THE CHINESE PIPER?

The U.S. should not be in hock to another country, but we cannot entirely blame China, and in the short run there is no way out.*

by Steven G. Livingston

China purchased some $500 billion of U.S. bonds and assets last year alone. Is it the piper that will soon call the tune? China's recent warning to the U.S. Treasury was a wake-up call as well as a demonstration of some new realities.

The United States has racked up an eye-popping amount of debt. The government is the problem, yes. The federal budget deficit in 2008 alone was $455 billion. But average Americans are the problem, too. Our national savings rate has hit historic lows. The inability of Americans to save shows up in the balance of payments. This balance measures how much we buy (imports) versus how much we sell (exports). In 2008, our trade deficit—imports over exports—approached $600 billion. The order of the day seems to be not "buy American" but "buy everything!"

Who finances all this debt? Who is America's banker? Try China, among others. In effect, they loan us the money to keep spending. Of course they do want this money back—and with interest, please.

Now, we can blame the Chinese for this. They manipulate their currency, aid their exports, and are too tolerant of pirated American goods. But, quite frankly, that is too easy. America runs a trade deficit with just about everybody. If China didn't exist, we would only be buying, and borrowing, from someone else. Remember the Japan-bashing of 20 years ago? The Chinese don't force our government to run budget deficits.

The Chinese don't force us to buy flat-screen TVs on credit, either. And they certainly didn't make anyone buy toxic securities. These are our problems. We made them.

Of course, the U.S. should not be in hock to another country, and certainly not to one with as many differences as we have with China. We don't want to tremble every time China—or anybody else—makes noises about our economic policies or about the value of the dollar.

The dilemma is that, in the short run, there is no way out. The eventual solution is to bring federal spending under control, place American entitlement programs on a sound footing, and return Americans to their earlier savings habits. Unfortunately, if we did this right now, our weakened economy might collapse altogether. Ending spending when the economy is in the midst of a rapid decline is madness. Hence, the stimulus plan, among other policies.

Yes, this will pack more debt on top of the mountain we already have. And yes, China will be buying a lot of it. But what's the alternative? All we can say is that China and other creditors are at least in the same boat we are in. If we collapse, they lose their investments.

In the longer run, this cannot go on. Once through this crisis, we must make the reforms necessary to wean ourselves off our addiction to debt. If we cannot do this, the Chinese piper will indeed call the tune. And it will not be a pretty melody. ■

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