Towards a "New Great Depression" in America: Sluggish Economic Growth, Staggering National Debt

Between Scylla and Charybdis

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The American economy is caught between the Scylla of sluggish economic growth and the Charybdis of a staggering national debt aggravated by Washington's unyielding partisan deadlock over taxes and spending cuts.

After the Great Recession of 2008, the approaching "fiscal cliff" at the end of this year threatens to cause even more economic havoc and bring about another recession which some "doom-and-gloom" economists darkly predict may turn into a new Great Depression. The new "normal" state of the economy is marked by a stalled economic recovery, low consumer demand as well as persistently high unemployment engulfing large sectors of the population. The same "gloom-and-doom" economists even claim that the real level of unemployment may be close to the Great Depression level of 25% if one subtracts the number of those gainfully employed from the number of all working-age adults in the active population. But even "optimists" like the IMF's chief economist Olivier Blanchard insist that economic turmoil will continue and that the global economy may take a decade to recover from the financial crisis.

According to Dr. Joseph Stiglitz, the Nobel Prize-winning ex-chairman of President Clinton's Council of Economic Advisers, a growing economic inequality between the "haves" and the "have-nots" endangers America's future. In his latest book, Stiglitz argues that deeply unequal societies like ours cannot have stable economies and that worsening economic inequalities lead to instability and great economic crises. It does not take a Ph.D. in economics to see that the World Bank's former chief economist is right. As a result of the neoliberal "supply-side" policies embraced by both Reaganite Republicans and Clintonian Democrats, the US has lost much of its middle class—that bastion of democratic capitalism first created by FDR's New Deal which was not only a barrier to the spread of communism during the Cold War but formed the backbone of the post-WWII economic boom and "consumer society." With the fall of Soviet-style Communism and the demise of the Democratic Party's "Great Society" dream, which has been replaced by the so-called "Washington' consensus" crafted by the Bill Clinton Administration, differences in material well-being have recently become so egregious that many writers have begun to refer to our post-welfare-state era as the new Gilded Age. Globally, matters are becoming not that different from the middle of the 19th century—the "hard times" described by Charles Dickens and Emile Zola, especially in view of the social dislocations and hardships already inflicted by "globalization" and "tricke-down" economics. With the fall of Communism especially there is no need any more to bribe the working classes through welfare-state generosity.

Thanks to the globalization policies pursued and promoted by the champions of neoliberalism, much of the once unrivaled US manufacturing base has been moved offshore to take advantage of lower wages and laxer tax and environmental laws overseas. According to Dr. Paul Craig Roberts, a former Assistant Secretary of the US Treasury in the Reagan Administration, “The US has lost critical supply chains, industrial infrastructure, and the knowledge of skilled workers.” While this “off-shoring” (or “out-sourcing”) of American industry has brought about super-profits for multinational corporations and increased capital gains for equity owners, ordinary Americans have lost ground both financially and socially, as widespread unemployment, under-employment, job insecurity, and falling incomes have eroded their once enviable living standards, known as the “American Dream.” What is equally important from an economic point of view, their purchasing power has plummeted in this “race to the bottom,” reducing consumer demand for goods and services which cannot be made up for by the “conspicuous consumption” of the moneyed classes (to use here Thorstein Veblen’s old but apt phrase), especially when the so-called “1-percent” elite is fond of investing its money in China and India or depositing it in “tax havens” like the Cayman Islands or in secret Swiss bank accounts. As the middle class keeps losing jobs and income due to a capital flight abroad in search of lower taxes, looser regulations, and higher profits, consumer demand keeps plummeting in a national economy, over 70% of which derives from consumer spending. This is the inevitable consequence of setting up a globalized and highly competitive free market, where each year 4 million more cars are produced (and usually exported) than are actually sold. The sky-high wall of tariffs, import duties, and other protectionist barriers behind which America built its vaunted industry in the late 19th and early 20th centuries is all gone in the name of free trade, open borders, and globalization.

There are few protections left against the tidal wave of cheap foreign imports, mostly Chinese, that is flooding the American market. Many of the traditional tools to make up for the domestic lack of wage competitiveness in this “free-for-all,” WTO-ruled “brave new world” are no longer effective. For instance, the old Keynesianism of pre-”Washington Consensus” days used both fiscal steps (lower taxes and large federal budget deficits) and “easy” monetary measures (low interest rates, easily available credit, as well as a lot of money-printing) to spur demand for goods and services and thus stimulate economic growth and employment at home. The Administration of George W. Bush, for one, tried to boost economic demand by cutting taxes, especially for the upper income brackets, engaging in a military spending spree unprecedented in peacetime history, and also by spreading American homeownership through easy credit and seductively low mortgage rates. Encouraging debt was seen as a way out of the problem of stubbornly slow economic growth. The hitch was that many consumers were already overburdened with debt, so in the end many of them defaulted on their mortgages and the housing bubble eventually burst. As a result, the “too big to fail” banks and whole industries dependent on them for cheap loans were suddenly in trouble and the federal government had to bail them out (instead of rescuing many local governments which have also been up to their neck in debt).

Nor is the old policy of “military Keynesianism” sustainable any more given the tsunami-like size of future federal deficits. In 1946 President Truman and Republican Senator Arthur Vandenberg discussed in private the need for a massive military built-up against the “Soviet threat” to avoid the country relapsing into a new Great

Depression ("You'll need to scare the hell out of the American people to achieve that," demurred the Senator from California). But this year the size of the federal debt (over $16 trillion and counting) has surpassed the annual GNP, which in fiscal terms makes the US worse off than most of the debt-ridden and crisis-plagued European nations that are daily in the news. For the foreseeable future the federal government will continue to accumulate over a trillion dollars in debt each and every year ($1.1 trillion in the last fiscal year ending in September 2012 alone). That is why the idea of Dr. Paul Krugman (another Nobel Prize-winning economist) of the federal government spending $8-10 trillion over the next decade just to stimulate the economy and spur employment, even if implemented, is hardly practical as it could only sink the country into an even deeper sea of red. Even Dr. Stiglitz's much more modest idea for targeted federal investments to spur domestic demand and rebuild the country's crumbling infrastructure, could equally undermine the US credit rating and probably re-ignite inflation.

Paul Craig Roberts has suggested that the federal government may attempt to print its way out of the indebtedness quagmire but this is equally unrealistic. Printing huge amounts of new money could fatally undermine the value of the national currency at a time when many foreign governments, most notably the BRICS countries, are moving away from the US dollar in trade and are instead using their own currencies as well as the euro or the yuan, gold and silver, or even barter. This could threaten the long-term viability of the US dollar as the international reserve currency, as the rest of the world may eventually choose another reserve currency such as the Chinese yuan (the renminbi). But, as former Secretary of the Treasury and of State James Baker recently warned, if the US dollar loses its status as an international reserve currency, the U.S. will become just another Greece (that is, the country will be unable to pay its debts or even pay for vital imports).

Money-printing, which increases the volume of money and credit relative to available goods and services (or what economists call monetary inflation) may unleash destructive price inflation down the road which would certainly end the tenure of any incumbent administration that dares attempt it, if not endanger the entire political system itself (much as it doomed the post-WWI Weimar Republic). For once released, it may not be so easy to put the genie of inflation back into the bottle. To control price inflation resulting from increased demand for goods and services, higher taxes and high interest rates will have to be used to reduce disposable income and curtail consumer spending. Not only is higher taxation unrealistic in the current political climate, but such recessionary policies would only depress economic growth and increase unemployment, as happened in the early Reagan years. It could even usher in another Great Recession under the current unstable economic conditions. So, getting out of the indebtedness trap through "a little bit of inflation" (that is, reducing the real value of the national debt via price inflation), as some popular CNBC commentators have suggested, is a pipe dream, as it could only scare off potential investors and foreign creditors.

After the failure of QE1 and QE2 to provide momentum to the economic recovery, QE3, announced in September 2012, shifts the policy of the Federal Reserve from fighting inflation to battling high unemployment—an important admission of how intractable the problem of unemployment is—by nothing short of re-inflating the housing bubble, forcing people, especially seniors, to withdraw their bank savings due to the nearly negative interest rates, and plunging their life savings instead either into the stock market or into resurgent real estate. Not only is there a danger of disastrous recent history (the 2008 Great Recession) repeating itself, but it is also questionable if this risky plan would boost real economic growth and job-creation, since it stimulates real estate and stock market speculation far more than it does consumer demand. And if the re-inflated housing bubble were to burst once again, this time there will be very little money available for another massive bail-out given the surging mountain of government debt.

With the federal government borrowing four out of every ten dollars it spends today, the state of the national economy seems to be much more dire or even desperate than our politicians, including President Obama and Mitt Romney, are prepared to admit. Given the formidable array of financial and economic ills facing them and the severely limited options they have for dealing with them, it is unclear at this time if any remedy is at hand to avoid a double-dip recession, if not much worse. Pledging to create 12 million jobs over the next four years, while cutting everyone's taxes and slashing federal spending is hardly a serious election-time promise, let alone a workable plan for the future. Perhaps it is time for the practitioners of that "dismal science," the herd of economists that we see daily on TV news, to put their heads together and make sure that the proverbial light at the end of the tunnel does not turn out to be the oncoming train of economic collapse. For, if a new recession is now almost a certainty, one cannot dismiss out of hand the dark predictions for a second Great Depression, either.

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