US treasury secretary touts Obama austerity policies in China visit

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The two-day visit by US Treasury Secretary Timothy Geithner to China sheds light on the historic decline in the global position of American capitalism as well as the austerity policies being mapped out by the Obama administration to impose the full burden of the economic crisis on the American working class.

Geithner's visit follows calls by Beijing to end the dollar's role as the world reserve and trading currency and replace it with a basket of major currencies, and hints that China might scale back its purchases of US Treasury notes. Geithner's main objective in talks with top Chinese officials is to reassure Beijing that the Obama administration will safeguard China's holdings of US debt by bringing down the federal budget deficit and phasing out the current policy of flooding the financial markets with dollars.

As Geithner suggested in a speech Monday at Peking University and in public statements, the US administration's strategy is to slash social spending and permanently reduce so-called "discretionary spending" by the American people once the banking system has been restabilized through the injection of trillions of dollars in public funds.

This is meant to reassure the Chinese that their vast dollar holdings—$1.45 trillion in US denominated assets, including $768 billion in Treasury securities—will not plunge in value as a result of rising interest rates and a sharp fall in the value of the dollar. China is now the biggest purchaser of US government debt, and the functioning of the massively indebted American economy has become dependent on China's continued recyling of its export earnings, largely dependent on the US market, to provide loans to the US government.

Geithner's visit has taken on a crisis dimension following US congressional projections of a record US budget deficit of $1.75 trillion for the fiscal year ending September 30. This is four times the $455 billion shortfall for 2008, and equivalent to 12.9 percent of US gross domestic product (GDP).

The exploding US deficit and massive debt taken on by the Federal Reserve Board have driven down the value of the dollar in recent weeks and heightened concerns on world markets about the stability of the dollar and the credit-worthiness of US Treasuries, causing a sharp rise in long-term US interest rates. This has the effect of eroding the value of Chinese dollar holdings. The market value of Chinese holdings in Treasury notes has already declined 5 percent this year.

Geithner's trip provides the spectacle of the US being compelled to pledge the same sort of austerity policies that the US routinely demanded in past years of bankrupt lesser powers. Now it is the US government that must pledge to slash the living standards of its population in order to salvage its currency and protect the interests of its financial elite.

The very fact that China has publicly raised the question of the privileged role of the US dollar is a sign of the economic decline of the United States. It marks the first time in the post-war period that the dominant role of the dollar has been challenged by a major economic power.

En route to Beijing, Geithner sounded the main theme of his trip, telling reporters, "No one is more concerned about future deficits than we are."

In his speech at Peking University, he said, "We are going to have to bring our fiscal deficit down to a level that is sustainable over the medium term. This will mean bringing the imbalance between our fiscal resources and expenditures down to the point—roughly three percent of GDP—where the overall level of public debt to GDP is definitively on a downward path."

He continued: "The temporary investments and tax incentives we put in place in the Recovery Act to strengthen private demand will have to fall back to a more modest level relative to GDP, and we will have to be very disciplined in limiting future commitments through the reintroduction of budget disciplines, such as pay-as-you-go rules....

"Let me be clear—the United States is committed to a strong and stable international financial system. The Obama administration fully recognizes that the United States has a

special responsibility to play in this regard, and we fully appreciate that exercising this special responsibility begins at home."

Geithner made clear that this will entail a permanent reduction in the consumption level of the American people—that is, a sharp fall in their living standards. While asserting that an economic recovery was on the way, Geither indicated that it would not be a recovery in general living standards, but rather a protracted period of high unemployment and lower public consumption. He alluded obliquely to that day's bankruptcy filing by General Motors and said there would be more plant closings and layoffs.

"Consumer spending in the United States will be restrained for some time relative to what is typically the case in recoveries," he said, adding, "These are necessary adjustments. They will entail a longer, slower process of recovery, with a very different pattern of future growth across countries than we have seen in the past several recoveries....

"In the United States, saving rates will have to increase, and the purchases of US consumers cannot be as dominant a driver of growth as they have been in the past."

As a result, Geithner stressed, China would have to revamp its economy to drive up domestic consumption and make it less dependent on exports. Although he did not spell it out, the US has a vested interest in such a development. Under conditions of a protracted reduction in exports to the US and other countries, the ability of China to continue to subsidize the US economy is dependent on its ability to generate profits internally.

As an inducement, Geithner pledged that the US would avoid protectionist measures and champion a larger role for China in international policy-making bodies such as the International Monetary Fund.

In return, he called on China to provide the US with "increased opportunities to export to and invest in the Chinese economy." Geithner gingerly raised the contentious issue of the valuation of the Chinese currency, the yuan. US corporations and their mouthpieces in Congress have for years denounced China for holding down the value of the yuan in order to promote Chinese exports, and Geither himself, at a Senate confirmation hearing only two days after Obama's inauguration last January, accused China of manipulating its currency—a charge that carried with it an implicit threat of trade and currency retaliation.

That threat was quickly dropped when it became apparent the US would be even more dependent on Chinese capital as it expanded its bailout of Wall Street and pumped ever-greater amounts of credit into frozen markets. Last February, when Secretary of State Hillary Clinton visited China on her first overseas tour, she dropped the currency charge and instead made an explicit plea for China to continue buying US Treasuries. Geithner is following suit in his visit, playing down the currency issue and stressing US-China "partnership."

Geithner's visit follows a series of trips by US politicians to Beijing over the past week, including House Speaker Nancy Pelosi, Chairman of the Senate Foreign Relations Committee John Kerry and the Democratic and Republican co-chairs of the US-China Working Group in the House of Representatives.

Geithner is to meet Tuesday with Chinese President Hu Jintao, Premier Wen Jiabao and Vice Premier Wang Qishan. The Chinese, for their part, are making demands in return for keeping up their purchases of US Treasuries, including an end to restrictions on US high-tech exports to China and greater access for Chinese capital in US markets.

Behind the diplomatic niceties, tensions between the two countries are intensifying. China is in considerable crisis over the size of its US holdings. The regime is facing growing popular discontent over its subsidies to the US under conditions of plant closures and the destruction of more than 26 million jobs of migrant workers, and growing calls from economists for a more aggressive policy to reduce its US holdings.

China Daily on May 31 cited Wang Jian, secretary-general of the China Society of Macroeconomics, as saying, "Prospects for the US dollar and US Treasuries do not look good at the moment, and even worse in the long run."

However, any precipitous reduction in Beijing's US Treasury purchases runs the risk of provoking a dollar panic, massive losses in Chinese dollar holdings and a collapse of its main export market, the United States.

China protested "buy American" provisions of the Obama administration's stimulus package, and Geithner is expected to raise in his talks with Chinese officials the funneling of that country's stimulus spending into "buy China" projects.

Relations have been further strained by Beijing's moves to assert the role of the yuan in international trade to the detriment of the dollar. China is forging currency swaps with Asian and Latin American nations to enable those countries to bypass the dollar in trade with Beijing.