<u>US Balance of Payments Problem</u>

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The USA had emerged from WWII victorious and imposed its own financial order through the Bretton Woods Agreement in 1944. The dollar was to be the global currency peg and with it the USA prospered as its 'empire' grew with a positive BoP (Balance of Paymets) exporting its surplus capital for foreign influence. This was all put into reverse after the dollar was removed from the gold peg in 1971. This could be considered the date when sound money disappeared and with it the start of a modern era of globalisation where the self-interest of nationhood was being undermined.

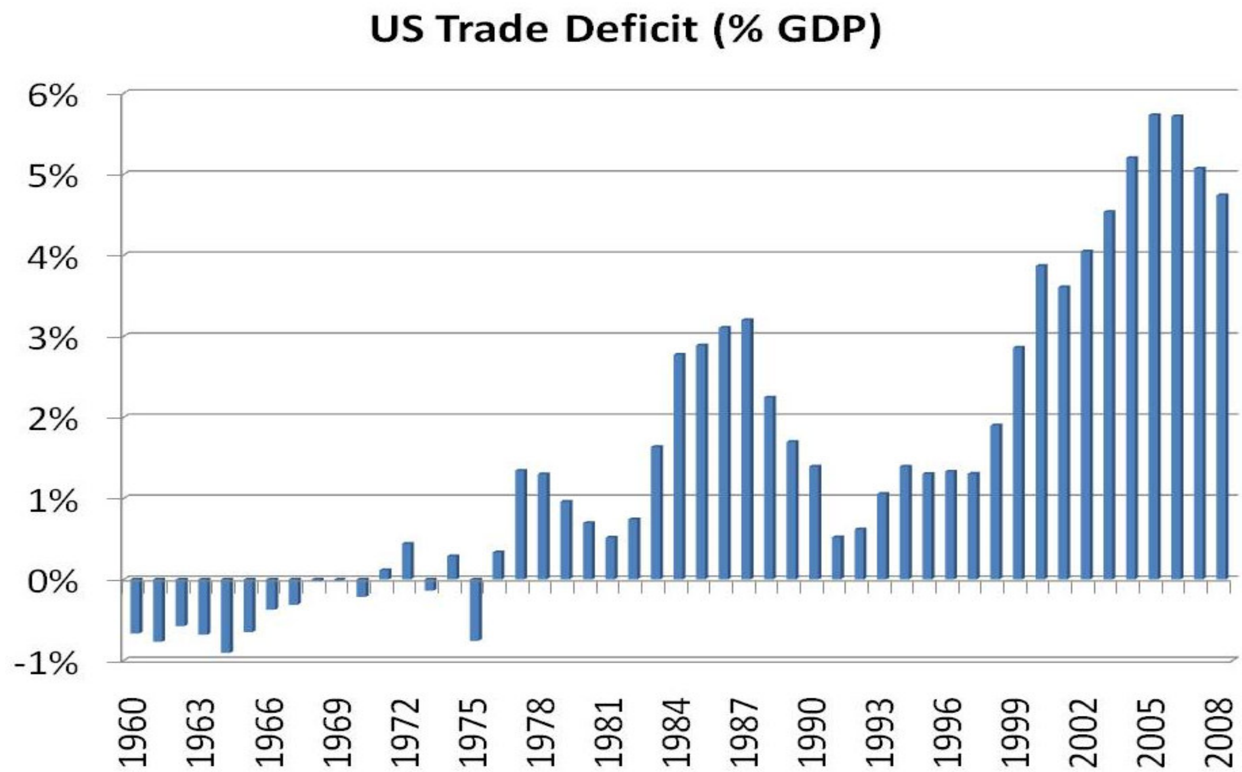
As a Merchant Navy Officer I recall being in the US in the 1970s when the US had been humiliated post Vietnam war. There were many dysfunctional Vietnam veterans who were traumatised and the US was in the doldrums – in Portland Maine there were soup kitchens. Ayatollah Khomeini had easily deposed the US sponsored Shah of Iran and further embarrassment was piled on the US with a failed attempt to rescue its Tehran Embassy hostages.

Along came President Ronald Reagan and a special relationship developed with the arrival of Margaret Thatcher in the UK. It is by no coincidence that financialization took off in this period to boost the US economy and bring back a feel good factor. However, it was all to be at the price of destroying the real economy and replacing it with a global financial order that cared not for the nation state.

The graph below clearly shows the post 1971 period leading up to the financial crisis of 2007/8 where there was an unsustainable BoP problem for the US. Instead of addressing this problem successive administrations – both Democrat and Republican compounded the problem with deregulation and President Clinton made the greatest error by repealing the 'Glass-Steagal' Act which then allowed retail banks to engage in proprietary trading.

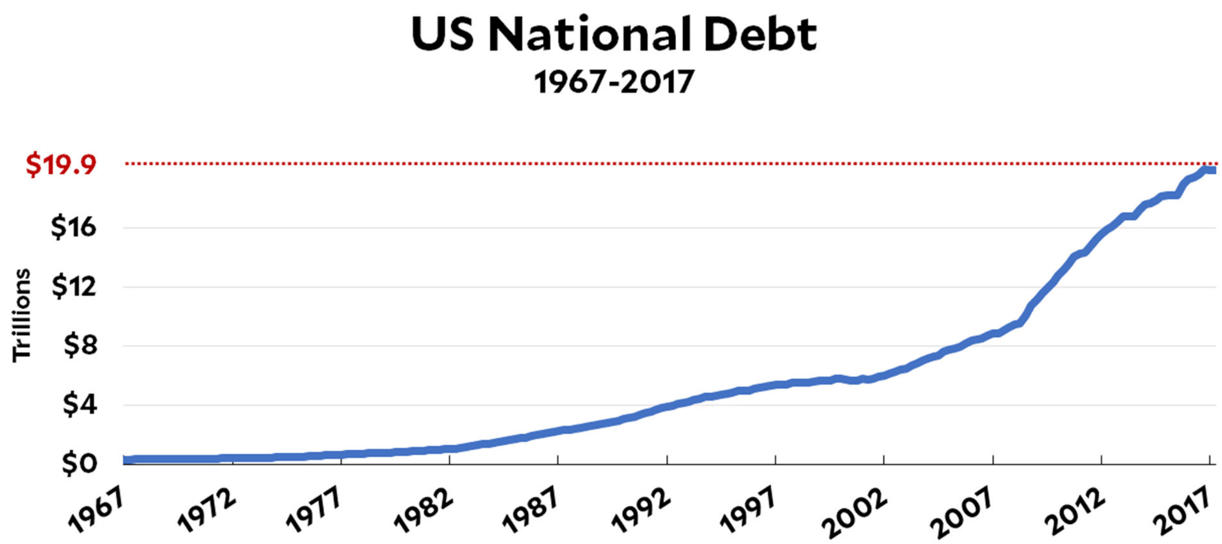
The defeat of the Soviet Communist system with the symbolic collapse of the Berlin Wall allowed Western politicians to feel vindicated in this new global financial order but by removing countries from the Soviet prison they had enslaved the rest of the

West in a financial prison. The BoP for the US and with it the real economy was sacrificed for this new global order.



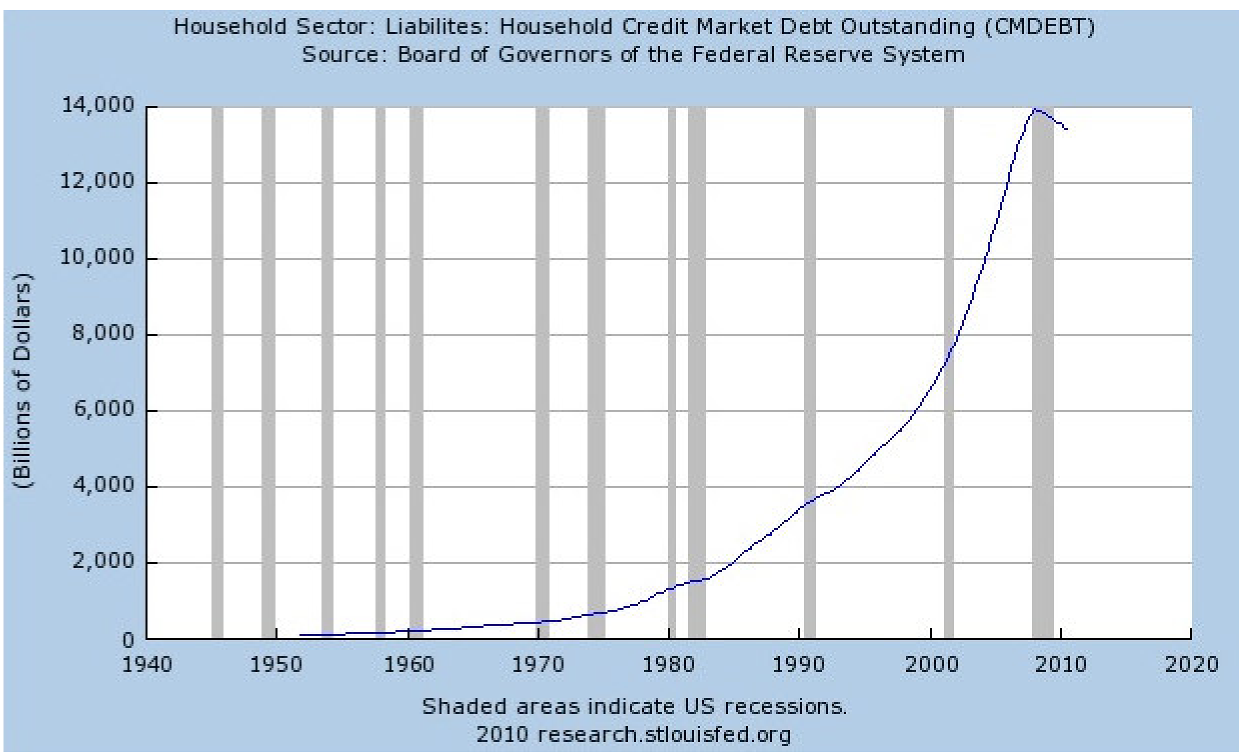
With this new global financial order free of capital controls, corporates and wealthy individuals could move their capital for maximum return; this inevitably was at the expense of investment on infrastructure and jobs within the USA. The US Government with dollar hegemony was able to finance a large military complex , limited welfare and national spending by borrowing in its own reserve currency. The graph below clearly shows the US Govt debt growing post 1971.

Whatever ones view of President Donald Trump as a person he has certainly woken up to the BoP problem and that will inevitably require painful adjustment as the US tries to claw back trade and move towards a more mercantilist approach. The debt below is still growing and is about £21trn as of 2018. Whilst much of this is held by US nationals the growing cost of servicing it will conflict with the need to invest in the real US economy to allow it to rely less on imported goods.



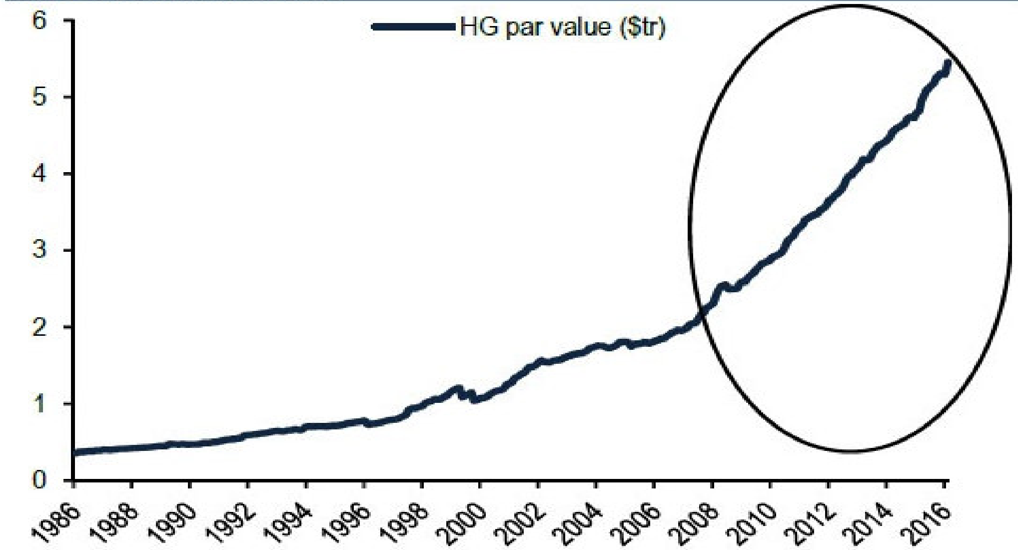
Source: Treasury Department via FRED

Similarly to the UK there is a huge level of household debt, student debt and car loans . The graphs below show how these as part of total household debt have been ramped up in recent years.



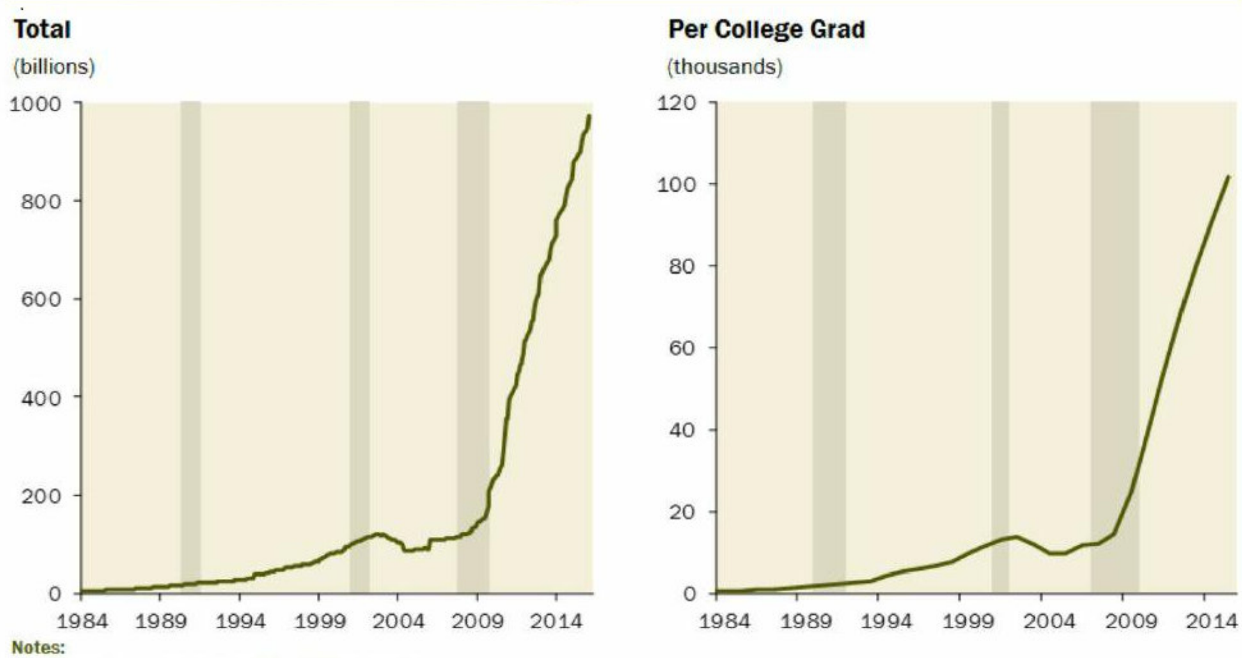
Corporate debt has also grown substantially since the last financial crisis as the Federal Reserve has engaged in QE (Quantitative Easing) to help keep interest rates below normal for several years. This has enabled corporates to buy back their own stock and therefore pushing up share price and remuneration for executives.

Figure 1: US HG corporate bond market has more than doubled in size since the financial crisis



Source: BofA Merrill Lynch Global Research

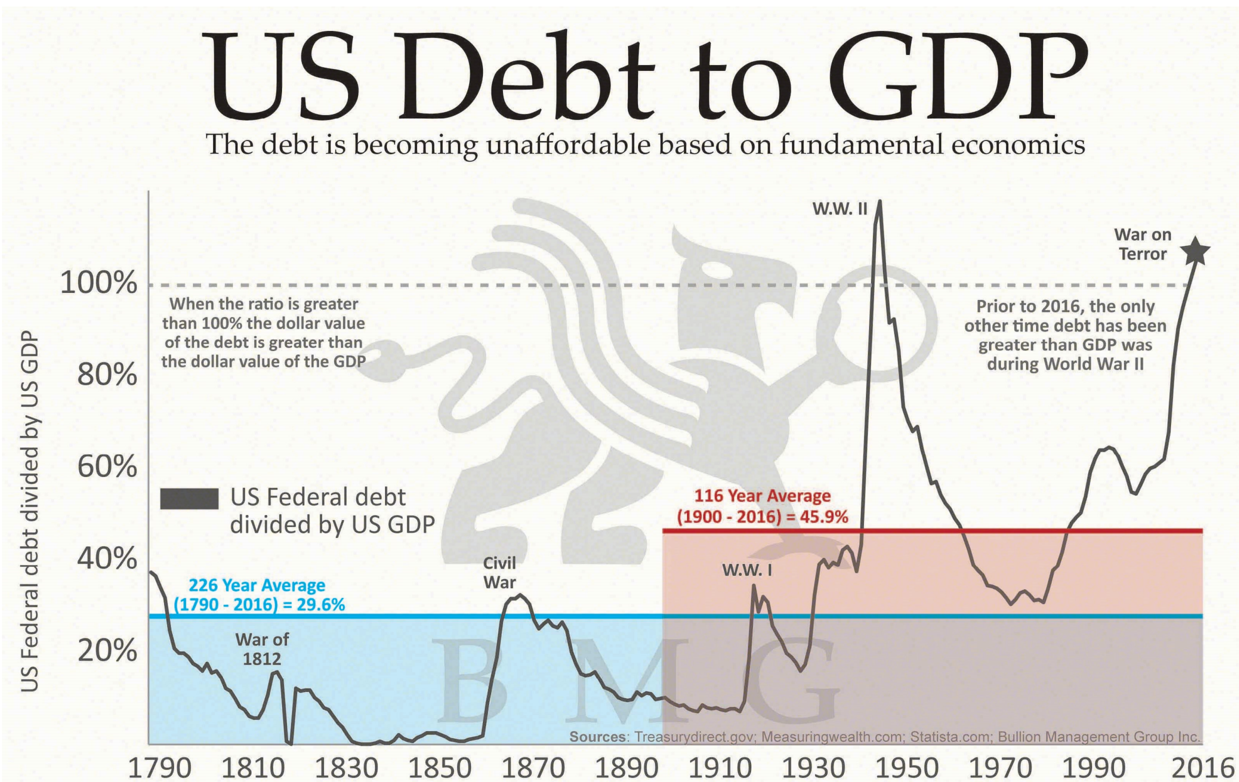
United States: Student Loans Outstanding



Notes:
Shaded regions represent periods of U.S. recession
Source: Haver Analytics, Gluskin Sheff

The corporate debt above is HG ('High Grade') and doesn't include other lower grade banking loans. You can also see student debt climbing as Universities become more like corporate businesses and motivated for profit rather than outcomes.

The graph below shows how the US Govt debt is now at a dangerous level and still growing. If you add household and total corporate date the US has debt levels well in excess of 300% GDP.



There is no easy solution to the debt problem but by correcting the trade deficit the US will help protect itself from future currency fluctuations and reliance on imports.