The Vicious Circle of Debt and Depression – It Is a Class War

BY ISMAEL HOSSEIN-ZADEH

Never before has so much debt been imposed on so many people by so few financial operatives—operatives who work from Wall Street, the largest casino in history, and a handful of its junior counterparts around the world, especially Europe.

External sovereign debt, as well as occasional default on such debt, is not unprecedented [1]. What is rather unique in the case of the current global sovereign debt is that it is largely private debt billed as public debt; that is, debt that was accumulated by financial speculators and, then, offloaded onto governments to be paid by taxpayers as national debt. Having thus bailed out the insolvent banksters, many governments have now become insolvent or nearly insolvent themselves, and are asking the public to skimp on their bread and butter in order to service the debt that is not their responsibility.

After transferring trillions of dollars of bad debt or toxic assets from the books of financial speculators to those of governments, global financial moguls, their representatives in the State apparatus and corporate media are now blaming social spending (in effect, the people) as responsible for debt and deficit!

President Obama's recent motto of "fiscal responsibility" and his frequent grumbles about "out of control government spending" are reflections of this insidious strategy of blaming victims for the crimes of perpetrators. They also reflect the fact that the powerful financial interests that received trillions of taxpayers' dollars, which saved them from bankruptcy, are now dictating debt-collecting strategies through which governments can recoup those dollars from taxpayers. In effect, governments and multilateral institutions such as the IMF are acting as bailiffs or tax collectors on behalf of banksters and other financial wizards.

Not only is this unfair (it is, indeed, tantamount to robbery, and therefore criminal), it is also recessionary as it can increase unemployment and undermine economic growth. It is reminiscent of President Herbert Hoover's notorious economic policy of cutting spending during a recession, a contractionary fiscal policy that is bound to worsen the recession. It is, indeed, a recipe for a vicious circle of debt and depression: as spending is cut to pay debt, the economy and (therefore) tax revenues will shrink, which would then increase debt and deficit, and call for more spending cuts!

Spending on national infrastructure, both physical (such as roads and schools) and social infrastructure (such as health and education) is key to the long-term socioeconomic developments. Cutting public spending to pay for the sins of Wall Street gamblers is bound to undermine the long-term health of a society in terms of productivity enhancement and sustained growth.

But the powerful financial interests and their debt collectors seem to be more interested in collecting debt claims than investing in economic recovery, job creation or long-term socioeconomic development. Like most debt-collecting agencies, the IMF and the states serving as banksters' bailiffs through their austerity programs may shed a few crocodile tears in sympathy with the victims' of their belt-tightening policies; but, again like any other debt-collecting agents, they seem to be saying: "sorry for the loss of your job or your house, but debt must be collected—regardless"!

A most outrageous aspect of the debt burden that is placed on the taxpayers' shoulders since 2008 is that most of the underlying debt claims are fictitious and illegitimate: they are largely due to manipulated asset price bubbles, dubious or illegal financial speculations, and scandalous conversion of financial gamblers' losses into public liability.

As noted earlier, onerous austerity measures to force the public to pay the largely fraudulent external debt is not new. Benignly calling such oppressive measures "Structural Adjustment Programs," the International Monetary Fund and the World Bank have for decades imposed them on many less developed countries to collect debt on behalf of international financial titans.

To "help" the indebted nations craft debt-servicing arrangements with external creditors, the IMF imposed severe conditions on the way they managed their economies—just as it is now imposing (in collaboration with the European and American bankers) those austerity policies on the debtor nations in Europe. The primary purpose of such restrictive conditions is to divert or transfer national resources from domestic use to external creditors. These include not only belt-tightening measures to cut social spending and/or raise taxes, but also selling-off public enterprises, national industries, and future tax revenues.

Calling such fire-sale privatization deals "briberization," the ex-World Bank chief economist Joseph Stiglitz revealed (in an interview with the renowned investigative reporter Greg Palast) how finance ministers and other bureaucratic authorities in the debtor countries often carried out the Bank's demand to sell off their electricity, water, transportation and communication companies in return for some apparently irresistible sweetener. "You could see their eyes widen" at the prospect of 10% commissions paid to Swiss bank accounts for simply shaving a few billions off the sale price of national assets [2].

The IMF/World Bank/WTO "structural adjustment programs" also include neoliberal policies of "capital-market liberalization." In theory, capital market deregulation is supposed to lead to the inflow and investment of foreign capital, thereby bringing about industrialization, job creation and economic expansion. In practice, however, financial liberalization often leads to more capital outflow (or capital flight) than inflow. To the extent that there is an inflow of capital it is not so much productive or industrial capital as it is unproductive or speculative capital (also known as "hot money"): massive amounts of capital that is constantly in transit across international borders in pursuit of real estate, currency, or interest rate speculation.

To attract foreign capital to the relatively vulnerable markets of debtor nations, the IMF frequently recommends drastic increases in interest rate. Higher interest rates are, however, both anti-developmental and detrimental to the goal of debt servicing. Higher interest rates tend to destroy property values, divert financial resources away from productive investment, and increase the burden of debt servicing.

For example, in the Philippines, which in 1980 adopted the IMF's Structural Adjustment Program, "Interest payments as a percentage of total government expenditures went from 7 percent in 1980 to 28 percent in 1994. Capital expenditures, on the other hand, plunged from 26 percent to 16 percent." By contrast, "the Philippines' Southeast Asian neighbors ignored the IMF's prescriptions. They limited debt servicing while ramping up government capital expenditures in support of growth. Not surprisingly, they grew by 6 to 10 percent from 1985 to 1995. . .while the Philippines barely grew and gained the reputation of a depressed market that repelled investors" [3].

A major condition of the IMF/World Bank/WTO's "restructuring program" is trade liberalization. Free trade has always been the bible of the economically strong, self-righteously preached to the weak. It enables the strong to use their market power for economic gains, thereby perpetuating an international division of labor in which the technologically advanced countries would specialize in the production and export of high-tech, high-value added products while less developed countries would be condemned to the supply of less- or un-processed products. It is not surprising, then, that such a lop-sided policy of trade liberalization is sometimes called "free trade imperialism."

Taking advantage of the so-called Third World debt crisis, the IMF, World Bank and WTO imposed free trade and other "adjustment programs" on 70 developing countries in the course of the 1980s and 1990s. "Because of this trade liberalization," points out Walden Bello, member of the Philippines House of Representatives and president of the Freedom from Debt Coalition, "gains in economic growth and poverty reduction posted by developing countries in the 1960s and 1970s had disappeared by the 1980s and 1990s. In practically all structurally adjusted countries, trade liberalization wiped out huge swathes of industry, and countries enjoying a surplus in agricultural trade became deficit countries." Bello further points out, "The number of poor increased in Latin America and the Caribbean, Central and Eastern Europe, the Arab states, and sub-Saharan Africa." By contrast, in China and East Asia, where the neoliberal free trade and other Structural Adjustment Programs were rejected, significant economic development and considerable poverty reduction took place [3].

The attitude of the international financial parasites and their collection agencies such as the IMF regarding the disastrous consequences of their "restructuring" conditions is instructive.
An IMF official was quoted as acknowledging that the Fund's austerity packages have often led to debt-collection without economic growth. But he added: "the Fund is a firefighter not a carpenter, and you cannot expect the firefighter to rebuild the house as well as put out the fire." Obviously, what the "firefighter" tries to save from burning are external debt claims, not the economies or livelihoods of the indebted.

Another component of the IMF/World Bank's "adjustment program" to service external debt is called elimination of "price distortions," or establishment of "market-based pricing." These are fancy, obfuscationist terms for raising prices on essential needs such as food, water and utilities. They also include elimination of subsidies on healthcare, education, transportation, housing, and the like; as well as curtailment of wages and benefits for the working class. In essence, these are roundabout ways of taxing the poor to pay the rich, the creditors.

Where such belt-tightening measures have made living conditions for the people intolerable, they have triggered what has come to be known as “the IMF riots.” The IMF riots are “painfully predictable. When a nation is, ‘down and out, [the IMF] takes advantage and squeezes the last pound of blood out of them. They turn up the heat until, finally, the whole cauldron blows up,’ as when the IMF eliminated food and fuel subsidies for the poor in Indonesia in 1998. Indonesia exploded into riots. . . ” [2]. Other examples of the IMF riots include the Bolivian riots over the rise in water prices and the riots in Ecuador over the rise in cooking gas prices. As the IMF/World Bank riots create an insecure or uncertain economic environment, they often lead to a vicious circle of capital flight, deindustrialization, unemployment, and socio-economic disintegration.

Only when the riots have tended to lead to revolutions, the parasitic mega banks and their debt-collecting bailiffs, the IMF and/or the World Bank, have been forced to accept less onerous debt-servicing conditions, or even debt repudiation. The Argentine people deserve credit for having set a good example of this kind of debt restructuring.

In late 2001 and early 2002, they took to the streets to protest the escalated austerity measures imposed on them at the behest of the IMF and the World Bank. “Political demonstrations and the looting of grocery stores quickly spread across the country. . . . The government declared a state of siege, but police often stood by and watched the looting ‘with their hands behind their backs.’ There was little the government could do. Within a day after the demonstrations began, principal economic minister Domingo Cavallo had resigned; a few days later, President Fernando de la Rua stepped down. . . . In the wake of the resignations, a hastily assembled interim government immediately defaulted on $155 billion of Argentina's foreign debt, the largest debt default in history” [4].

Argentina also freed its currency (peso) from the US dollar (it had been pegged to dollar in 1991). After defaulting on its external debt and dropping its currency peg to the dollar, Argentina has enjoyed a most robust economic growth in the world. Debt re-structuring a la Argentina, that is, debt repudiation, is what today’s debt-strapped nations in Europe and elsewhere need to do to free themselves from the shackles of debt peonage.

Having subjected many nations in the less-developed countries of the South to their notorious austerity measures, international knights of finance are now busy applying those impoverishing measures to the more developed countries of the North, especially those of Europe. For example, the Greek government has in recent months announced a series of wage and benefit cuts for public workers, a three-year freeze on pensions and a second increase this year in sales taxes, as well as in the price of fuel, alcohol and tobacco in return for a bailout plan promised by the IMF and the European Central Bank.

Debt collectors’ austerity requirements in a number of East European countries (such as Latvia and Lithuania) have been even more draconian. Thomas Landon Jr. of *The New York Times* recently reported that, threatened with bankruptcy, “Lithuania cut public spending by 30 percent — including slashing public sector wages 20 to 30 percent and reducing pensions by as much as 11 percent. . . . And the government didn’t stop there. It raised taxes on a wide variety of goods, like pharmaceutical products and alcohol. Corporate taxes rose to 20 percent, from 15 percent. The value-added tax rose to 21 percent, from 18 percent" (April 1, 2010).

As these oppressive measures led to the transfer of nine percent of gross domestic product (euphemistically called "national savings") from domestic needs to debt collectors, they also further aggravated the economic crisis: "Unemployment jumped to a high of 14 percent, from single digits — and an already wobbly economy shrank 15 percent last year" [Ibid.].

In Latvia, another victim of the predatory global finance, the recessionary consequences of creditor-imposed austerity measures have been even more devastating: "Latvia has experienced the worst two-year economic downturn on record, losing more than 25% of GDP. It is projected to shrink further during the first half of this year. . . . With 22% unemployment . . . and cuts to education funding that will cause long-term damage, the social costs of this trajectory are also high" [5].

While the debt crises of the weaker European economies such as Greece, Latvia, Lithuania, Spain, Portugal and Ireland have reached critical stages of sustainability, the relatively stronger economies of Germany, France, and UK are also in danger of debt and deficit crises. Indeed, according to a recent IMF estimate, even in the more advanced economies of Europe the debt-to-GDP ratio will soon rise to an average of 100% [6].

Of course, the United States is also burdened by a mountain of debt that is fast approaching the size of its gross domestic product (of nearly $13.5 trillion). A major difference between the United States and other indebted nations is that the US is not as much at the mercy of its creditors or the IMF as are other debtor nations. Therefore, it can reasonably be argued that, on the basis of national or public interests, it could embark on an expansive fiscal policy, that is, a more aggressive stimulus package, that would take advantage of the power of "government as the employer of last resort," more or less as FDR did, thereby creating jobs, incomes and economic growth. This would also add to government's tax collection and reduce its debt and deficit.

Judging by the record, as well the budgetary projections, of the Obama administration and the lobby-infested Congress, however, such an expansionary fiscal policy seems very unlikely. Not only has the bulk of the government's anti-recession assistance been devoted to the rescue of the Wall Street gamblers, but also the relatively small stimulus spending has largely been funneled into the pockets of the private/financial sector—through wasteful and ineffectual programs such as "cash for clunkers," tax credit for new homebuyers, tax incentives for employers to hire, and the like. This stands in sharp contrast to what FDR did in the earlier years of the Great Depression: creating jobs and incomes directly and immediately by the government itself.

Not only is the administration's feeble stimulus package soon coming to an end, but the government also recently imposed a three-year spending freeze on all public outlays except for military spending and the so-called entitlements. As their tax revenues, along with their traditional shares of federal assistance, are dwindling many states (especially California, Florida, New York, Arizona, Nevada and New Jersey) are facing serious financial difficulties. And as they curtail or shut down essential services at the libraries, museums, parks, schools, art centers, and hospitals, and give pink slips to their employees, the recessionary conditions are bound to exacerbate.

The wrenching economic hardship in the debt-ridden countries is not so much due to insufficient or lack of resources as it is the result of the lopsided and cruel distribution of those resources. It is increasingly becoming clear that the working majority around the world face a common enemy: an unproductive financial oligarchy that, like parasites, sucks the economic blood out of the working people, simply by trading and/or betting on claims of ownership.

Rectification of this unsavory situation poses stark alternatives: either the powerful financial interests, using the state power, succeed in collecting their debt claims by impoverishing the public; or the public will get tired of the vicious cycle of debt and depression, and will rise in protest—akin to the "IMF riots" in Argentina—to repudiate the largely fictitious and illegitimate debt. This is of course a class war. The real question is when the working people and other victims of the unjust debt burden will grasp the gravity of this challenge, and rise to the critical task of breaking free from the shackles of debt and depression.

While repudiation may cleanse the current toxic debt off the economies of the indebted societies, it would not prevent its recurrence in the future. To fend off such recurrences, it is also necessary to nationalize the banks and other financial intermediaries. It only stands to reason that national savings be placed under democratically controlled public management – not unelected, profit-driven private banks.

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[1] For a comprehensive account of the history of sovereign debt crises and/or defaults see, for example, Carmen M. Reinhart and Kenneth S. Rogoff, *This Time is Different: Eight Centuries of Financial Folly*. Princeton, NJ: Princeton University Press, 2009.

[2] Greg Palast, "The Globalizer Who Came In From the Cold," *gregpalast.com*, October 10, 2001.

[3] Walden Bello, "The Poverty Trip – Is Corruption the Cause," *Counter Punch*, April 30 – May 2, 2010.

[4] Arthur McEwan, "Economic Debacle in Argentina—The IMF Strikes Again," *Dollars & Sense*, March-April 2002.

[5] Mark Weisbrot, "Baltic Countries Show What Greece May Look Forward to If It Follows EC/IMF Advice," *The Guardian Unlimited*, April 28, 2010.

[6] Nouriel Roubini, "The Debt Death Trap," *Project Syndicate*, April 16, 2010.