

US Elections: Time to Recognise America's Vulnerabilities?

US Presidential hopeful, Barack Obama, has stolen the lead in the Democratic nominee race with his call for 'change'. The call has also triggered the imagination of many of the American people judging by the high number of people attending his campaign speeches and record high voter turnout at the primary elections. To all but the most partisan of outside observers this is an encouraging development as it is in stark contrast to the style of the Bush Administration of no change and no consultation other than with an elite few.

The irony is that whoever wins the election in November will not need to create 'change' as the global economic and political landscape has been shifting rapidly for sometime and not in favour of the United States. The urgent task for the incoming President will be to understand, interpret and react to the changing world in a way which is in the best interest of the American people and hopefully the rest of the world. The current economic slowdown maybe exacerbated by the failure of the Bush Administration to address some of the strategic economic issues. The price for failing to react appropriately by the next Administration will at the very least be a sharp weakening in the value of the US dollar and higher US interest rates.

Strategic Economic Challenges Facing the United States

The US economy has been a bastion of strength for the global economy for much of the latter part of the 20th century. Today US companies are world leaders in every area of economic activity, even if much of the activity takes place outside of the US. However, there are now clear signs that the US's economic dominance is beginning to be eroded. One of the major catalysts for the erosion of US economic dominance was the determination of the Chinese authorities to raise rapidly the living standards of its people. Their remarkable success, however, has contributed significantly to the following changes:

1. A shift in international trade flows of key commodities and goods that has benefited the East at the expense of the West.
2. A geographical shift in production from the West to the East which has been accompanied by a corresponding shift in the demand for labour.
3. Acceleration in technological knowledge and innovation from the West to the East in a wide range of politically sensitive areas.

4. A shift in the ownership and control of key natural resources by Eastern nations as demand for all commodities has rocketed but supply has not increased and easily obtainable reserves are in terminal decline.

5. Eastern economies have been the major beneficiaries of an extraordinarily large shift in foreign exchange reserves from West to East. This has culminated in the recent phenomenon of Sovereign Wealth Funds that are now buying significant shareholdings in strategic enterprises in the United States and elsewhere.

The above developments serve to weaken the economic dominance of the US by increasing its reliance on foreign entities for access to export markets, supply of key resources and capital. This need not be economically damaging, indeed the US can still use its influence, if it chooses to, by forging new international links and entering into quid pro quo arrangements. Failure to recognise the change and react, however, will lower the long term growth potential of the US economy which will increase the burden of servicing its growing foreign debt.

The new President will need to urgently assemble a convincing economic agenda which addresses US competitiveness and the US fiscal deficit in order to maintain the willingness of foreign investors to maintain their current record high holdings of US dollars.

As the economic balance of power swings eastwards so will political strength and influence. Prior to the war with the Iraq the US had a historically unparalleled hold on economic and therefore political power and influence. The Iraq war, coupled with the economic rise of China, has substantially curtailed US political influence. Note the rapid build-up of Chinese economic, political and cultural links with resource based economies including Africa. The Bush Administration has been in denial of this fact but the next President cannot be.

Short Term Economic Challenges

The current credit-crunch induced economic slow down in the US is highlighting some of the strategic weaknesses in the US economy. The bursting of the bubble in the housing market and the consequential problems in the credit markets is a severe test for the economy. The risks of a recession are high but such an outcome is not yet a certainty. The short term needs for capital by the financial sector have been partially provided by the Federal Reserve but much has come from the purchase of large chunks of equity of key US financial institutions by sovereign wealth funds at low prices. This may be a short term palliative but it may also have potentially long term adverse consequences. Another indication of the strategic challenges impinging upon the current economic troubles is the high and stubborn pace of inflation. There is a general belief, which also appears to be held by members of the Federal Open Market Committee, that the pace of inflation will slow as the pace of US economic growth slows. It is therefore considered prudent to cut interest rates sharply now even though the rate of inflation is still accelerating. The change in the global economic picture outlined above means that there is a significant risk that commodity prices, including energy and food, will continue accelerating. A weakening of the US dollar will compound the inflationary effect on the US economy. The combination of a weak US economy and an inflation rate that remains sticky will increase the likelihood that the current economic difficulties will become much worse.

Good time for Presidential elections but maybe a bad time to win.

The timing of the Presidential elections could not be better as the short and long run issues are clear for the electorate to see. The long term strategic economic and political challenges have been put on the back burner for too long by the Bush Administration. The current economic problems can be managed smoothly but the neglect of strategic issues may worsen the current economic downturn as the US dollar comes under pressure. This leaves the US economy potentially a hostage to political issues and makes the solution to the current economic crisis more difficult. Resolving these issues will be the making of the next President. Failure will be the breaking of them.

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