ISSUES ’08: ‘THE SITUATION’
By Michael Ventura
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On Oct. 29, 2004, days before our last presidential election, this column ran with the headline, “Welcome to the Situation.” After huffing and puffing about the inability and/or unwillingness of the candidates to discuss the capital-S Situation frankly, I defined the Situation thus: “The great days of the United States of America are over.”

It was a sloppy use of the word “great.” By great, in that sentence, I meant powerful and rich. What could I have been thinking? On any more-or-less sane day I know power and riches are not necessary for greatness. The blacks and Creoles of New Orleans were neither powerful nor rich when they invented jazz, nor were the Wright Brothers when they gave us flight, nor was Italy when it produced the cinema of Federico Fellini, Roberto Rossellini, Michelangelo Antonioni, and Luchino Visconti. For that matter, America wasn’t powerful and rich when it created its Constitution. Examples abound. America can be great without being powerful and rich. But to get on with the Situation, in 2004 I defined it like this:

“China has become a manufacturing colossus while our factories are gone or going… China invests vast sums... in its infrastructure… from cultural and educational institutions to grand construction projects; we’re spending comparable sums futilely in Iraq, while our infrastructure… crumbles. We’re fighting for oil in the Middle East; China is in negotiation with Russia to have oil piped through its backdoor – while, through its front door, it has a sweet deal with Australia for natural gas (while we spend millions “defending” Australia against – China!)… As to our heavily indebted federal government, its solvency is now supported mostly by Asians buying our bonds. Why do they buy our bonds? Because the American consumer is still the engine of world prosperity. How is this possible? Because of credit cards and the like [“the like” being mortgage refinancing, etc.]. Without the American way of credit, we’d be in a depression. The paramount fact: The United States… is now important economically *only* because of its citizens’ consumption. That consumption is fated to decline, while in the near future… China will prosper enough for its 1.3 billion citizens to become significant consumers… When that happens, China and Southern Asia [India, etc.] can support their own growth and will have no more use for us. Then they need not defeat us militarily. They have merely to stop buying our bonds. Or even threaten to stop… *That* is the Situation.”

Fast forward to the present. You don’t need a rehash of our economic morasses to know the shape we’re in; you just need to buy groceries, pump gas, or try to get a loan. Meanwhile, the Situation is upon us, and the Chinese don’t need us anymore. “Chinese retail sales rose 22 percent in April [!], an indication that domestic demand is offsetting the effect of declining exports [to the U.S.]… It was the fastest rise since the government

started gathering monthly data (*New York Times*, May 14, p.C9)." Says Robert Rubin, former U.S. Treasury Secretary, "My impression is that China and India both have sufficient domestic-led growth to continue to have vibrant growth even if the U.S. has a sustained period of difficulty" (*Newsweek*, June 16, p.21).

And now that they don't need us, what's happening? "India's foreign ministry says the U.S. dollar will no longer be accepted at the Taj Mahal" (CNN, Jan. 4). That's because "since 2002, the dollar has fallen by 25% against the currencies of its major trading partners… a further decline of the dollar is likely, especially against key Asian currencies" (*USA Today*, July 23, p.B3). And, because of that, foreign capital has been fleeing U.S. markets for the past year; in a report on CNBC's Power Lunch, March 4, no one consulted has ever seen anything like it. (Capital-flight? From the U.S.A.? Doesn't that only happen in the troubled Third World?) And "foreign investors are losing their appetite for U.S. bonds. Foreigners represented only 5.8 percent of bidders at [a March] auction, down from an average 25 percent" (*The Week*, March 28, p.40, quoting the *London Daily Telegraph*). That's big trouble because "the bare facts are that the nation – heavily indebted – needs to attract some $800 billion a year abroad, either by borrowing the money or by selling American assets. No serious analyst believes that an imbalance of that magnitude is sustainable" (*New York Times*, Aug. 19, 2007, p.WK9).

The Chinese, our principle bankers, don't believe it either. "China Less Willing to Be America's Piggy Bank," headlined a *New York Times* story on Dec. 22, 2007 (p.C3): "For the last three years, China has been the financier that kept the American government well funded… But… China reversed course in 2007 and has become a net seller of Treasury securities." You'll notice that since China "reversed course," our economy has gotten shakier and shakier.

After I wrote "Welcome to the Situation" in 2004, I received a hand-written letter in excellent English from a Chinese student in Beijing accusing me of being anti-Chinese. (They read the Chronicle in Beijing?! Guess so.) If I were Chinese and wrote as freely as I do, I'd be imprisoned; so – there's that. Aside from that, I'm not anti-Chinese. I'm merely assembling the facts as accurately as I'm able. To wit, *The Economist*, May 17, p.89:

"The credit crisis has cooled Asia's ardour toward Western banks… A senior Chinese regulator recently described to this newspaper his view of big global investment banks in one unusually graphic word: 'shit.' … [And] Jiang Jianquing, chairman of Industrial and Commercial Bank of China, the world's most valuable bank, recently talked down the merits of investment in American bonds and banks."

Nor am I anti *The Economist*, probably the most respected Western news magazine in the world, but even I was surprised when they led off an editorial with "Time to Break Free – The Middle East's oil exporters should end their currencies' peg to the dollar" (Nov. 24, 2007, p.18). *The Economist* is a financially conservative, socially mainstream British outfit, so traditional that, in 19th Century fashion, articles are rarely signed. Take it from a journalist, they don't lead an editorial that radically unless they're repeating the

undercurrent of talk in their very well connected circles. On July 19 (p.15) they lead an editorial with, "It was another one of those frantic weeks that were never meant to happen in the world's most advanced economy [meaning the U.S.]." You need a little familiarity with posh English humor to get that as scathing sarcasm. Even so, I wasn't prepared for the last line of a major article in that issue , chillingly titled "End of Illusions" (p.79): "Perhaps it is no surprise that traders in the credit-swaps market have recently made bets on the unthinkable: that America may default on its debt."

Again, take it from a journalist: An outfit like *The Economist* doesn't pull a sentence like that out of thin air -- nor would they give it starring position as the article's finale -- unless privy to serious off-the-record talk that America might, just *might*, default.

And: "The F.D.I.C. said the combined profit of the financial institutions it regulates plunged 46 percent… during the first three months of the year" (*New York Times*, May 30, p.C6). "The American economy has shed jobs in each of the first six months of the year" (*The Economist*, July 12, p.17). "Blue-chip stocks down 21.2% in past year. Wholesale prices have risen 9.2% since June 2007. U.S. Dollar down 13.2% vs. euro during past year. Foreclosures up 53% since this time last year" (*USA Today*, July 16, p.1). While our numbers are down, "China's GDP rose by an estimated 10.1% in the second quarter" (*The Economist*, July 19, p.105). And there's this: "Perhaps more than 50% of American currency reside outside the U.S." (CNBC, Kudlow and Company, Aug. 22, 2007), and "the 50 biggest stocks in the U.S. have half their earnings abroad' (CNBC, Street Signs, Aug. 23, 2007) – meaning we have no control over our currency and our biggest corporations stay solvent only by investing abroad, while our financial institutions have lost almost half their value (some have lost much more). "Foreigners must purchase more than $3 billion every business day to fund the [U.S.] imbalance… The loss of the dollar's purchasing power and international respect has some experts worrying that the euro might replace the dollar as the so-called primary currency… a withdrawal [from the dollar] could have enormous consequences" (AP online, July 6).

Fortunately for us, greatness does not require that one be rich and powerful, only that one be creative and have strength of character. Ready?

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