamentals? For the capitalist system, notwithstanding all the attention to growth rates, productivity, inflation and the like, it is the level of profits. It is here that some of the fundamental problems of the global capitalist economy are starting to emerge, above all in its heartland, the United States.

Not only have US profit rates declined very sharply over the past year it seems that they have been considerably overstated for the past four.

The latest issue of the US magazine *BusinessWeek* points out that as far as the earnings of American companies were concerned the last quarter was a "bloodbath."

"Even with an 8 percent gain in sales, the 900 companies on *BusinessWeek's* Corporate Scorecard saw second-quarter profits plummet 52 percent from a year earlier, while margins fell to 3.2 percent from 7.2 percent. That's the largest decline ever recorded in the quarterly scoreboard—nearly twice the 27 percent year-to-year drop in the fourth quarter of 1991. And the current profit plunge follows a 25 percent decline in the first quarter."

Losses suffered by individual companies in the high-tech and communications area have been unprecedented. Last month JDS Uniphase, the world's largest maker of fibre-optic parts, announced that it was undertaking a $44.8 billion writedown of acquisitions it had made over the previous two years, taking its full-year loss to $50.6 billion. This is an amount equivalent to the gross domestic product of Hungary for the year 2001.

Other big loss makers have been Lucent Technologies, $3.35 billion, and the Canadian firm Nortel, $19.4 billion.

The losses and sharp profit drops go across the board. The US investment bank Credit Suisse First Boston has announced that, whereas in January it had expected profits for companies on the S&P 500 stock market index to be up 9 percent in the third quarter, it now expects them to be down by 9 percent.

A report by the firm UBS Warburg pointed to the dramatic turnaround in high-tech industries. "The lethal combination of rapidly expanding capacity and an abrupt downturn in demand," it noted, "has caused the tech sector to shift from 36 percent year-on-year

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earnings growth in the first three quarters of 2000 to a 65 percent decline in second-quarter 2001."

In addition to the profit figures, other statistics now coming in indicate that the years since 1997—the era of the "new economy"—were not all they were made out to be. Last month the US Commerce Department published its revised estimates for gross domestic product growth in 2000. These showed that instead of expanding at a rate of 5 percent, as previously reported, the American economy grew by 4.1 percent. This decline of almost one percentage point represents about $90 billion.

Even more significant than the GDP estimates were revisions to the estimates of corporate profits. One of the themes of the "new economy" proponents was that increased productivity, resulting from the introduction of new technologies, had ensured a continuous increase in profits and even the elimination of the business cycle.

The new estimates from the Commerce Department suggest that instead of growing by 10.3 percent last year profits rose by 5.7 percent, while the share of post-tax profits as a share of national income between 1997 and 2000 dropped from more than 12 percent to 8 percent last year. In other words, when the "new economy" was at its height, profit rates were actually falling.

What then is to account for the discrepancy between the picture of booming profits painted at the time and the real situation over the past four years?

The very least that can be said is that there is clear evidence for the large-scale practice of what is euphemistically known as "creative accounting." This is the process by which corporate executives and the upper echelons of corporate management inflate profit results in order to push up share values.

Not only does this ensure an increased flow of funds to their corporation, it directly boosts their individual salary packages, bonuses and stock option holdings which are most often tied to the share price. In short, the figures now coming in point to the fact that a key feature of the "new economy" was systematic looting.

Of course when this process came to an end—as it inevitably had to—it has not been the corporate chiefs who have paid the price but the workers.

A recent report by the US Treasury found that as a result of the slashing of investment plans some 350,000 workers lost their jobs in the second quarter alone. And this process will continue.

According to a comment by Morgan Stanley Dean Witter (MSDW), the squeeze on profit rates "dictates a regimen of corporate cost-cutting that is likely to persist even as the recovery unfolds. Labour costs and capital spending both face the axe. We expect that job growth will at best remain anaemic, and more likely, companies will continue to shed workers in the early stages of a turn in the economy."

But, according to MSDW, any turn around may be some time coming. This is because "business capital spending, which nose-dived at 13.6 percent annual rate in the second quarter, probably faces a couple more quarters of significant decline. And the risk is that this capital spending downturn could last even longer."

So much for "sound fundamentals". What has really been taking place over the past four years is the spread of rot and decay at the heart of the profit system, compounded by the practices of those in charge of its largest corporations.

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