

The two largest economies

The United States and China are the two largest economies in the world today: the order depends on whether one uses nominal or purchasing power parity exchange rates. As it happens, both could have leadership changes in the next month. The U.S. presidential election is due on November 8, 2012, and the Congress of the Chinese Communist Party meets from the same day to elect a new political bureau and its standing committee. This would bring in a new leadership at the top (the President and the Prime Minister) for the next decade.

In China, *“as incomes have risen, so has the disparity between rich and poor. Corruption has proliferated The most common complaints include land grabs by property developers in cahoots with corrupt local officials.”* (Time, October 22). We, as a democracy, do not seem to be doing much better on these issues; on the other hand, authoritarian China has done a far better job in terms of providing basic social services like education and healthcare to its people than democratic India. Perhaps no wonder – the legitimacy of the Communist Party rule depends on continuous improvements in living standards for the people and job creation. True, growth in the current year is likely to be below 8% for the first time since 1999; on the other hand, as many as 10 mn jobs have been created in the first 9 months of the year. Not much change in policies need be expected after the new leadership takes over. Meanwhile, China has taken major steps to increase domestic consumption and reduce its external surplus, which has come down from a record \$ 400 bn in 2008 to \$ 80 bn in H1 2012.

Somewhat strangely, even as the Chinese external surplus falls, anti-China rhetoric in the U.S. is growing. The Republican candidate, Mr. Romney, has promised to brand China as a currency manipulator as his first act on taking oath. The big issue in the U.S. election is, however, quite different, and ideological: whether social welfare should be a legitimate part of government economic policies and fiscal spending. The Republican agenda would not only cut taxes on the rich but simultaneously eliminate most social welfare programs to balance the budget: the Republican Right would like nothing better than to go back to the *laissez faire* capitalism of the 19th century. They have contempt

for those dependent on government assistance. To quote Mr. Romney in his comments before his wealthy supporters, *“There are 47 percent who are with him, who are dependent upon government, who believe that they are victims, who believe that government has a responsibility to care for them, who believe that they are entitled to health care, to food, to housing, to you name it.”*

In a way, it is somewhat strange that there should be debate on the issue in the 21st century. The famous Hammurabi Code formulated almost 4000 years back, claimed divine authority *“to further the welfare of the people”*. Thomas Cromwell, the 16th century right-hand man of Henry VIII had proposed increase in taxation to help the poor. Early last century, President Theodore Roosevelt, had demanded a Square Deal, i.e. fairer division of spoils *“between the men who possess more than they have earned and the men who have earned more than they possess.”* And, in the U.S., social welfare has been an integral part of governmental responsibilities since the 1930s, under Franklin Roosevelt’s New Deal. Surely, there needs to be a better appreciation of the fact that, the poor are not poor merely because they are lazy parasites, not wanting to work – and too much of wealth is an accident of birth and background, not efforts or abilities, not *“representing the marginal cost of value addition to society”* as the ideological right believes. In fact, much of it is due to ability to *“manage”* the complex tax code, tax-driven financial engineering, speculation, etc. The result? – the U.S. has the highest income disparity amongst the OECD co countries (medium earning power has gone down in the last 30 years despite the growth in economy); a far costlier and the less than universal health service as compared to Europe. People tolerate the inequalities so long as *“everyone can dream that they, too, will become rich”* but *“a good education, the passport to prosperity is becoming unaffordable”* for most people (Raghuram Rajan, Financial Times, October 18th).

But to come back to the 47% comment, why has the political consensus on social welfare changed? Is it a genuine belief in the virtues of *laissez faire* capitalism? Or is it something more sinister, indeed racial? The fact is that a disproportionate number of welfare recipients are non-white.

As it happens, George McGovern, an opponent of the Vietnam War, who suffered the largest defeat ever in a Presidential election (1972), died earlier this week. The winner

was Richard Nixon, the most corrupt President in U.S. history, who was forced to resign (remember Watergate?) – and the U.S. suffered an ignominious defeat in Vietnam, in a few years. Are voters really wise as often proclaimed?

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