Is the USA 2005 Technology Environment Headed in the Wrong Direction? Part 2

Business, economic & geopolitical indicators cause high anxiety in high technology, circa May 2005

by Russ Henke, Henke Associates

Abstract:

After eight years of an improving technology environment, the last five years have moved us in the wrong direction. This is the ***second in a series of articles*** *that explores business, economic and geopolitical indicators that have been causing high-anxiety in the world of high technology in the United States and elsewhere.*

The author observes at least a dozen enervating factors occurring over the last five years: *(1) unremitting extravagance in the face of the shift from US federal budget surplus to deficit, (2) the definite long-term trend of a rich-get-richer, poor-get-poorer US income distribution, (3) sluggish net job growth well below the requirements of US population increases, (4) a net US disadvantage in globalization, (6) weakened US environmental stewardship, (6) the ballooning real and psychic costs of war, (7) reduced worldwide admiration for US leadership, (8) the weaker US dollar, (9) rising energy, oil & gas prices, (10) a deteriorating domestic stock market, (11) ongoing corporate fraud, and (12) record trade deficits, requiring the US to borrow billions of dollars every week from abroad.*

The first article in this series was posted on CAD-Portal.com on April 15, 2005. It primarily covered items (3) and (10) from the above list of debilitating factors. ***This second article*** *mainly deals with the following topics: (1), (2), (8), (9), (11) and (12).*

Future articles in this series will focus on the remaining aspects of the "Dirty Dozen" factors mentioned above. Selected tech-industry success stories in coping with this overall negative atmosphere will also be provided in subsequent articles.

Factors that make it difficult to compete

Depressing as the ongoing sluggish US job growth and deteriorating domestic stock markets are (see Article #1 of this series dated April 15, 2005), there are plenty of other factors that make it difficult for companies to compete in today's business, economic and geopolitical environment.

inflation is back

Unfortunately, significant inflation is back. A 0.6% increase in the Consumer Price Index in March 2005 was the largest in five months. The 0.4% jump in the core rate, *which excludes* food and energy, was twice the forecast from analysts and the biggest monthly increase in nearly four years.

Consumer confidence is ebbing

US consumer sentiment fell *for the fifth straight month* in mid-May 2005 to its *lowest level in two years*, according to the May 13 announcement by researchers at the University of Michigan. The consumer sentiment index fell to 85.3 in from 87.7 in

April. *It's the lowest since the start of the Iraq War in March 2003.* The decline in the sentiment index was driven by the *expectations index*, which dropped to 73.7 in May from 77.0 in the previous month, *the lowest since March 2003.* The *current conditions index* fell to 103.3 in May from 104.4 in April, *the lowest since December 2003. "The consumer numbers out there were very frightening,"* said Chris Johnson, manager of quantitative analysis at Schaeffer's Investment Research in Cincinnati. *"The consumer is in the driver's seat in this economy, and a lot of big names depend on healthy consumer spending."*

Orders to US factories for major manufactured goods declined

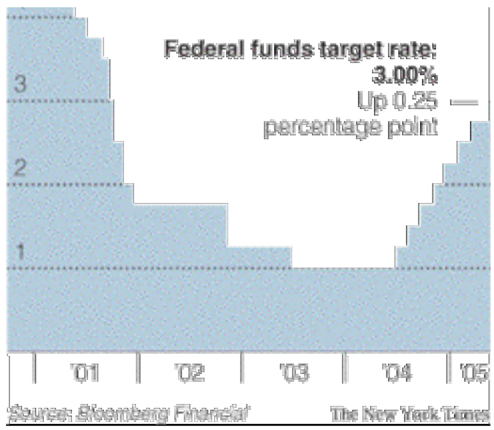
Orders to US factories for major manufactured goods declined 2.8% in March, the biggest reversal in over two years and the third straight monthly decline, the Commerce Department said April 27, 2005. The March drop, showing more fragility than had been expected, followed declines of 0.2% in February and 1.2% in January. The weakness in durable goods orders was just the latest evidence that the economy is entering still another ''soft patch'' as both consumers and businesses cut back on their purchases. The 2.8% drop in overall orders was the biggest decline since a 6% plunge in September 2002. It was a far worse performance than "analysts" had forecast; they had been expecting that orders would *rise* by 0.3% in March. The three consecutive monthly declines in new orders was the longest stretch of weakness since the three straight declines from July through September 2001 (during the "official US recession" of March through November 2001).

US GDP slow growth bodes stagflation

The US economy (GDP) grew only 3.1% during the first three months of 2005, the second straight quarterly decline and the slowest rate in two years, the government also reported on April 27, 2005. The slowing growth and rising prices revived talk of **stagflation**, the troubling economic condition that combines the worst of both worlds. The recent GDP report showed business investment slowing sharply in Q1 2005 from the fourth quarter 2004. Investments in equipment and software were the slowest in two years. An inflation gauge tied to the GDP report and closely monitored by the Fed (Federal Open Market Committee) showed a 2.2% Q1 2005 rise in prices, *excluding* food and energy. That was up considerably from the 1.7% rate recorded in the fourth quarter of 2004, and marked the highest quarterly reading since the final quarter of 2001.

On May 2, 2005 it was announced that another respected barometer of manufacturing fell sharply. The **Institute of Supply Management's index** of factory activity dropped to 53.3 in April, from 55.2. It was the fifth monthly drop in a row for that index. Meanwhile, global economic growth appears to be slowing to a lethargic 1% per year.

"Stagflation is rearing its ugly head," said Peter Morici, a business professor at the University of Maryland. "The Fed faces a Hobson's choice: **either** reigning in inflation **or** tolerating unacceptable levels of unemployment." ***Not surprisingly, the Fed chose the former on May 3, 2005.*** *It increased its target for overnight interest rates by one-quarter of a percentage point to 3%, the eighth such raise since last July.* The May 3rd language of the Fed's accompanying policy statement left little doubt that more rate increases will follow, although later in the day, the Fed inexplicably revised its statement, adding a phrase that "longer-term inflation expectations remain well-contained." Huh? "They appear to be just as confused as the rest of us" (on the economy), said Mike Holland of the Holland Balanced Fund. Also, in contrast to the wording used in March, on May 3rd the panel omitted a soothing declaration that higher energy prices had not significantly fed into increases in "core" consumer prices outside of food and energy.



Manufacturing job loss continues

The Labor Department reported May 6, 2005 that US employers added a preliminary total of 274,000 jobs in April 2005, enough to keep up with population growth for the month and keep the country's unemployment rate level at 5.2%. *However, manufacturing again lost jobs (the 9th decline in the last 12 months), while 229,000 (84%) of the April gains came in service industries (e.g. leisure and hospitality 58,000; professional & business services 36,000; retailers 24,000).* Furthermore, there remained 7.7 million US inhabitants unemployed in April, with the average duration of 19.6 weeks without work, the highest level in a year. For the 31st month in a row, more than 20% of out-of-work people have been unemployed longer than six months. Counting April 2005, the average job growth for the past 12 months is only 181,000 jobs a month, not nearly enough to allow the US economy recover from the lowered standards of living and lost savings that the periods of recession and unemployment have caused since 2001.

Today American workers (especially younger ones) face depressing jobs' prospects. The employment rate for US teenagers in the first 11 months of 2004 - just 36% - was the lowest it has ever been since the US government began tracking teenage employment in 1948. The recent modest surge in jobs in the last 12 months has left out most young Americans. From 2000 through 2004, gains among recently arrived immigrants seem to have accounted for the *entire net increase* in jobs. Some segments of the population have been almost totally bypassed. In Chicago, only one of every 10 black teenagers found employment in 2004. In Illinois, fewer than one in every three teenage high school dropouts are working. Accordingly, it's no accident that the standard of living of large segments of the US population is tumbling when corporations retain all the power, including the dogged support of the current administration. As previously mentioned, US workers can't even get a modest increase in the national minimum wage! *"The economy is growing and real output is up,"* said Andrew Sum, a professor at Northeastern. "*But the distribution of income, in terms of how much is going to workers - well, the answer is very little has gone to the typical worker. In many cases, young men and women of today are faring less well than their parents' generation did at a similar age. Two-thirds of this generation are not living up to their parents' standard of living."* Globalization was supposed to be the ultimate tool for raising the standard of living for all. Instead, US wealth has become even more dangerously concentrated. Bob Herbert of the New York Times recently quoted Louis Brandeis: *"We can have democracy in this country, or we can have great wealth concentrated in the hands of a few. But we can't have both."*

Productivity is up, but rate declined

Preliminary figures for US productivity came at an annual rate of 2.6% in Q1 2005, the Labor Department just reported. While 2.6% would be the best showing in nine months, it is still below the larger gains of earlier years. In fact, productivity gains since the third quarter of last year have been decidedly lower than the increases that occurred when the US economy was trying to pull out of the 2001 recession. US employers then were able to boost output *without hiring back laid off workers*; one can only imagine what the employers will do with the lower productivity gains these days. Hourly wages have improved only 2.7% over the last year, not enough to keep up with the 3.1% annual inflation rate. Also, economists said that the April Jobs Report would keep the Fed on a course of raising interest rates through the rest of 2005.

Ongoing Corporate Fraud remains fundamentally unpunished:

With only a few exceptions (e.g. Worldcom's CEO Bernard Ebbers temporarily convicted of fraud on March 15), **corporate fraud remains fundamentally unpunished.** Even when prosecuted, minor fines often replace real accountability. *Ten directors of Enron agreed to pay a paltry $13 million to settle a class action lawsuit, yet Enron's 2001 collapse wiped out $60 billion in shareholder value (that's billion with a "b").* Twelve Worldcom directors recently got a similar easy deal ($24.5 million total). *Time Warner Inc. just agreed in mid-March 2005 to pay $300 million to settle a complaint by the S.E.C. that the company's AOL unit overstated revenue for nine quarters. Time Warner had initially settled with the S.E.C. staff in December 2004 on another matter for $210 million. The S.E.C. and the Justice Department could still file additional complaints against individuals involved in AOL's accounting scandals. (Meanwhile, the company plows on –- on May 4, 2005 it was announced that Time Warner Inc. topped Wall Street's expectations with its first-quarter profit).*

In the American International Group's most recent inventory of accounting improprieties, disclosed on May 1, 2005, the company said it would probably reduce its net worth by $2.7 billion, some $1 billion more than it had previously estimated.

New frauds and cover ups seem to appear almost monthly (insurance brokers, drug companies, et al).

Instead of decreasing, the number of ***restatements of corporate financial reports*** *in 2004 was the highest in five years*. The number of shareholder lawsuits also increased in 2004. The quality of corporate earnings "gap" is still at 13.7%, vs. the long-term average of 6.7%. (This "gap" is the difference between GAAP earnings and "operating earnings" which do not include write-offs and other unusual items). Yet the S.E.C. is now under pressure from administration officials, business groups and Wall Street to retrench on the recent regulations meant to help curb corporate abuses.

Bankruptcies continue - pension plans in jeopardy

On May 10, 2005 a Chicago Bankruptcy Court judge approved **United Airlines'** request to ditch its pension plans and shift responsibility to the government, the latest move by the troubled airline. United thus becomes the biggest pension defaulter in the history of corporate America. The change will definitely cut United employee pensions. Many United employees and retirees view the company's pension-cutting plan as a kind of betrayal. They spent years -- in many cases, decades -- working for the airline. Between these changes in United pensions *and the current political fights over Social Security,* employees rightly wonder how much retirement income they'll really have. Many workers see the pension change as just the latest painful concession they had been forced to make. The airline's employees already have given up $2.5 billion a year in wage and benefit cuts.

Oh yes… one day after that federal judge allowed United to terminate 120,000 employee and retiree pensions, the bankrupt airline was back in court May 11 seeking cost-cutting changes in its labor contracts. Here's the headline: "UNITED STILL WANTS MORE FROM UNIONS. Pension handoff not enough: After losing $1.1 billion, airline seeks another $725 million in labor savings." And so it goes…

With this default, United will unload $6.6 billion of obligations onto the **Pension Benefit Guaranty Corporation,** the federal agency created in 1974 that insures corporate pensions. The number of pension plans so dumped onto US taxpayers rose to 192 last year, up from 155 in 2003. The number of workers and retirees in such plans now exceeds 1.1 million, including United Airlines' workers and retirees. That's not counting the some 1,200 relatively stable companies that *chose* to close down their fully funded pension plans last year in an effort to move workers into less costly retirement savings plans, like 401(k)'s.

Alas, American companies often under-fund their pensions. The New York Times reported that only 20% of a total of $450 billion in under-funding is due to actual financial distress at companies. The rest is occurring at businesses that are financially healthy but are simply and evading their responsibility to put the proper resources into their pensions. With the United default alone, the federal pension agency's deficit will rise to $23 billion; as recently as 2001, it had a surplus of $7.7 billion. Sound familiar? Analysts had predicted that if United won *its* case, there could be a **domino effect** as other airlines are forced to seek bankruptcy protection to bring their pension costs down to United's levels. Such moves would probably swamp the Pension Benefit Guaranty Corporation.

Meanwhile, **Delta Air Lines'** battered stock fell May 11 *to its lowest level in at least 25 years* following the company's warning about *further losses* and –- yes -- *the possibility of bankruptcy.* Continental & Northwest may not be far behind.

The defaulting pensions' story is just part of a far wider problem. Consider this quote from **Marshall Loeb**, former editor of Fortune, Money, and The Columbia Journalism Review, from the May 13 CBS MarketWatch*: "No matter what curveballs and disappointments life might throw at you, there always have been several unshakeable things in which you could trust: your family, your closest friends, your community -- and, of course, your retirement, supported by your long-promised pension. Indeed, this bond of trust has been the crucial part of the American social contract, which links workers and managers in common cause. Managers trusted that workers would be efficient, industrious and loyal. Workers trusted that the managers would treat them decently and pay them fairly, whether on the job or in retirement.* But now that trust is being ominously strained. *Increasingly, Americans are being told that they won't always be able to count on their pensions to carry them through their lengthening life, not even if they have worked for decades for one of the world's great companies."*

Of course, the fate of **the US Social Security System** now hangs in the balance as well.

Rising energy, oil & gas prices:

Utility prices are now much higher due to illegal price manipulations by power market brokers, yet US consumers are now stuck with the bills. Oil and gasoline prices in the US soared to record levels in late 2004 and were then reduced slightly at a maddeningly slow pace, before spurting up again in February-May 2005. Crude oil futures ended the week 2.5% higher on May 6, 2005.

Despite the high prices, gasoline *demand* in the United States has shown no sign of a slowdown; over just the month of March 2005 demand was more than 2% *higher* than it was a year ago. For 2004 overall, the price of energy in the US was up 16.6% vs. 2003.

US dependence on foreign oil continues at a historical high. The situation has gotten worse since the first oil crisis of the 1970s. Then, the US relied on overseas sources for about a third of its oil. Today, dependence has grown to over 56% and by 2025, would reach 68%, if nothing changes, according to the US Energy Information Administration (EIA).

The nation's passenger fleet (cars and light trucks) gets virtually the same mileage today as it did some 25 years ago (about 25 miles per gallon), according to the Department of Transportation. Fuel economy standards have not been updated by Congress since 1987. Moreover, pickups and SUV's are still exempted from the fuel-economy standards that apply to cars, weighing down the overall fleet mileage. *Yet the current administration and Congress studiously ignore the surest way to reduce demand and thus oil dependency, which is to mandate standards to improve the fuel efficiency of America's cars and trucks.*

At the same time, US gasoline reserves are falling. The US EIA continues to see a tight global oil supply and demand balance through 2006. The strong demand growth coupled with limited spare crude oil production capacity means that high energy prices are here to stay. Global oil demand continues to grow at 2 million barrels per day or more, without a comparable increase in crude oil production capacity (e.g. no new refineries in the US in years). Unless actions are taken, it's difficult to imagine demand slowing or supply capacity growing significantly. That is why the EIA is not expecting oil to fall below $50 per barrel for a sustained period anytime soon. The price of natural gas has also risen over 11% in the western United States. Meanwhile, oil company profits are at obscene levels. *Could it be that oil companies are actually profiting from the rise in raw material (crude oil) costs, at the expense of US consumers?*

A letter to President Bush in March 2005 signed by more than 30 military and security officials, including Robert McFarlane (former national security adviser to President Reagan) stated, "We believe that the United States' dependence on imported petroleum poses a risk to our homeland security and economic well-being,"

Of course, many in Congress and in the oil industry argue that the US *does* have a plan to reduce dependence on foreign oil: *the new Energy Bill now before the Congress!*

But such measures aren't nearly enough, critics say. Even the package of energy-saving measures unveiled recently by the bipartisan *National Commission on Energy Policy*, which goes well beyond the provisions of the current Energy Bill, would cut oil imports by only 1.6 percentage points by 2025. *(By the way, the new Energy Bill gives $8.1 billion in* new *tax breaks to oil companies. Say what?).*

Unfortunately, big oil companies have not been using their enormous profits to invest in more refinery capacity. As a result of this deliberate strategy, Mark Baxter, director of the Maguire Energy Institute at the Cox School of Business at Southern Methodist University in Dallas, said of the potential impact that with oil prices so high, supplies so tight and refineries running at very high capacity, the BP explosion would probably bump prices of oil and gasoline higher in the short term. "The magnitude of the impact today is greater than it would have been 10 years ago," Mr. Baxter said, "because we are in such a tight, volatile market."

US Auto Industry Struggles with Globalization

With the high prices for gasoline and declining consumer confidence, the number of US consumers planning to buy an automobile in the next six months recently fell to 4.2%, the lowest level since 1967! The US auto industry is sorely affected, with shares of General Motors and the Ford Motor Company trading near one-year lows and the companies continuing to lose customers.

Sales at GM fell 12.6% in February from the same month a year earlier, according to monthly sales reports released by automakers on March 1, 2005; Ford's sales fell 2.8%. Both companies scaled back the numbers of cars and trucks they planned to make. Overall, auto sales in the United States fell 1.8% in February from the same month a year earlier. Full-size SUV sales fell 21% in February, compared to a year earlier, and that's after a 31% drop in January, according to data from an affiliate of J.D. Power and Associates. On March 16, GM stock fell 14% in one day when it estimated a loss of $1 Billion for the previous six months. On April 1, both General Motors and Ford said that new vehicle sales in March 2005 failed to match year-ago levels, despite hopes for a recovery after a tough winter. Meanwhile, some Asian brands reported record US demand. On April 19, GM announced a $1.1 billion loss for Q1 2005 alone.

Little Relief in sight

Alas, April 2005 figures provided no relief to GM and Ford. The latest automobile sales stats were bad news for GM and Ford, which both saw their sales slip again. But both Toyota and Nissan posted sales gains, such that overall auto sales in North America were actually up 1.8% in April! GM's sales fell 7.7% from the same month a year earlier, primarily because of a weaker demand for SUV's. Ford sold 5% fewer vehicles in April compared with a year ago.

Meanwhile, Toyota reported that April 2005 was the most successful month in its history. Its sales were up 21.3% on big gains in the number of passenger cars sold. Nissan also had a record month with sales up 27%. Toyota said the surge in sales of its gas-electric hybrid (the Prius) and other fuel-efficient models, were the primary reasons for its excellent April.

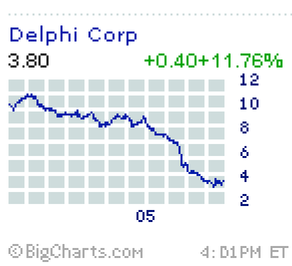
Market share fell at both GM and Ford in April. GM lost the most; its market share dropped to 25.1% in April, down 2.6% from April 2004. Toyota's North American share jumped to 14% from 11.7% a year ago.

The Chrysler division of DaimlerChrysler was the only share gainer among the Detroit automakers, eking out a meager 0.4% rise year-over-year. However, Toyota sold more vehicles in the United States than did Chrysler in April, a rare event likely to become more frequent going forward. (DaimlerChrysler's overall sales in the United States were up 4.6% in April).

On Cinco de Mayo, Standard & Poor's Ratings Services declared the billions of dollars of debt owed by General Motors and Ford to be "junk," a hit that will increase their borrowing costs. The companies' debt was downgraded to "below investment grade" (a.k.a. "junk" status), causing both automakers' stock to fall on Wall Street and leading their respective stock markets lower. Over and above their large health care and post-retirement liabilities, GM paid about $12 billion in interest on debt last year and Ford's cost was around $7.1 billion. GM's consolidated debt as of March 31, 2005 was $292 billion and Ford's totaled $161 billion, Standard & Poor's reported. While the two companies will likely have little difficulty accommodating "near-term cash requirements." the debt downgrading will cause many institutional investors to sell GM and Ford bonds at a lesser value, since some institutions are barred from trading in junk bonds. GM shares fell 6% on May 5, dragging the Dow down 44 points. Ford shares declined 4.5%, helping to drive the S&P 500 down some 3 points.

Billionaire corporate raider **Kirk Kerkorian** said he intends to more than double his current GM stake. In the auto industry, Kerkorian is best known for a bid to buy Chrysler some 10 years ago. While that attempt failed, he was left with a large chunk of Chrysler shares that he proceeded to unload at a robust profit. Should Kerkorian actually acquire more GM shares, some analysts believe that he might end up demanding that GM sell part or even all of its profitable finance division, which is itself valued greater than GM's total consolidated current market worth. Should this happen, GM would be left without much of its present financial cushion.

GM’s troubles of course affect a giant supply chain. To chose just one, struggling auto parts supplier Delphi Corporation on May 13 posted a first-quarter loss of $409 million, reflecting weaker-than-expected production volumes from US automakers, particularly General Motors, its top customer. Delphi's revenue fell about 7% to $6.9 billion in the latest quarter. Delphi stock is trading near its lowest point since spinning off from GM in 1999 (see graph below). Delphi now projects that GM's North American operations will turn out about 4.5 million units this year. This, in turn, would mean a *reduction of a billion dollars* in Delphi's revenue forecast for 2005.



The upcoming **Annual GM Shareholders Meeting** in Delaware on June 7, 2005 should provide CEO Rick Wagoner an important chance to articulate GM’s comeback strategy.

US imports exceed exports at record levels

Today, overall US imports are exceeding exports at record levels, bloating the country’s **trade deficit.** November 2004 provided a then-record high trade deficit of $60.3 billion; the bill for imported oil jumped 17.7% in the month! The year 2004 saw a record trade deficit of $618 billion, a 70% increase since 2001. Then America's appetite for foreign imports broke all previous monthly records in January 2005, reaching $159.1 billion (see the graph below) and contributing to a monthly trade deficit that was then the second highest on record (second to ... November 2004).

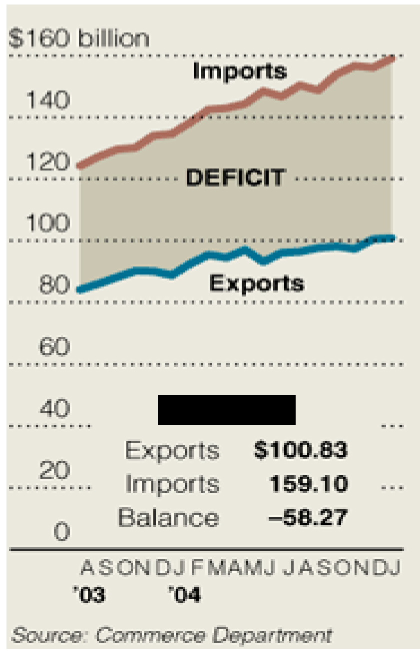
The January $58.3 billion trade deficit defied "predictions" that a weakened dollar would narrow the United States' trade gap.

While most other industrialized countries enjoy a trade surplus with China, the United States had a deficit of $15.3 billion in the month of January 2005 alone, the largest with a single country on record. Galvanized into broad action, the US administration, at long last reacting to the flood of Chinese clothing imports since January 2005, announced on May 13, 2005 that it would seek to impose new quotas on Chinese cotton shirts, trousers and underwear. *Wow!* Pressure had been building on the administration to slow Chinese imports long before the global textile quota system ended on January 1, 2005. But since then, China's booming textile and apparel industry, unhampered by quotas, has grown ominously. Chinese exports of cotton trousers to the US have grown by 1,500% and by 1,350% for cotton knit shirts, according to trade figures. At the same time, the US textile industry has lost 16,000 jobs and 18 factories have closed, per US government reports.

Unfortunately the new clothing quotas won't take effect for quite awhile, since the administration must first "notify" China of its decision and then "hold discussions" about the size of the limits. China has already warned the US (and Europe) that it will resist any attempt to limit Chinese textile and apparel exports.

Of course, textile issues are just the tip of the trade deficit iceberg with China. Lawmakers in the US Congress say that China fails to follow the WTO rules. *No kidding?* Several new bills are being debated that would impose penalties on China for currency manipulation, violating intellectual property rights and following other forbidden practices like giving its producers overly lenient loans and export tax rebates. We'll see how long it takes for Congressional or administration action to occur on these fronts.

The trade deficit may be the single most important issue in assessing the extent to which US lives beyond its means. Accordingly, it should cause US citizens and leaders to finally comprehend the dangers of huge deficit spending. "But the White House is showing virtually no sign of action, as if doing nothing might make the problem smaller", according to The New York Times. For having done such a good job managing the country's trade deficit, while the US manufacturing sector lost 2.8 million jobs over the last three years, the US Trade Representative Robert Zoellick was recently promoted to deputy Secretary of State under Condi Rice, who herself did such a great job as National Security Adviser for the last four years. For the first two months of 2005, the US trade deficit was running at an annual rate of $717.2 billion, about $100 billion above the record imbalance set in 2004.



The annualized Q1 2005 trade deficit subtracted some 1.5 percentage points from Q1 2005 GDP, the largest drag on US growth in two years. While exports increased 7%, imports swelled 15% over the quarter.

On May 11, 2005, the Commerce Department reported that the US trade deficit narrowed slightly without warning in March 2005. Exports rose as predicted some 1.5% to $102 billion in March, *but instead of increasing, imports fell 2.5% unexpectedly to $157 billion.* Robert Brusca, chief economist at Fact and Opinion Economics, was concerned with this unusual reduction in imports. "Import slowdowns are a good and reliable barometer of economic weakness," Brusca said on May 11. This was the largest decline in imports since December 2001. The decline in March 2005 imports was widespread, with sharp drops in imports of consumer goods and autos. Even with the reduction of imports in March, Chinese textile imports for the first three months of this year are up 54% compared with the period last year. The reduction in March imports could have been even worse (imports of goods alone fell over 3.1% in March to $131 billion) were it not for the – you guessed it -- strong imports of crude oil. The US imported 326 million barrels of crude oil in March 2005, or 10.5 million barrels per day, up from 296.9 million in February 2005. The nation’s petroleum deficit widened 4% to $17 billion in March, the second largest US petroleum deficit on record.

On May 12, 2005 the Dow closed down 111 points, marking the *seventh* triple-digit decline for the blue chip gauge over the past month. The NASDAQ and the S&P 500 also dropped. Decliners outnumbered advancers 24 to 9 on the NYSE and 19 to 11 on the NASDAQ. Wal-Mart, THE LARGEST CORPORATION IN THE WORLD, was a big loser, off 2%, after the company reported that both revenues and adjusted earnings came up short of expectations. Paul Nolte, director of investments at Hinsdale Associates, said that the Wal-Mart announcement put a negative spin on the May 11 trade numbers as it confirms that higher oil prices and interest rates are having an impact on the economy. *"In general, the numbers are pointing down and pointing to a slower economy,"* Nolte said. The Labor Department also reported, on May 13, that *prices of imports* into the US rose a greater than expected 0.8% in April. Excluding the 3.1% increase in imported oil prices, import prices increased 0.4% -- *the largest gain since November 2004.*

The Federal Budget Deficit Balloons

From a huge surplus only 3 years ago, US federal deficits have now ballooned to unprecedented levels. And the latest federal budget submitted in February 2005 does little to reduce the deficit in fiscal 2006. Today, the national debt is near $8 trillion! *Over the last four years, federal revenue as a percentage of GDP has plunged to levels not seen since the 50's. To paraphrase a slogan from past elections,* It's the REVENUE, stupid!"

The ranks of US citizens living in poverty are steadily increasing. Consumers, who have been the remaining driving force of growth for the last four years, are pushing themselves to the limit. Estimates are that the personal savings rate in 2004 dropped to 0.8%, the lowest level since 1933! Health Care costs increase by double digits yearly, yet more & more Americans have no health insurance. Meanwhile, the average pay for CEO's of the S&P 500 has tripled since 1993. The top 1% of US households now own nearly 40% of the household wealth.

The **value of the US dollar** has fallen to record lows. In November 2004, gold rose above $450 an ounce for the first time in more than 16 years, driven by investors looking for an alternative to the American currency. As mentioned earlier, to this point, the dollar's depreciation has not narrowed the nation's trade gap.

The "Twin Deficits" - trade and federal budget

If the decline in the dollar gets too severe, it could drive US bond yields up like it did in the early 80's under President Reagan. For anyone who chooses to remember, this could mean a return to 15% to 20% mortgage rates and a similar recession, when **the "twin deficits" in trade and the federal budget** severely damaged US economic competitiveness. Worse, the country is now being led into deeper and deeper dependency on debts owed to rival nations, who could "pull the plug" at any time.

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Future articles in this series will focus on other aspects of the "Dirty Dozen" Factors mentioned in the Abstract above.

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Russell F. Henke, PhD, FSME, PE, FASME, is president of *Henke Associate*s, business/management consultants to over 30 hi-technology client companies worldwide for the last nine+ years. During the previous 25 years -- while serving as corporate officer, board member or entrepreneur -- he was active in developing, marketing, selling and supporting commercially-successful applications software & global professional services in electronic design automation (EDA); finite element analysis and Mechanical CAD/CAM, including the most modern Internet e-commerce; as well as industrial and electronics manufacturing. He held consecutive corporate executive positions at Mentor Graphics Corporation, Automation Technology Products, Gould Electronics, Schlumberger Applicon, and SDRC. He started his career in the machine tool training program at the Cincinnati Milling Machine Company and simultaneously earned ME, MS and PhD degrees at the University of Cincinnati. Henke also "moonlighted" as an adjunct assistant professor, teaching mathematics and engineering for 13 years. In 1989, Henke received a Distinguished Alumnus Award from UC. A member of ASME, IEEE and the SME, Henke was elected an SME Fellow in Class of 2000, one of only 225 Fellows in SME's entire history. Henke was also elected in 2001 by the SME Membership as an International SME Director. Henke received an award for Professional Leadership from the IEEE in 2002. He was elected an ASME International Fellow in 2003. http://www.henkeassociates.net

CAD-Portal.com, founded in April 2000, provides a website community that unites the best CAD resources on the internet. The website focuses on MCAD, ECAD, AEC, GIS and more, as well as hosting TechniCom's eWeekly newsletter. eWeekly focuses on the mechanical CAD/CAM/CAE/PLM marketplace. Each issue provides the latest industry news, events, and is often added to by industry analysts who provide reviews of the latest software and tools. CAD-Portal.com's internet engineering portal allows users to contribute and get feedback in aninteractive environment. The various forums are used by customers and industry experts, which enables CAD-Portal.com to be a non-partisan judge of the best CAD resources on the internet. CAD-Portal.com's technology partner, TechniCom, Inc., a leading market research and consulting firm, focuses on the dynamics surrounding the mechanical engineering design and manufacturing marketplace. http://www.cad-portal.com.