

Will There Be a Recession?

By Fred E. Foldvary

The beginning of a new year is the traditional time to look ahead, make plans for the coming months, and try to guess what may happen. Many people are wondering what will happen to the economy. Will the economic boom continue? Will the trouble in East Asia spread to the rest of the world? What will happen to wages and profits?

Economic theory enables us to make conditional forecasts and predictions. However, since national economies are heavily politicized, the future depends not just on the market process but also on the decisions of officials such as the President, Congress, and the Federal Reserve and other central banks. There can also be natural disasters that can overturn forecasts. There are so many variables that nobody really knows the future. However, theory suggests that if nothing interferes, economies will move in particular long-run directions.

Many economists and journalists are surprised that the US economy has been so prosperous for so long without a recession or inflation. But this is the way economies should normally behave! The current economy is no surprise or mystery to those grounded in the geo-Austrian theory of the business cycle, which I have written up in the October 1997 issue of the American Journal of Economics and Sociology. The evidence during the last 200 years is that there are several types of cycles, which we can call short, major, and long cycles. **The short cycles run every four years or so, the major ones every 18 to 20 years, and then there are long cycles of about 60 years.** My focus is on the short and major cycles.

The short one has been called an inventory cycle and a political cycle. Since the last major bottom was around 1991, forecasters expected a recession around 1995. Officially, there was no recession, since the economy continued to grow, but the growth slowed down. On a per-capita basis, I would say there was a minor recession, since growth was below population increase for three out of the four quarters. After that, the economy took off. My view is that the economy is now on the next short cycle which would have a duration from 1995 to about 1999 or 2000. That puts 1998 in the middle of the short-run boom, coinciding with an election year when the politicians try to avoid any slowing of growth. Any economic problems due to the year-2000 computer problem will most likely occur in 1999 or 2000, not 1998.

The major cycle is tied to the real-estate cycle. The last major downturn was around 1990, which would put the next major recession around the year 2008. The US economy recovered from the major bottom and has entered the boom phase. Unemployment is low, profits are up, inflation is low, interest rates are low, and real estate is booming, with vacancies low, rents rising, and construction picking up. With the short and major cycles expanding, a recession is unlikely, though always possible.

It should be noted that even if the economy continues to prosper, that does not imply that the stock market will keep going up or that any particular investment strategy will do well. Financial

markets are influenced by psychology and speculation which don't always follow the economic trend. Financial markets look to the future, and expectations are often wrong.

What will happen to the economies of Thailand, Malaysia, Indonesia, South Korea, and the others affected by the collapse of their currencies and real-estate booms? This depends very much on the policies of the governments and the rules imposed by the International Monetary Fund as a condition for massive loans. Some of the policy changes, such as liberalizing their financial markets, will help their economies. Currency devaluations will boost their exports. Bankruptcies and a collapse of the unsustainable real-estate booms will clear the way to a fresh start. The US boom has been so strong that it has not been much affected by the Asian problems. Some industries, such as automobiles, will be pressured by cheap imports from Asia, but then consumers will benefit. The global boom, especially in the U.S. and Europe, will most likely pull up the Asian economies, not to speak of IMF bailouts. If there were a real global crisis, the price of gold would not likely be at such historical lows.

An ever-present threat to the global economy is war. The Israeli/Palestinian conflict remains deadlocked over the land question. The situation in Iraq remains a danger. But a more predictable long-term danger to prosperity comes from two key economic variables: money and land. The East-Asian problem is a precursor to the greater global crash that awaits the end of the major cycle. Though price inflation is low in the US, there is still money inflation. Instead of showing up in retail prices, money inflation can fuel the real-estate and stock markets and create an unsustainable boom in investments. Real-estate speculation in both construction and land prices, fueled by cheap credit, will ultimately lead to a great global crash. This has happened repeatedly in the US since the early 1800s, it happened to Japan in the 1980s, and we have just seen it occur in East Asia. **The remedies, free banking and public revenues from rent, are not even being talked about. Since theory indicates the big crash is a decade into the future, and both the short and long cycles are in the boom phases, 1998 should be a prosperous year. Too bad the politicians won't solve the long-term problem while there is time.**