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THE US ECONOMY IN THE POST CRISIS SCENARIO – HOLDING LITTLE CAUSE FOR CHEER

C. BARATHI
RESEARCH SCHOLAR
MANIPUR INSTITUTE OF MANAGEMENT STUDIES
MANIPUR UNIVERSITY
CANCHIPUR, IMPHAL

S. PRAVEEN KUMAR
SR. LECTURER
DEPARTMENT OF MANAGEMENT STUDIES
PANIMALAR ENGINEERING COLLEGE
ANNA UNIVERSITY
CHENNAI

ABSTRACT
The impact of the global economic crisis which had engulfed the entire world and left a trail of losses, albeit of different magnitudes in global economies has not completely abated. Global economic growth has not yet reached the pre-crisis levels. The emerging markets have weathered the impact of the crisis in a strong manner compared to the developed economies. Though the World Bank and the IMF have estimated better growth rates for 2011-12 the persistent crisis in the Euro zone the inconsistencies in the policy response and the lack of a long term action plan to revive the US economy place significant hurdles in improving growth rates. The legal framework and a weak regulatory system were the basic causes for vested interests to earn massive amounts of illegal profits at the cost of the economy, there has not been any significant action to strengthen the regulatory system in the US to ensure non repetition of the crisis. To further worsen the already bleak scenario, commodity prices, oil prices have risen to all time highs and prices of basic food items have increased manifold and are expected to remain high due to poor output. This paper discusses the impact of the financial crisis on the global and US economy, impact of the stimulus packages and the quantitative easing on the US economy, current scenario with special emphasis on employment, poverty the financial system, deficits, inflationary trends, the government response and the unfolding economic scenario.

KEYWORDS
Global Crisis, Stimulus Package, Emerging Global Scenario, The Us Economy – Emerging Trends.

INTRODUCTION
The impact of the global economic crisis which had engulfed the entire world and left a trail of losses, albeit of different magnitudes in global economies has not completely abated. Global economic growth which has recovered in the previous year (2009-10) has not yet reached the pre-crisis levels. The emerging markets have weathered the impact of the crisis in a strong manner when compared to the developed economies which are yet to recover in a significant manner. Though the World Bank and the IMF have estimated better growth rates for 2011-12, the persistent crisis in the Euro zone, the inconsistencies in the policy response and the lack of a long term action plan to revive the US economy place significant hurdles in improving growth rates. Inspite of the clear realization that dilution of the legal framework and a weak regulatory system were the basic causes for vested interests to earn massive amounts of illegal profits at the cost of the economy, there has not any significant action to strengthen the regulatory system to ensure that there is no repeat of the crisis. Many of the banks which had been bailed out by the government have continued to pay sky high bonuses to the top management despite their financial position being fragile and without any significant improvement in their operational parameters.

There has not been any marked revival in employment because of the continuing weakness in both consumer and investment demand and the millions of jobs lost during the height of the crisis have left a vast section of the population in an impoverished state. To further worsen the already bleak scenario, commodity prices have risen to all time highs and prices of basic food items consumed by the general public have increased manifold and are expected to remain high due to poor output. Another significant cause for concern is the rise in oil prices which have already touched $80 per barrel. Experts in the industry estimate that oil prices would cross $100 and possibly rise to $120. Such increases would further reduce the already weak global growth trends. The number of poor and malnourished people the world over has swelled and due to the declining assistance to the vast multitudes in the African nations, who were in an extremely deprived state even before the onset of the crisis, many global agencies have predicted deaths due to disease and starvation to rise exponentially. This paper discusses the impact of the financial crisis on the global and US economy, impact of the stimulus packages and the quantitative easing on the US economy, current scenario with special emphasis on employment, poverty the financial system, deficits, inflationary trends, the government response and the unfolding economic scenario.

RESEARCH METHODOLOGY
The paper is conceptual in nature and has adopted the analytical approach to study the global scenario in the aftermath of the crisis. A literature review has been conducted to understand the viewpoints of experts. The period of study is 20006-07 to 2011-12.

NEED FOR THE STUDY
There have been sharply divergent views regarding the global economic trends and growth patterns in the post crisis period as well as the effectiveness of policy responses of the US government to revive the economy. The quantitative easing (QE2) announced by the US Federal Reserve and the various tax concessions granted extended by the Obama government to kick start economic growth have revived optimism about the future performance of the economy. Globally renowned agencies have pointed out significant decline in social indicators while stock market experts predict that the US stock markets would perform well in 2011-12. Amidst the mixed opinions and signals it becomes imperative to take stock of the emerging trends.

LITERATURE REVIEW
Balaji CD (2009) stated that the sub-prime mortgage crisis happened because the financial institutions in the US sacrificed morals and prudence at the altar of greed. Weak regulation, market fundamentalism and innovation with wrong intentions were the main reasons for the financial inferno. Dan Ariely (2009) felt that the world is paying a terrible price for the unblinking faith in the power of the invisible hand and is painfully blinking awake to the falsity of standard economic theory—that human beings are capable of always making rational decisions and that markets and institutions, in the aggregate, are healthily self-

regulating. Narayanan VG, Fabrizio Ferri, Lisa Brem (2009), examined the cause of the crisis from a national and global perspective and explored the actions taken by the US and European governments, Pankaj Ghemavat (2009) opined that the world looks far different today than it did before the global financial crisis struck. Reeling from the most brutal impacts of the recession, governments, economies, and societies everywhere are retrenching and pushing hard for increased protectionism. Left unchecked, heightened protectionism could prevent peoples around the world from achieving the true gains afforded by cross-border openness. Yiorgos Allayannis (2009), stated that the fundamental issue surrounding this crisis was the misjudgment of the risks taken, with the result that risk management failed to do its job of curtailing and managing risk as expected, Danielle Caddieux, David W. Conklin (2010), stated that by the fall of 2009, the crisis had stabilized, and the appearance of "green shoots" gave promise of recovery. By 2010, it was possible to put the financial crisis in perspective, and to raise questions about the causes and consequences. Of particular concern was whether new regulations might be needed to prevent a recurrence, and whether some of the tighter regulations should be international in scope, Raghuram Rajan (2010) stated that trade and investment policies, considerations of domestic sovereignty and the role of international agencies are all involved in global capitalism. If the 'global crisis' is to be resolved, every one of them has to be addressed and it is not going to be easy, Eric Janszen (2010), stated that the one economic indicator that seems to point toward long-term hope for businesses is the increase in the U.S. household savings rate—the portion of income that wage earners aren't spending. Savings were close to nil until the economic collapse but have been rising ever since stands at about 4.8%.

CONTOURS OF THE CRISIS

The origin of the global economic crisis can be traced to the consistent weakening of the legal and regulatory framework of the US financial system by successive governments. The systemic loopholes on the one hand enabled collusion among commercial and investment banks, insurance companies, mortgage lenders and brokers and on the other hand, created financial instruments of a dubious nature whose value was not known clearly to neither the seller nor the holder of the instrument. This created the FIRE economy i.e., Finance, Insurance and Real Estate economy which was characterized by easy availability of finance, insurance and soaring real estate prices which led to unsound lending practices by financial institutions, aggressive selling by the mortgage brokers, slicing and dicing of loans by the investment bankers and undue speculation which led to the piling up of household debt. When the housing bubble burst, real estate prices crashed, defaults increased bringing down major banks and insurance companies starting from Lehman Brothers.

IMPACT OF THE CRISIS: The IMF paper on the human costs of recession have put forth the fact that due to the economic slowdown, unemployment has increased by more than 30 million since 2007, and the global figure now is 230 million. The recession would result in lower lifetime earnings leading to poor access to education and healthcare. Moreover in most of the developed economies, growth plummeted; unemployment of the youth and long term unemployment have increased in an alarming manner. Another cause for serious concern is the decline in permanent employment and employees forced to take up temporary jobs to ensure their survival. As a result of the crisis, more than $6.3 trillion in financial assets and over $5 trillion in real estate value vanished in the 24 months between late 2007 and late 2009. The net worth of households declined a staggering $11 trillion over 2008 and 2009.

THE US STIMULUS PACKAGE AND QUANTITATIVE EASING

The stimulus package implemented by the US government was quite small when compared to the magnitude of the crisis. Further, the package was not aimed at job generating recovery of the US economy but instead relied on tax cuts to spur consumer demand, which has not materialized as visualized. The situation that is being witnessed today in the US can be termed as 'de-leveraging'. The US public had ran up huge amounts of debt due to the irrational lending policies of the banks and household debt which was 83 per cent of household income in the 1990's shot up to 130 per cent in 2007. Now the households are paying back the debt that they had accumulated in the past and as a result the household debt has fallen to 118 per cent of household income. The result is there have been cutbacks in spending resulting in low consumer demand (China has overtaken the US as the largest market for passenger vehicles in 2009). The tax breaks would not spur demand due to the fact that the rich and the middle class are less likely to increase spending and the tax breaks to the industry would not result in increased investment because there is already excess capacity.

The recent package announced by the Obama Administration to revive the economy will pump in $850 billion of stimulus to the US economy. The concessions granted include:

(i) The new payroll tax cut for the employed (social security tax levied would be reduced from 6.2% to 4.2%)
(ii) Extended benefits for the unemployed,
(iii) Estate tax cut (rates to be maintained at 35% from the earlier proposal of 55%) for the rich,
(iv)Extension of the Bush era tax cuts for two years
(v) Business tax breaks including credit for research and development expenditure
(vi)Protection for middle class families from the alternative minimum tax

There has been growing criticism over the recent Federal Reserve's move to buy bonds aggregating $600 billion in a phased manner at $75 billion dollars every month. There is growing skepticism over whether the program would boost the economy and many of the critics have opined that it would only increase inflation and commodity prices. The bond buying program whose objective was to lower yields on government securities has achieved just the opposite with the yields on US Treasury bonds rising from the date the government made the announcement (November 3).

EMERGING GLOBAL SCENARIO

Global growth which showed signs of picking up in the third and fourth quarters of 2009, slumped in the first two quarters of the year 2010, prompting the OECD to mention in its interim assessment of the global economy issued in September 2010 to state, "The world economic recovery may be slowing faster than previously anticipated". It is the consumption expenditure and government expenditure which keeps the growth engine of the economy moving, but in the aftermath of the criris, private consumption expenditure which slumped in 2009 has not recovered and public expenditure which increased due to the fiscal stimulus packages in 2009 has fell sharply in 2010. IMF has projected that the slowdown could extend to the second half of 2011. With the governments in developed economies having exhausted their resources in stimulus packages and in some cases borrowed excessively to support such packages, the continuing slow down is bound to have an adverse impact on the already weak employment markets.

In general, gross domestic product (GDP) is growing faster in emerging economies and developing countries. Economic indicators suggest that the economic scenario of the developed countries continues to remain uncertain. Though the developed world was expected to grow slower when compared to the developing countries, questions are now raised whether even the slow growth rates would materialize. The GDP of the OECD countries increased by 0.7 per cent on a sequential basis in the first and the second quarter of 2010. The UK economy grew by 1.1 per cent; Germany tops the growth charts at 2.2 per cent while the Japanese and US economy slowed down to 0.1 per cent and 0.6 per cent respectively. GDP for the United Arab Emirates as a whole fell by 2.9 per cent in 2009-10 and is expected to rise by 2 per cent in 2010-11. Policy makers are confounded with the dilemma of whether to withdraw the stimulus measures or to announce a fresh set of measures. Withdrawing the stimulus might push the economies in the throes of a double dip recession while continuing stimulus measures might result in piling up of debt, which might be harmful in the long run. The FAO Food Price Index averaged 205 points in November 2010, up 7 points from October and only 7 points below its peak in June 2008. However, a total of 925 million people are still estimated to be undernourished in 2010, representing almost 16 percent of the population of developing countries.

THE US ECONOMY – EMERGING TRENDS

The US which is the number one economy in the world in terms of GDP and per capita income has been severely affected by the crisis. GDP growth rates have declined, unemployment is at 26 year highs, consumer demand has slumped, industry is left with huge surplus capacity, poverty rates have increased, the number of people without insurance has grown manifold, exports from the country have been badly affected, government revenues are down, debt and deficits have soared to record levels and recovery seems to be a mirage. The following is an analysis of the trends in the US economy:

GDP: After a decline of 2.2 per cent in GDP in 2009, the US is expected to grow at 3.3 per cent this year. The US whose share of global GDP grew from 26.3 per cent in 1990 to 29.8 per cent in 1999 has declined to 24.3 per cent in 2009 while the shares of Indian and China have increased. The GDP of US was around $14 trillion in 2009 and experts point out that China which has already overtaken Japan to become the second largest economy in terms of GDP will unseat the US by 2030 to become the world's largest economy. The per capita income of the US at $46,000 in 2009 was the highest among the large economies. The worrying fact is that income disparities are further widening in the US economy. In 1976, the top one per cent of households had a share of 8.6 per cent of income and in 2007 their share of income had shot up to 23.5 per cent and in 2008, seven out of ten Americans found their incomes stagnating. Paul Krugman wrote in a New York Times op-ed (February 27, 2006) that in the last 30 years the redistribution of wealth through tax cuts has provided average working families with at most a 1 percent increase in income, while those in the 99.99th percentile gained approximately a 497 percent increase in income. Leiserson and Rohaly of the Tax Policy Center estimate that in 2006 family incomes in the 99th percentile were approximately $402,000 and those in the 99.9th percentile were approximately $1,672,726. At the same time, the Children's Defense Fund report "America's Cradle to Prison Pipeline" documented that child poverty could be eliminated in the U.S. for $55 billion a year, meaning that ending some of the tax cuts for the wealthiest 1 percent of taxpayers could end child poverty. The median household income in the US dropped from $51,726 in 2008 to $50,221 in 2009. The US GDP fell just one per cent in the second quarter of 2009 compared to a fall of 6.4 per cent in the first three months. The GDP growth is expected to turn positive with a growth of 2 percent in 2010, and rise to 3.8 per cent after a year. The economy is gradually showing signs of stability but unemployment continues to be a major issue though the rate at which jobs were being slashed has come down. On a positive note, banks have started seeing second-quarter profits.

TAX REVENUES: Tax collections of the US government declined due to the slow down as well as various tax concessions. During FY 2009, the US government collected about $400 billion less than FY 2008. Individual income taxes fell by 20 per cent, while corporate taxes declined 50 per cent. At 15 per cent of GDP, the 2009 collections were the lowest level of the past 50 years.

FISCAL DEFICIT AND DEBT: The White House has forecast a whopping $9.05 trillion deficit for the 2010-2019 periods, up by $2 trillion from the February estimate. The rising fiscal deficit could hit further reforms and economic growth. The Office of Management and Budget forecasts a weaker economic recovery as the gross domestic product falls by 2.8 per cent this year. US President Barack Obama pumped in a $787-billion stimulus to revive the economy; a total collapse was thus avoided. Today, each citizen's share of this debt is $44,393.

EMPLOYMENT: Job losses during the recession were much worse relative to output declines when compared to the previous economic slumps and as at the end of December 2010, official payroll data has not shown any big increase in hiring. While some big companies are expanding, other are merely replacing vacancies due to resignation or retirement.

According to the Associated Press, the US has lost 7.5 million jobs in the last 35 months since December 2007. In other words, on an average 7,000 jobs have been lost every day. There were 14.8 million people who were unemployed as on October 2010.If the persons who are currently working in part time jobs but desire full time employment and those who have given up their quest for employment due to the bleak scenario are taken into account, nearly 27 million people or 17 per cent of the labour force is underemployed. The United States Bureau of Labour Statistics point out that, about 46 per cent of those were jobless for 27 weeks or longer and 31 per cent were unemployed for 52 weeks or more.

From January 2009 when the Obama government assumed power to till date, government employment has fallen by over 3 lakh jobs and since January 2008, the private sector has lost more than 8 million jobs. The US unemployment rate went up to 9.8 per cent in November 2010 up from 9.6 per cent in the preceding three months. The number of job losers and persons who completed temporary jobs rose by 3, 90,000 to 9.5 million. The number of people who were looking for permanent jobs remained more or less unchanged at 9 million. The number of those who were not in the labour force but wanted and were available for work and had looked for a job sometime in the prior 12 months rose by 2.3 million from the earlier year figure. Nonfarm employment has barely changed adding a very small number of jobs. Even the small job creation was in temporary help services indicating a shortfall in permanent job creation. Job openings have decreased in many sectors, the number of workers forced into part time employment has increased and only three States have unemployment rates of less than 5 per cent and even highly skilled workers are desperate for employment.

Government data however shows an increasing trend in job openings. There were 3.2 million private sector job openings at the end of October 2010, up from 2.3 million a year earlier, though the number is below the 3.7 billion in October 2007 before the recession according to the US Bureau of Labour Statistics. Private sector job openings are showing a slow revival particularly in accounting, retailing, consulting, healthcare, telecommunications and defense related industries. According to data collected for the Wall Street Journal by Indeed Inc., which runs one of the largest employment websites, the number of US job postings in the internet rose to 4.7 million in December 2010 up from 2.7 million, a year earlier and 3.3 million in December 2008. The fact however remains that all vacancies are not posted online and skilled jobs are over represented while unskilled and semi skilled jobs in agriculture and manufacturing are underrepresented in online positings.

New claims for unemployment benefits declined by just 3,000 to 4,20,000 in the third week of December 2010 indicating a marginal slowing down of job losses. Economic experts estimate that job growth would be moderate in 2011 and the unemployment rate would be at 9 per cent.

HOUSING MARKET: For the period starting from World War II until 2008, Americans households had 60 to 80 per cent equity in their homes while mortgages accounted for the balance. After the bursting of the housing bubble in 2008, banks own more than 60 per cent of the average American home. The decline of the housing market appears to be never-ending since millions of people do not have jobs; millions of others work only part time; millions more work fulltime but make very little money; and additional millions fear losing their jobs. In July 2010 alone, 300,000 owners lost their residences because they didn't make their mortgage payments. Morgan Stanley had warned earlier this year that it would take four years for the US housing crisis to be over. According to the report, 10 per cent of loans are delinquent. Meanwhile, new figures showed home foreclosures in August hit the highest level since the mortgage crisis began. Banks repossessed 95,364 properties in August, up by 3 percent from July and an increase of 25 percent from August 2009.

FISCAL, MONETARY POLICY AND INFLATION: To counter the slow down in the economy characterized by record high unemployment and weak consumer demand the government has adopted a loose monetary policy with interest rates kept at very low levels. The government has come out with a series of tax concessions and would continue tax cuts of the Bush era. Though core inflation which excludes the volatile food and energy prices is at a fifty year low and the inflation rate is at a low 1.2 per cent, the rising oil prices are a cause of concern (oil prices have increased by 16 per cent in the last four months). Oil prices have already crossed $90 per barrel and a $15 rise in oil prices would reduce the already low GDP growth by half a percentage point and would erase the stimulative effect of QE2, the bond buying program of $600 billion.

POVERTY: The number of poor people in the US is rising to record levels and the country has the third worst poverty rate among the advanced nations. One in seven Americans was living in poverty in 2009 with a family of four living on less than $21,954 a year, according to the US Census Bureau. The official poverty rate in 2009 was 14.3 per cent (the highest in the last 51 years), up from 13.2 per cent in 2008. This was the second statistically significant annual increase in the poverty rate since 2004. In 2009, 43.6 million people were in poverty, up from 39.8 million in 2008 -- the third consecutive annual increase in the number of people in poverty. Between 2008 and 2009, the poverty rate increased for children under the age of 18 (from 19.0 per cent to 20.7 per cent) and people aged 18 to 64 (from 11.7 per cent to 12.9 per cent), but decreased for people aged 65 and older (from 9.7 per cent to 8.9 per cent).Between 2007 and 2009, the child poverty rate and the number in poverty increased by 2.7 percentage points and 2.1 million.

DOLLAR: The dollar would remain stable until China reduces its purchase of government debt and problems in the Euro region continue. The debt problem in the Euro region especially in Ireland, Iceland, Portugal, Greece and Spain does not seem to subside inspite of huge governmental borrowing and assistance from the Euro zone. It is felt that the contagion would spread to other countries and might affect the financial stability of the Euro zone. The fact that needs to be remembered is that spiraling debt and easy money would result in a weaker dollar.

EXPORTS: The US President has called for doubling of exports over the next five years. If such a thing happen it would greatly spur job creation and economic growth, but, it is a tall order for an economy which has been driven by consumption and investment in housing. One more thorn is the artificial devaluation of the Chinese currency despite a volley a protests from the US. Unless the Chinese currency is allowed to reach its natural level (which would be higher than the current level) the competitiveness of US exports would remain a question mark. Another important cause of worry in the export front is that hi-tech exports from the US are on the decline.

STOCK MARKETS: The positive news in the retail sales front in the past few months and the slowing down of job losses has renewed investor optimism. For the period ending December 24, 2010, the Dow and S&P recorded four consecutive weeks of gains and it was the fifth week of consecutive gains for the NASDAQ. Though volumes are low, the investor sentiment has turned positive as borne out by the facts that, according to the latest AAII Sentiment Survey, the level of investor optimism rose to 63.3 per cent in the week ended December 22, the highest since 18 November 2004. The level of pessimism was the lowest since 24 November 2005 and the bull bear spread was at the highest since 15 April 2004. The Bank of America-Merrill Lynch (BoFa-ML) survey for December 2010 found that 16 per cent of investors were overweight on equities as compared to 1 per cent in the previous year. The US commodities market is also on an upswing. Due to the loose monetary policy investors expect that inflation would move up and therefore many of them had exited from bonds and have starting investing in commodities and the net overweight position in commodities was at 23 per cent.

INSURANCE COVERAGE: The percentage of people without health insurance increased to 16.7 per cent in 2009 from 15.4 per cent in 2008. The number of uninsured people increased to 50.7 million in 2009 from 46.3 million in 2008. The number of people with health insurance decreased to 253.6 million in 2009 from 255.1 million in 2008. This is the first year that the number of people with health insurance has decreased since 1987, the first year that comparable health insurance data were collected.

CONCLUSION

The US government's move to achieve the turnaround by piling up debt (US debt is 60 per cent of GDP) and printing money is fraught with serious consequences. There has been only a partial improvement in the regulation of the financial sector which was the primary cause of the crisis, and without doubt there is much more that needs to be done. After the government support to the financial institutions which were on the verge of collapse, it was expected that they would reform themselves and adopt better control mechanisms and ensure tighter internal controls. But, reports from the financial media point out that no such thing has happened and many of the institutions are back to their old ways. The government also has not acted with alacrity and firmness. This inaction on the part of the government and the financial industry may plant the seeds for financial crisis of a much greater magnitude in the future.

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Hoping an appropriate consideration.

With sincere regards

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Sd/-

Co-ordinator