

# PROTECTIONISM RETURNS

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American people are enthused by the possible win of democratic Party nominee Barack Obama for the November presidential elections. Many believe that Republican Party nominee John McCain will continue with old policies of war in Iraq, free trade and outsourcing and the American economy will continue to sink. There is partial truth in this. Obama is opposed to the Iraq war and wants US troops back home within two years. But he also supports aggressive US military intervention in other areas. In a TV interview he said that the military power saved from Iraq should be used to secure a decisive win in Afghanistan. In the result, there will be only small reduction in defense expenditures and the US economy will continue to sink as now.

The decline of the US economy is fundamentally due to reduction in the incomes of American workers, import of cheap goods like garments and toys from China and of cheap services like processing of insurance claims and call center services from India is leading to lower wages for American workers. They had previously taken loans and bought houses in expectation of continued high incomes. A software programmer working for lead bank J P Morgan explained how they landed into trouble. One person purchased a house on zero down payment and borrowed \$250,000 from a bank for this. He had to pay instalment of \$1,700 every month. He rented out the house at \$1500 per month. He paid the deficit of \$200 every month from his pocket. He hoped to get possession of the house almost for free at the end of 30 years when the loan was fully repaid. But the recession changed this rosy picture upside down. The amount of instalment increased from \$1700 to \$2500 because the loan was taken on variable rate of interest. The instalment increased along with the rate of interest in the US economy. At the same time, the income from rent declined from \$1500 to \$1000 because lower wages of American workers forced them to live in smaller houses. In the result the deficit increased from \$200 to \$1500. The borrower was not in a position to bear this impact and his house was forcibly taken over by the bank. The bank, in turn, tried to sell the house in order to recover its money. This led to increased availability of houses for sale and lower prices. The financial sector thus slipped into a crisis.

Obama wants to solve this problem by embracing protectionism. Higher import duties will be imposed on import of goods and services from China and India. Higher rates of taxes may be applied to US companies outsourcing services from India. He is also opposed to the free trade agreement the US was made with Mexico and Canada known as NAFTA. This will lead to higher price of imported goods and services and make it possible for US employers to pay higher wages. Obama's strategy appears to be in the right direction.

McCain's approach, on the other hand, is to lower import duties so that US corporations can stay competitive in the world markets. This will help US companies to survive but not help generate higher incomes for the US workers.

Obama presents a hope for the American people. A middle aged woman working as a delivery person for FedEx said, "The economy will go up with Obama."

But Obama also wants to increase government delivery of social services. American schools are wholly financed by the Government. Education up to level 12 is free. The teachers appointed by the Government do not impart good quality teaching just as Government schools in India provide shoddy education. Americans are consequently not able to compete with the Indian and Chinese suppliers and jobs are moving abroad. The problem seems to lie in poor motivation of government teachers. Yet Obama wants to increase government expenditures in education. He wants to provide funds to schools to retain good quality teachers. But the problem is of motivation, not of salary. This will lead to more government monies going down the drain

Obama may not deliver. Protectionism will lead to higher incomes for US workers while increase in government expenditures on education and health will wipe out that gain. McCain's policies are no better. He will bring more troubles for US workers by promoting free trade; but his policy of not increasing government expenditures will be good. In the end both the candidates will fail to lift the US people from their present miseries.

The immediate problem before US policymakers is that of the banking crisis due to default on housing loans by large number of borrowers. Both Obama and McCain want to use government money to protect borrowers from losing their only house to banks. Obama wants to create a government fund of \$20 billion while McCain wants to make a smaller fund of \$7 billion to bail out borrowers. This policy will not deliver because the fundamental causes of the crisis are not attended to. The decline in wages of US workers will not be arrested by providing such subsidies.

The next issue is that of rising prices of oil. Americans are having to pay more for commuting from home to office because they like to live in suburban areas. Businesses are under stress because their cost of production has increased. Obama has suggested suspension of taxes on oil to provide relief to people while McCain has suggested lesser relief. This policy will be harmful for America. Lower prices will encourage Americans to burn more oil and put heavier load of imports on the economy. The dollar will sink more. That said McCain will be better because he proposes lesser reduction of taxes.

The source of American prosperity is creation of new technologies. The assembly line, nuclear power, jet airplane, personal computer and internet are all gifts of this country. American companies earn huge monies by selling their new innovations at high prices like Microsoft sells Windows. Many of these innovations have been jumpstarted with government grants. Nuclear power and the internet are two examples. American Government must continue to make large investments in research to maintain this lead. Obama is disinterested in this. His focus is on reaching good quality education to the poor. McCain is more focused. He wants to increase government investment in research in areas such as energy. Thus McCain will be better for the US economy.

Obama's heart is at the right place. He wants to protect American people from the tyranny of the global markets. It is likely that he will win the presidential race. His policy of protectionism will provide some relief to the people. But this will be

nullified by his other policies-increase in government expenditures on education, more relief on housing loans and on price of oil and less investment in research. In the end the US economy is likely to continue going downhill although American people may get some temporary relief with Obama. □□□