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The Economy and Anarchy

Ron Tabor

August 18, 2008

The economic events of the last few months have raised a lot of questions about where the US and world economies are headed and what this means for the political climate in the United States. In what follows, I have attempted to answer these questions. As much to clarify my own thinking as to explain my thoughts to others, I have tried to place the recent economic developments in the context of both my previous understanding of the economy and a brief, and very sketchy, outline of the history of the US economy since 1970.

In the late 1960s and early 70s, I developed an analysis that attempted to explain the nature of the post-World War II era of economic prosperity in the United States and why that era would come to an end. At the time I began to develop my ideas, that long period of economic expansion was coming to a dramatic close with the recession of 1970 and President Richard Nixon's imposition of wage-price controls in 1971, both of which exploded the claims of mainstream economists that capitalism had solved its major problems. My analysis was based largely on a reading of Karl Marx's theory of capital, as elaborated in his magnum opus, *Das Kapital*, along with the work of contemporary Marxist theoreticians, such as Michael

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Kidron, Paul Mattick, and (I am ashamed to admit) Lyndon LaRouche, then known as Lyn Marcus.

My fundamental thesis was that the post-war boom, based to a considerable degree on a vast increase in defense spending (the “permanent arms economy”), which was financed in part by government deficits (borrowing), had not solved any of capitalism’s contradictions, particularly, the tendency of the rate of profit to fall. Instead, it had merely covered them over—in effect, “borrowing from the future” to pump up the economy in the present. In a nutshell, based on the experiences of the Great Depression of the 1930s and World War II, the capitalists had learned how to temporarily restore conditions of profitable production through a variety of artificial means, most of which involved the proliferation of debt, government and private, and what Marx called “fictitious capital,” claims, in the form of stocks, bonds, and other securities, to wealth that does not in fact exist. Based on this analysis, I predicted that at some point in the future, the US and world economies would experience a 1929-type financial collapse and an economic crisis similar to the Depression. This in turn, I thought, would lead to a period of intensified competition between the major capitalist powers, the growth of radical right-wing movements, a resurgence of militant working class struggles, intensified regional conflicts, and possibly, another world war.

Today, I am no longer a Marxist and do not subscribe to Marx’s theory of capitalism. One of my major reasons for rejecting Marx’s analysis is that, like mainstream (“bourgeois”) economics, it attempts to describe our socio-economic system as a self-contained whole, independently of its relation to nature. Specifically, although Marx recognized that the products of nature—raw materials, air, water—constituted essential elements of capitalist production, he insisted that human labor, and only human labor, is the source of all value. This was based, at least in part, on his belief that the products of nature were, for all practical purposes, infinite and therefore

wide discussion possible; for the first time in our history, we can actually have an international conversation about what we, as a species, need to do to survive. But there is no dynamic that will necessarily move us in the right direction; there is no God, no transcendental logic or Reason, no “laws of history” that will force us to make the right decision(s). The responsibility and the choice rests with us. It involves, as the Danish existentialist philosopher, Soren Kierkegaard, put it in another context, a “leap.” People have to *decide* that they want to cooperate; they have to be aware of the necessity of working together and then choose to do so. (This is why I have no interest in the discussions and debates among anarchists about the precise form of property or society—collective, communal, etc.—that best embodies our ideals. When human beings decide that they really want to cooperate with their fellows, in their own country and around the world, the abstract question of precisely what forms this cooperation might take—forms of property and forms of organization—will virtually disappear; the answers will be worked out as we go along.)

And just as we need to see our fellow humans as part of “us” rather than “them,” and to cooperate rather than compete with them, we must begin to see the Earth in the same way; not something we can attack and plunder, but something that is really part of us, something with which we need to cooperate.

This posing of the need to cooperate with ourselves and our planet is the other side, the potentially positive side, of the economic/environmental crisis that we are currently struggling with. It may finally force us to come to grips with who we are and what we are doing to our home, the Earth. Like the rapidly rising waters of a river in flood, it may be what finally convinces human beings that they need to unite, to cooperate on a world scale, and to throw ourselves into what needs to be done, to fill the sandbags, as it were, and to stack them at the river’s edge while there is still time.

uniting and cooperating on an Earthwide—species-wide—level. And this will require a change in our attitudes toward our fellow humans, so that we increasingly see them (all or most of them) as “us” rather than “them.” Thus, a revolution that even has a chance of solving our global problems has to be based on a profound psychological/social transformation of human beings. (As the great Russian writer, Fyodor Dostoyevsky, put it (in *Winter Notes on Summer Impressions*, his work criticizing capitalist societies of 19th century Western Europe): “There has to be a change of heart.” And it won’t do to believe, as some have argued, that this psychological transformation will occur by itself, during the process of the revolution, as people in struggle are supposedly impelled to unite and develop solidarity; as we have often seen throughout our history, people often unite in order to attack others. Panhuman unity needs to be posed as an explicit goal and fought for, devising methods of argument and struggle that embody this principle in action.

The creation of the kind of global, species-wide cooperation that I have been talking about really adds up to an evolutionary step for humanity, the human species evolving to a higher level. I do not believe there is anything inevitable about this. (To be frank, I am not even sure it is possible.) History (and literally, the Earth) is littered with the ruins of societies that collapsed because they destroyed the natural environment on which they depended. (For those who would like to read about this, I suggest Jared Diamond’s *Collapse: How Societies Choose to Fail or Succeed*.) There is no guarantee that this won’t happen to the human species as a whole. True, there are things that might help facilitate the transformation I am describing. Today, human technology is capable of feeding and clothing everybody on the planet (but how long will this be the case?). The global economy is bringing more and more people into economic and social contact with each other. Equally important, global communications make an Earth-wide, humanity-

free (without cost). Today, it should be obvious that this is not the case; in fact, it is a devastatingly erroneous assumption. (One indication of this is the tremendous environmental destruction that occurred in the former Soviet Union, where the rulers attempted to plan the economy with methods that were based on Marx’s theory.) Although the relation between capitalism and our increasingly severe environmental crisis can be explained in Marxist terms, such an explanation has an added-on, ad hoc character. Instead, I believe that a truly revolutionary (and accurate) analysis of global capitalism must be based on the crucial recognition that nature and our economic system do not represent two independent realms, and that, as a result, the economic crisis and the environmental crisis are integrally connected. Among other things, this requires a new theory of value, one that recognizes nature’s essential contribution to the creation of value, and thus a substantively new theory.

Despite this, I believe that my old analysis has general validity. That is, I believe that capitalism has not solved its fundamental problems, but that the capitalists (actually, their economists and central bankers) have learned how to manipulate the system to moderate the business cycle (previously, the system’s tendency to swing between speculative booms and depression, “booms” and “busts”) and to engender conditions of relative prosperity for a period of time through the expansion of debt and through deferring many of the system’s problems to the future. A look at the situation confronting Social Security, our healthcare system, and our public schools—indeed, the entire infrastructure (including roads and highways, trains, airports, public transit systems, dams and levees, electric power systems, etc.) of the country—along with vast public and private indebtedness, suggests the truth of this position.

The environmental crisis needs to be understood in the same way. Instead of setting aside resources to replace and/or restore

what we take and have taken from Nature, capitalism, assuming, as Marx did, that natural resources are infinite, just takes from, or plunders, the planet. Just as a capitalist firm can boost its profits in the short term by deciding not to set aside funds to replace its plants and equipment when the current machinery wears out or becomes obsolete, and instead to include these funds in its accounts as profits, international capitalism boosts its profits in the short term by failing to set aside funds to pay for what it plunders from the Earth. And just as eventually the firm, if it is to continue, has to come up with the money to replace its equipment, cutting into future profits as it does so, the economic system as a whole must eventually come up with the resources to restore the environment. If it does not, the whole system will stagnate and perhaps die. (At the very least, the prices of the raw materials Nature provides, including water, will rise as these materials become harder to reach and to process or become depleted altogether.)

While the danger of a 1929-style financial crisis and global depression à la the 1930s is real, I am no longer convinced that such events are inevitable or even highly likely. As it turned out, the Depression of the '30s was exacerbated by unique historical circumstances: (1) the saddling of Germany, one of the world's strongest economies, with enormous reparations payments (debts owed to the Allied powers—France, Great Britain and the United States) after World War I; (2) in part resulting from this, the Nazis' takeover of Germany and their efforts to turn the German economy inward, toward autarchy, that is, an attempt to isolate the country from the global economy; (3) the Russian Revolution of 1917 and the imposition of an embargo against the Russian economy by the traditional capitalist countries; (4) actions by the US and other capitalist governments that intensified the crisis, including attempts to balance government budgets (President Herbert Hoover raised taxes), and the enactment of high tariffs barriers that drastically curtailed world trade; (5) an agricultural depression in the United States

while millions of people are slaughtered. Equally important, many of those involved in these revolutions, including and in particular their leaders, become morally corrupted, too willing to kill large numbers of human beings and to resort to brutal, coercive measures to get their way.

Aside from being at least relatively pacific, the kind of transformation I am talking about must be, above all, a moral or spiritual one. Human beings must learn a new way of relating to their fellows and to the natural world: working together rather than competing, sharing instead of taking, discussing rather than killing. And this will not be possible if millions (billions?) of people become brutalized by violence.

Many anarchists have long insisted that human beings naturally cooperate. This, to them, is the real basis for the possibility of an anarchist—a truly democratic, egalitarian, and cooperative—society. But it is easy to overlook the fact that this cooperation has almost always taken place in hierarchical, competitive settings; masters and slaves, bosses and workers, politicians and voters, preachers and congregations, leaders and followers. Some people like to point to the existence of what Marx called “primitive communism,” that is, small, locally-based societies, usually centered around kinship groups and lacking social stratification and formal governments, as a kind of proof that a non-hierarchical, cooperative society is possible. If it happened once, it is implied, it can happen again, but on a more advanced level. But they forget that even where these groups were/are truly non-hierarchical, they almost always existed/exist in conflict with other groups of people. It seems as if human beings have only been able to work together, to truly unite and cooperate, when they do so against outsiders, against an “other,” in other words, by dividing humanity into “us” versus “them.” In fact, the human species has never been able to cooperate on a truly global, pan-human scale. But what we need now, and will need even more in the coming years, is precisely this, human beings

Second, to really address the crisis will require a truly cooperative approach, not only among nations but among the peoples making up each nation and across the globe. The problems of the world—economic, social, and environmental—are too vast for any one country, for any small group of countries, or for a tiny global elite to solve. Real solutions will require the massive mobilization of group and individual efforts. Even now, the world food crisis is not being addressed primarily by governments, but by so-called “non-governmental organizations.” If that crisis and other crises, including the environmental one, are to be addressed, the cooperation of large numbers of people will be required. And if this cooperation is to be meaningful, it will have to involve giving those people both a real say in whatever discussions take place and real power to effect decisions, not only local ones, but national and international decisions as well. Truly effective feedback mechanisms will have to be developed to determine what works or what doesn’t work and why, while implementing decisions will require the mobilizing of millions of people. If all this is to be real, it will require a drastic equalization of wealth and political power throughout the world. For how else is true cooperation going to be possible if a few people have most of the money and, therefore, most of the power, while the vast majority have little or none?

Finally, this drastic equalization of wealth and power amounts to what many of us used to call a socialist revolution, and what today I prefer to call an anarchist transformation of society. This revolution does not have to be violent, in the sense of being an orgy of killing and bloodletting. Most of the revolutions we have seen in the last few decades have involved very little violence. While they have not been totally non-violent or against violence in principle, they have been carried out with relatively little killing, let alone the massacres that characterized previous revolutions. The danger of truly violent overturns, such as the French, Russian, and Chinese Revolutions, is that entire countries are devastated

that lasted through most of the 1920s and into the ’30s; and (6) some of President Franklin D. Roosevelt’s own New Deal policies, specifically his measures to prevent prices from falling. (Had prices declined, it might have been possible to reestablish conditions of profitable production earlier than they were.) Meanwhile, since the Depression, the economists and the capitalist class as a whole have learned a great deal about managing the economy; the aggressive actions taken in the last few months by the Federal Reserve Bank under Federal Reserve Board Chairman Ben Bernanke to ease the credit crunch, shore up the investment banks, and calm the stock markets demonstrate this. As a result, the system has avoided a serious crisis for now (although the financial sector is still in turmoil), but only through the continuation of the process I had described, that is, by postponing dealing with fundamental problems and running up more debt. A brief look at the economic history of the country since the 1970s suggests how this played out in practice.

Although there was no dramatic collapse and depression, the 1970s were a period of substantial economic crisis. (Economically, it was the second worst decade, after the 1930s, of the 20th century). This included the OPEC oil embargo, the drastic increase in the price of oil, significant inflation (rising prices and a declining value of the dollar) in general, and at least two severe recessions—economic downturns, less severe than depressions, officially defined as two consecutive quarters of a decline of the Gross Domestic Product. This period of “stagflation” (stagnation plus inflation) was brought to a close in the early 1980s, largely through the Reagan government’s vicious attack on the labor unions, a lowering of taxes, and a drastic increase in arms spending. While this led to a huge increase in the federal budget deficit (and growth of the government’s debt), it also laid the basis for a significant economic upturn, along with growth of the stock market (based to a considerable degree on a merger and acquisition binge), throughout much

of the decade. This, in turn, led to the beginning of the boom in the private housing sector (and the proliferation of mortgages and mortgage-based debt), which, despite some ups and downs, lasted until August of last year.

In 1988, the stock market “crashed” (prices of stocks dropped substantially in a short period of time), but the downturn that usually follows such events did not occur until two years later. The recession of 1990–1991 was pretty severe, especially in California, since it entailed a considerable cut in arms spending and the dismantling of a significant section of the defense/aerospace industry, much of which was based in southern California. Although the recovery from that recession was slow, it did eventually pick up steam, fueled in large measure by the rapid expansion of the new high tech industries (the development and distribution of personal computers, the creation of the Internet, bio-technology, etc.), a substantial rise in stock prices, and, once again, the growth of the housing sector. Although this upturn was artificially extended for several years, largely through the efforts of then Chairman of the Federal Reserve Bank, Alan Greenspan, to keep interest rates low, it finally came to an end in the year 2000, when the “dot.com bubble” burst and the stock market dropped substantially once again. Although the recession of 2000–2001 was not very deep (among other things, it did not involve major layoffs of workers), the economic recovery was, once again, lethargic (the attack on the World Trade Center significantly dampened economic activity), and stock prices remained relatively low for quite some time, not reaching their previous highs until some years later. The ensuing period of economic expansion (the one that recently ended) was led by the continued but less robust development of the high tech industries and, increasingly as the boom developed, the growth of the housing sector that had begun in the 1980s.

The burgeoning of the home-building related industry was fomented in large measure by the extension of so-called

When the increasing price of food really starts to hit, how long will people remain content? And how long will undocumented immigrants allow themselves to be made scapegoats for the problems of the country that are not of their making?

If the political debate does open up, what will we, as libertarian socialists and anarchists, have to say about the issues the country and world are facing? While we certainly need concrete proposals to address specific issues, we also need to make clear what our starting point is. Here is how I look at it, put in the most general terms:

First, the fundamental crisis we are confronting is global. The environmental crisis is obviously so, while the increasing globalization of the economy means that more narrowly economic issues are also international in scope. Consequently, our problems must be addressed internationally. Any plan of action that pits the people of the United States against other nations and other peoples will ultimately fail. For example, if the US raises tariff barriers in an attempt to protect US industries from foreign competition, other countries will probably retaliate (this is what happened in the 1930s). Then global trade will shrink and we will see an international depression, which will affect everybody. In addition, merely attempting to raise productivity/efficiency, through more automation, layoffs, speedup, etc., but without dealing with global warming and other environmental issues, will only work in the short term, at best. The problems of the US and international economy are far too great to be dealt with via the methods that have been utilized in the past. In fact, the situation we are confronting is not just an economic crisis or an environmental crisis. It is a crisis of humanity. The way we have been living throughout our entire history, among other things by attacking and brutalizing the natural world without bothering to replenish it, cannot continue for long. It is already having and will increasingly have a direct impact on our economic and social system, making capitalist-based economic growth ever more difficult to achieve.

about the lose them, about the millions of people who, even working several jobs, can't cover their monthly expenses, let alone pay off their debts? What are we to do about immigration, the world food crisis, and—oh yes—the environment? (Unfortunately, the rise in oil prices will create political pressure for measures, such as the resumption of off-shore drilling, that will make the environmental crisis worse, once again “solving” problems in the short-run, while makings things worse in the future.)

It is already quite clear, if one listens to the debates of the candidates and would-be candidates for the presidency, that the major parties have no serious proposals to address these (and the other) issues facing the country. During the Democratic primary campaign, Barack Obama and Hillary Clinton argued over whether to have the oil companies pay the gasoline tax; Clinton was for it, Obama against. Obama rightly insisted that it wouldn't make a dent in the problem, but what is his proposal? I have never heard it. The various ideas put forward to address the crisis in healthcare are similarly vacuous. And what about the other problems? Nobody is putting forward anything that remotely deals with them. Hopefully, this will lead to a broadening of the political debate in the country, granting some space to ideas that have been off the political map for a while, and offering at least the appearance of relevance to more radical—left and right—ideas and ideologies.

This opening of the political debate is likely to get a significant boost from what I expect (and hope) will be at least some increase in popular struggles. Although it is possible, I find it hard to believe that people losing, or in danger of losing, their homes are going to sit back and do nothing about it. Already there are the equivalent of shanty-towns, but now made of more high-tech materials, springing up near major cities to house those who have lost their homes. How high does the price of gasoline have to go before people start to take action? I don't know, but I do believe that, sooner or later, people will.

“subprime” and adjustable-rate mortgages, which appeared to make home ownership possible for many people who did not in fact have the financial wherewithal to buy a house. As the economic upturn wore on, it was more and more impelled by this expansion of debt, and the growth of the construction, home furnishing, and home financing industries that it stimulated, and less and less by other sectors of the economy. In addition, like all speculative booms, this one fed on itself. As home prices increased while the Federal Reserve Bank kept interest rates relatively low, more and more people, afraid to miss the boat, got into the act, buying houses that, as it turned out, they couldn't afford. Meanwhile, this bubble spread throughout the rest of the US and global economy through at least two mechanisms. (1) As homeowners saw the values of their houses go up (as prices rose), they believed that their financial assets had also increased and went on a spending spree, mostly through incurring more debt, via credit cards and installment buying, with other consumers following suit. (Since 2005, the net savings rate of people in the country has been negative—meaning that on average, people have been spending more than they earn—for the first time since the Great Depression. Today, the household debt-to-income ratio—how much people owe compared to how much they earn—has reached an all-time high, over 19%.) Many of the goods people purchased were made abroad, including in the newly industrializing countries of Asia, such as China, Malaysia, and India, thus stimulating their economies, but worsening the US balance of trade and balance of payments deficits. (2) Meanwhile, the mortgage lenders packaged their mushrooming mortgages into bundles of securities and then sold them to investors, including and in particular, vast institutions, domestic and foreign, government and private, that control enormous quantities of financial assets. This ballooning sector, based on extremely inflated home prices,

was relatively new and entirely unregulated, and nobody knew (or knows) exactly how much money was/is involved.

While the economic events I have been describing, that is, those that occurred during the period from 1970 to the present, were taking place, we also experienced substantial changes in the structure of the US economy and of our society as a whole. This included the “de-industrialization” of the country, as the big industries that had once been so economically and politically dominant—automobiles, steel, electrical appliances, textiles, chemicals, aerospace—either shrank, were displaced by foreign competitors or disappeared altogether. Increasingly, many US corporations built factories overseas to take advantage of lower wages and readier access to sources of raw materials and to foreign markets, while others went under or were bought up by more efficient foreign firms. Those that survived increasingly automated their operations, cutting down their workforces. These processes led to the disappearance of millions of unionized jobs, the drastic weakening of the trade unions, the implosion of many Midwestern cities, and a massive increase in the size of the service sector of the economy. While this led to the expansion of some sectors of the middle class, it also meant a major change in the nature of the US working class, as millions of unionized skilled and semi-skilled jobs disappeared. Meanwhile, many of the newer jobs in the service sectors offered much lower wages, and were taken by immigrants, legal and illegal. Virtually a whole layer of the working class was destroyed, and the labor movement, which had organized and represented these workers, dwindled in size. Meanwhile, the total amount of debt—federal and state government, private (mortgages, installment, and credit-card debt), and of the country as whole in the form of the long-standing balance of payments deficit—has exploded, reaching staggering levels. Next year’s federal budget deficit is projected to be about \$500 billion, while the national debt (which does not include the indebtedness of state and local

However, given the other issues involved in this year’s presidential contest, specifically, the possibility of electing an African American to the office, this may not determine the outcome of the election. (I dare not try to predict the victor in November. I have almost always gotten it wrong, perhaps because I am not really in tune with the American voters. It is safe to say, however, that it is the Democrats’ election to lose.)

Even if Republican John McCain were to prevail over the Democratic candidate in November, one of the key planks of the current conservative program in the United States, and of the Republican party more broadly, will be seriously damaged. Indeed, it already has been. I am referring to the insistence that the “market” and the capitalist system as a whole function best when they are allowed to operate freely. It should now be apparent that left to itself, the economy does not always do well; while at the moment, the question is not whether the government should intervene in the economy, but how much and in what ways. Clearly, some form of government action is needed. In fact, the recent actions of the Federal Reserve Bank, occurring (ironically) during a Republican administration, represent a historically significant increase in the power and role of what is basically the US government’s central bank.

The economic situation also makes it likely that demands will rise for serious measures to address the long-standing issues facing the country. When the economy is growing rapidly, and everybody, or at least most people, appear to be prospering or likely to prosper in the future, it is easy to sweep problems under the rug. Eventually, the explicit or implicit argument goes, economic prosperity will take care of everything and everybody. In today’s economic climate, that kind of talk rings hollow. People are going to start asking, with increasing vehemence, questions like the following: What are we going to do about Social Security, about the health care system, about the schools, about the highways, airports, public transit, etc., about the millions of people who have lost their homes or are

and increasing unemployment or underemployment (people employed but not earning enough to meet their expenses). In addition, given the continued decline in home prices, many more people will lose their homes, while they and others will be pushed downward, toward and under the poverty line. Meanwhile, the long-term problems of the economy, including the decayed infrastructure and the tremendous indebtedness, will continue to mount.

At the same time, the environmental crisis will increasingly have directly economic effects. We are already seeing this in rising food prices, not counting the cyclone (hurricane) that swamped southern Myanmar (Burma) and the Hurricane Katrina disaster of several years ago, possibly caused or made worse by global warming, and the flooding in the Mississippi Valley. To address the growing environmental problems will require increasing amounts of economic resources, which will not be available for other uses. While this may result in the development of new technology and new sectors of the economy, it will also weigh on economic growth as a whole, increasing the risk of stagnation.

Whatever precisely happens, the overall economic situation is likely to have an impact on the political scene in the country. Normally, the responsibility for economic conditions is placed on the sitting president and his political party, even though their policies, in fact, have little to do with determining those conditions. Thus, Ronald Reagan was credited with the expansion of the 1980s, while George H. W. Bush was blamed for the ensuing recession. Bill Clinton was considered a genius for supposedly overseeing the longest economic expansion in the country's history, while avoiding being blamed for the downturn that followed. (That, it turned out, didn't help Democratic presidential candidate Al Gore enough to win the 2000 election.) I think it likely that the current economic crisis will be blamed on George W. Bush and the Republicans more broadly.

governments, nor the unfunded liabilities of Social Security, Medicare, and Medicaid) is nearing \$10 trillion.) While all this has happened, the once overwhelmingly dominant position of US imperialism in the global economy has been eroded.

As all speculative bubbles eventually do, the most recent one burst, and the fictitious capital, represented by the inflated home prices and the billions of dollars of mortgage-based securities, began to be liquidated. Beginning in August of last year, homeowners who had bought their homes through questionable mortgages began to default (fail to meet their payments), houses began to be repossessed, and, as a result, housing prices ceased their decades-long rise and started to decline.

As these developments occurred, the holders of the mortgage-based securities began to demand higher interest rates to offset the increasing risk of default. And this, to make a complicated story less so (hopefully), led to a drastic "credit crunch," as various banks and other lenders panicked and essentially refused to extend credit to anybody on any terms. Consumers also got scared, as they saw their assets shrinking, and cut back their spending. (Consumer spending accounts for about two-thirds of the economy.) Meanwhile, the prices of stocks dropped dramatically and the economy slowed to a crawl.

Fortunately, the Federal Reserve Bank acted quickly to cut interest rates and to extend credit to the investment banks (including financing the buy-out of the cash-strapped Bear Stearns investment bank). This tended to calm the fears of both investors and consumers, at least temporarily. Meanwhile, stock prices, which started to drop in November and continued to fall through the first three months of this year, seemed to bottom out in March and turn up afterward. However, the stock market has remained extremely volatile and stock prices have recently dropped below the level reached in March. (Stock prices, which broadly reflect investor confidence, tend to lead the economy by several months.) Although the Fed's

intervention may well have prevented a financial meltdown, it did not forestall an economic slowdown.

Up to now, the actual decline in economic activity has not been great. (Nationally, less than 600,000 jobs have been lost, far less than in most of the other post-World War II recessions.) Although the housing sector is shrinking rapidly (and will likely continue to do so for some time), there have not yet been massive layoffs in other sectors, and it is possible that the economy may stabilize at or not too far below its present level. (This seems to have been a pattern of the last two recessions—this one and the one in 2000–2001—so much so that some economists have come up with a new economic category, the so-called “modern recession.”) On the other hand, the decline may continue for some time, perhaps leading to a severe recession in the US and a global slowdown, if not an outright contraction. Recent developments, such as increases in unemployment, continued volatility in the financial sector, and a collapse in the level of consumer confidence, suggest that this may be happening now. Moreover, home prices, however much they have already fallen, are still far above historic levels. They will mostly likely continue to decline for some time, as the banks write off billions of dollars of bad loans. (As of this writing, the banks have written off over \$300 billion; some experts predict that this figure will top \$1 trillion).

Even if we avoid a deep recession, economic problems, including inflation, will continue. We have already seen a rapid rise in the price of oil. This is in part caused by speculation (investors buying and selling oil-based securities for short-term gains), but it is also the result of a combination of other factors, including the increased demand of newly industrialized countries, the filling of various countries’ strategic petroleum reserves, production cutbacks by a number of foreign oil producers, and a global slowdown in oil exploration over the last period. Food prices have also shot up, impelled in part by the

fact that many previous countries that once exported food are now, because of their industrialization (their people can afford to buy more food), no longer doing so or are even importing food, by speculation in foodstuffs, and by the diversion of agricultural resources to the cultivation of ethanol and other bio-fuels. While the rate of increase may slow as speculators move out of commodities and into other areas, the underlying pressures are still inflationary, as the high price of oil, which is used in the production of many other commodities, will make its way to and through the rest of the economy. To these will be added the impact of the currently low interest rates, the Fed’s considerable expansion of credit, and, equally important, the declining value of the dollar (which will tend to raise the prices of imported goods). So, what is likely for the foreseeable future is some kind of recession, perhaps quite severe, followed by a period of very slow economic growth coupled with inflation, somewhat like the stagflation of the 1970s.

This will put the Federal Reserve Bank in a quandary, particularly as the economy bottoms out and starts to recover, since while the bank might like to keep interest rates low and credit easily available in order to boost the economic activity, it runs the risk of fueling inflation if it does so. On the other hand, if it keeps interest rates too high in the interests of keeping a lid on inflation, it may choke off or at least hamper an economic recovery. The federal government’s budget deficit puts it in a similar bind. Cutting the deficit will mean raising taxes and/or cutting back on government programs, either of which will dampen economic growth. On the other hand, allowing it to grow, which means more borrowing, will tend to increase inflation. The role of the dollar as an international reserve currency will also limit the Fed’s ability to act, since a rapidly depreciating dollar will wreak havoc with the global monetary and financial system.

One of the effects of this entire situation will be to lower the living standards of millions of people by cutting real incomes