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A debt culture gone awry

By Hamid Varzi

08/21/07 "IHT" -- -- -: August 17, 2007 --- - The U.S. economy, once the envy of the world, is now viewed across the globe with suspicion. America has become shackled by an immovable mountain of debt that endangers its prosperity and threatens to bring the rest of the world economy crashing down with it.

The ongoing sub-prime mortgage crisis, a result of irresponsible lending policies designed to generate commissions for unscrupulous brokers, presages far deeper problems in a U.S. economy that is beginning to resemble a giant smoke-and-mirrors Ponzi scheme. And this has not been lost on the rest of the world.

This new reality has had unfortunate side effects that go beyond economics. As a banker working in the heart of the Muslim world, I have been amazed by the depth and breadth of anti-Americanism, even among U.S. allies, manifested in reactions ranging from fierce anger to stoic fatalism. Muslims outside the United States interpret America's policies in the Middle East not as an effort to spread democracy but as a blatant neocolonialist attempt to solve its economic problems by force. Arabs and Persians alike argue that America's fiscal irresponsibility has forced the nation to seek solutions through military aggression.

Many believe that America's misguided adventure in Iraq was a desperate attempt to capture both a reliable source of cheap oil and a major export market for the United States.

The United States borrows a whopping \$2.5 billion daily from abroad to service its burgeoning debt. In order to continue borrowing at reasonable interest rates America needs to retain credibility with its overseas creditors, especially Far Eastern nations running huge trade surpluses. A cessation of foreign lending would force the Fed to raise interest rates to attract money, precipitating a collapse of the already weak housing market and pushing the economy into recession.

This is why the Chinese, in particular, have threatened to retaliate against proposed

U.S. trade sanctions by reducing their \$1.3 trillion in dollar holdings.

The U.S. debt situation is so grave that the Chinese would not even need to "dump dollars" to precipitate a meltdown but could simply refuse to extend further credit: They could cease purchasing additional Treasury Bonds and Treasury Bills, without selling any excess inventory. China has the far stronger hand, because a run on the dollar would merely reduce China's gigantic cash surplus while increasing America's debt burden to astronomical levels.

U.S. debt affects all nations, but in surprisingly different ways: Third world farmers suffer from the effects of gigantic U.S. farm subsidies aimed at reducing the trade deficit, while Russia has actually profited from America's lack of discipline.

Flush with funds generated from a decade of trade and account surpluses, Russia views U.S. sensitivity to its expansionist energy policy as a response to America's own failure to reduce energy waste and exploit alternative energy sources when it had the opportunity to do so. In sum, American economic decadence has become a source of Russian strength.

America's supply-side economists argue that there is nothing wrong with going into debt, but this is valid only as long as a nation and its consumers are gaining something in return.

What have Americans gained from their nation's mountain of debt? A crumbling infrastructure, a manufacturing base that has declined 60 percent since World War II, a rise in the wealth gap, the lowest consumer-savings rate since the depths of the Great Depression, 50 million Americans without health insurance, an educational system in decline and a shrinking dollar that makes foreign travel a luxury.

The best cars, the best bridges and highways, the fastest trains and the tallest buildings are all to be found outside America's borders. Supply-siders ignore the crucial distinction between, on the one hand, debt employed as an investment vehicle to enhance competitiveness and, on the other, debt used to pay off current expenses and to create even more debt.

The bottom line is that America is awash in red ink and seeks the wrong solutions to its debt problems. A return to fiscal responsibility would make America far stronger, both domestically and internationally, than would a continuation of current policies that falsely project strength through idle protectionist threats and failed military aggression.

Current tensions between the United States and the rest of the world will continue as long as America's military bark is louder than its economic bite.

A solution to the U.S. debt problem requires radical measures, including: the

elimination of corporate tax loopholes, a reversal of tax breaks for the ultra-rich, a bipartisan campaign to eliminate budget "pork," imposition of stringent limits on corporate debt and speculative lending, a vast reduction in military expenditure and, finally, an additional 50 cent per gallon gasoline tax that would slash the federal deficit, curtail energy waste and spur technological breakthroughs.

Let us hope America heeds the warnings, dispenses with junk-food economics and embraces a crucial diet of fiscal discipline. It remains to be seen, however, whether America's political leaders have the courage to instigate such reforms, and whether Congress is finally willing to do something for the future of ordinary, hard-working Americans.

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