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HURRICANE KATRINA: THE STORM AND THE METAPHOR

Shelter anyone?

We're not prepared for an economic hurricane either

By Alan Tonelson, a research fellow at the U.S. Business and Industry Council Educational Foundation and the author of "The Race to the Bottom"

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AS ITS BROKEN LEVEES AND drowned pumping systems made so painfully clear, if the Big One was widely predicted in New Orleans, it was never genuinely feared. After Hurricanes Katrina and Rita, disaster preparedness and prevention are no longer completely academic subjects.

If only such realism could be injected into U.S. policymaking before a widely predicted economic disaster finally strikes.

Hurricane-force winds of overspending are building storm surges of debt that tower over the levees and pumps available to American leaders. These mounting imbalances could wash over the economy and leave America and the world submerged in a deep, long-term downturn.

This building economic storm has generated at most pro forma acknowledgments. Even worse, discussing crucial international

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dimensions of the looming emergency is usually considered taboo, even though numerous, ongoing policy mistakes on this front have heightened America's and the world's vulnerability.

Ironically, these failures were showcased in the most prominent way possible just before Katrina, when key global economic aristocrats gathered for an annual gabfest in Jackson Hole, Wyo.

Beneath the Tetons, bankers, policy experts, finance whizzes and academic gurus alternated fly-fishing outings and nature hikes with sweeping discussions, such as "The Greenspan Era: Lessons for the Future." The subtext of the discussion: Has the U.S. economy become a bubble inflated by investors and consumers who have totally forgotten the concept of risk? And have Alan Greenspan's policies encouraged these excesses?

Upon returning to the real world, however, these folks disregarded any eloquently voiced concerns. They simply refused to acknowledge that specific U.S. foreign economic policies are inexorably widening the gap between the nation's desires and its ability to pay for them responsibly.

America's dangerously weak finances stem partly from the public's ravenous appetite for material goods and government services, combined with a bipartisan determination in Washington to feed them. The world's willingness to keep showering an overstretched America with cheap credit has been central as well.

Flip side: Inadequate income

However, the flip side of overspending is under-earning, i.e., inadequate income. And whether the problem is domestic wage stagnation or lagging exports, a major contributor has been a national trade strategy that tends to be championed by business and policy elites.

Inflation-adjusted median wages today have fallen back to 1967 levels, according to Department of Labor statistics. The only way for the typical American family to maintain its living standards has been to spend down its savings, double its outstanding household debt since 1992 (after adjusting for inflation), according to The Wall Street Journal, and often send a second wage earner into the workforce.

Surely at least some blame belongs with globalization policies that have resulted in the outsourcing of millions of the nation's best-paying jobs and job opportunities, and that have directly or indirectly exposed most other workers to the undertow of the "China price."

Similarly, record U.S. trade deficits cannot reasonably be divorced from 15 years of trade accords that have focused tightly on countries and regions either too poor or too broke to buy from Americans anything close to what they sell, or too mercantilist to seek such balance. A prime example is the new, narrowly approved Central America Free Trade Agreement, which targeted six economies whose markets combined only barely exceed that of New Haven, Conn. Even expanded trade with China has locked the U.S. in an embrace with a country whose production and exports will greatly exceed its consumption and imports for decades.

The establishment, however, strives to marginalize fundamental criticisms of these trade policies for two main reasons. First, it fears that admitting fault with today's trade policies will undercut free markets and capitalism around the world.

These leaders evidently have forgotten that domestic policy interventions have been widely accepted throughout the industrialized world for decades. They saved the essence of capitalism from the Depression and have buttressed free markets ever since. Moreover, since 1945, the principle of national interventions in international economic flows has been accepted as well, though mainly in currency management.

Given the failure of exchange-rate policies to even slow the growth of today's global imbalances, why should skillful, well-timed interventions in trade flows designed to restore macroeconomic balance--as opposed to safeguards restricted to specific industries--be so verboten? They are more likely to leave capitalism healthier than the prolonged worldwide slump whose odds the aristocracy itself believes are growing.

The second, and probably more important, reason for clinging to today's trade policies is political. Change would undermine the highly profitable, outsourcing-focused business models adopted by the U.S. multinational companies that dominate U.S. policymaking through their generous contributions to politicians, think tanks and universities.

The idea has been to produce goods in very low-cost countries but still sell most of them in high-cost countries--especially the U.S.--where the vast bulk of the world's purchasing power can still be found.

Recent research from consulting firm McKinsey & Co. shows just how thoroughly this strategy has turned U.S. multinational companies into super-importers. So proficient have they become at supplying America

from abroad that the share of the U.S. trade deficit produced by their operations jumped from single digits in 1995 to more than one-third in 2002. This figure has undoubtedly climbed higher as they have sent ever more export-oriented investment into the developing world.

Growing agreement that these deficits are unsustainable means that these business models will ultimately backfire on the multinationals themselves. Not even these firms will remain profitable if their American customers run out of credit.

As the trade deficits show, the emerging markets they tout so energetically won't even begin to substitute. Tragically, the American financial system creates few incentives for them to look beyond the next quarter, so they keep on pressing for new, CAFTA-like trade agreements to expand their outsourcing options and lower their costs--and Americans' earnings opportunities--still further.

Surcharge on imports?

To avert this economic disaster, the U.S. Business and Industry Council has drafted an omnibus trade bill that includes a temporary surcharge on imports until America's trade deficits and resulting debts are brought under control.

Much of the economic establishment will reflexively vilify such measures as protectionism. But if the economic elite can offer alternatives that have not already failed, Americans need to hear them now, so that a genuine national debate on the emergency can finally begin.

Containing today's likeliest economic disasters is even more important than preventing or containing natural disasters. An economic hurricane like the one gathering strength could flatten the world economy, not just local or regional economies. And unlike imminent natural disasters, economic disasters are directly strengthened by each new policy mistake and the excesses it breeds.

As widely observed but clearly not genuinely believed the larger a bubble becomes, the more destructive its bursting.

The resulting political storm will dwarf the ongoing post-Katrina finger-pointing because Mother Nature will be completely off the hook.

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