

NOTE

## The Decline of America

**Bharat Jhunjhunwala writes :**

America is slowly sinking into a recession. President George W Bush has reduced income tax rates to place more income in the hands of people, increase consumption and demand, and ward off the impending decline in living standards. The US Federal Reserve Board has simultaneously slashed interest rates by an unprecedented 0.75 percent to boost borrowing-led consumption such as in buying of cars. It is also expected to lower costs for US Corporations and enable them face competition from cheap imports. In all probability these measures will fail and, in fact, become the trigger for America sinking deeper into recession.

Economic growth is sustainable only when consumption rises along with increase in production. Investment can pull the economy forward for a short while only. This sustains only if there is demand for the goods produced. A farmer is much benefited in planting of teak trees if there is demand for them when ready. This is similar to establishing a factory. The same investment leads to heavy loss if demand is not forthcoming. This point was made by the legendary economist John Maynard Keynes: "Consumption-to repeat the obvious-is the sole end and object of all economic activity... The consumption for which we can profitably provide in advance (by investment) cannot be pushed indefinitely into the future... Each time we secure today's equilibrium by increased investment we are aggravating the difficulty of securing equilibrium tomorrow."

American economy is producing goods but demand is less. For example, real estate companies have built apartment complexes but there are no takers. The demand is less. Truly, this problem had reared its head five years ago after the bursting of the *dotcom* bubble. But the US Federal Reserve Board, under the leadership of Alan Greenspan, reduced interest rates, especially for housing loans. American people borrowed and bought homes in expectation of future incomes. The party continued for five years. But the borrowers were not able to generate incomes to repay the loans. This has now led to seizure of their properties, loss to lending banks and America is sinking into a recession.

The reduction in rates of income tax will lead to reduction in the income of the Government and increase of the same in the hands of taxpayers. This is not likely to lead to an increase in demand for American goods.

The US Federal Reserve Board has reduced interest rates. This too will be futile. Income of the people does not increase by borrowing. If that were the case debt-ridden Indian farmers would never have committed suicides. Remember that interest rates in Japan are near zero yet that economy is sinking into a recession. The basic point is that lower tax shifts income from Government to citizens and lower interest rates shift income from future to present. These measures do not create incomes.

America is in for deep trouble. That country has accepted the mantra of free trade. Agriculture is an exception, that does not change the basic complexion of their economy. In consequence, goods produced by cheap Chinese labour and

services produced by cheap Indian workers will be imported into the US and lead to undoing of the American economy.

The truth is that the meek will inherit the earth. The rich will suffer. Countries where there is poverty, that is, where the wages are low, or where the cost of production of labour power is less, will win. The policies implemented by the American leaders do not deal with this problem. The correct solution for America is to abandon free trade and adopt a policy of protectionism to protect its producers from cheap Chinese and Indian labour. But that requires a change of mindset that is difficult. Such a policy is moreover harmful for their corporations that are making huge profits in China. These American corporations are the biggest enemy of America. They are killing American industries and jobs by producing in China and they determine America's economic policies.□□□