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Trumponomics and the developing world

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So now we know: unlike many other politicians, President Trump will indeed do (or try to do) many of the things he promised or threatened to do before he was elected. Internally, he is apparently seeking to bring back a 21st-century version of Reaganomics: a combination of rising fiscal deficits resulting from lower taxes (especially on the rich) and more public spending on the military and on physical infrastructure, with higher interest rates delivered by the US Federal Reserve. He will deregulate private activity further and reduce various protections for labour and the environment that he believes constrain investment. He sought (unsuccessfully) to replace the Affordable Care Act or Obamacare, albeit with little clarity on what to replace it with, and seeks to reduce public spending on various social programmes. All this is supposed to create a domestic boom led by private investment, that is presumably to be financed once again by foreigners willing to pour their savings into US financial assets, particularly Treasury Bills. And some have predicted that such a US boom will once again pull the world economy along through the increased demand it will generate for the rest of the world's exports.

Externally, he has already moved the US out of some committed trade deals like the Trans Pacific Partnership and showed a propensity to undermine the World Trade Organisation if it does not work in a way that he perceives to serve US interests. His administration is already promising protectionist measures and looking at ways to impose unilateral sanctions against other WTO members. He is seeking to reduce immigration by deporting some who have already made it inside the US, and to place significant curbs on future immigration as well as on short-term movement for service delivery, through H1-B visas. He will try to build a wall on the Mexican border and raise tariffs on imports coming from other countries: most symbolically Mexico and China, but also potentially developing countries in general. He will reduce US spending on and engagement with international organisations like the United Nations and probably ignore US pledges and commitments to treaties that seek to address global warming and related issues.

His foreign policy is at present a confused mixture of aggressive bullying and personal support for other aggressive bullies elsewhere, but it is safe to assume that ultimately there will be more continuity than real change in this matter. Given the complete mess that US foreign policy has created in the world over the last few decades, that continuity is not necessarily very good for the rest of the world. Such change as does occur is likely to be adverse for progressive people in his country and across the world: it is not just Palestinians and those fighting against authoritarianism in Turkey, Egypt, India and the Philippines who have cause for worry, but people everywhere who are concerned about preserving and enlarging democratic rights. If there is one agenda that is now much more likely to be trampled upon globally, it is that of human rights.

But how much of this agenda can Mr Trump actually achieve? And how much of this is self-contradictory, in that movement in one direction will generate changes that affect other parts of the agenda or the goals? The declarations sound disruptive, but how much difference will all this sound and fury make in material terms? The answers to these questions are crucial not only for citizens of the US. They matter hugely for the rest of the world and developing countries in particular, because the US economy still remains dominant and affects global demand directly and indirectly, and because the continuing significance of the US dollar as the main global reserve currency affects both financial and real flows across countries.

It is probably over-optimistic and even misplaced to believe belief that Trumponomics can generate a boom in the US and thereby in the rest of the world, along the same lines as the Reagan boom. It is not just that the world economy is different from three and a half decades ago and that global capitalism has altered in significant ways; it is also that much of what he proposes is unlikely to work out as planned, given the political economy forces in the USA at the moment and the contradictory nature of the various impulses in his administration.

It is not just the failure of his attempt at health reform that generates more scepticism about any future possible successes. It is also the internal contradictions in his policy proposals. Consider the issue of whether President Trump will actually deliver in terms of generating a new boom with sustained medium-term growth of activity and employment. The basis for this is supposed to be the perception that increased public spending and lower tax rates will provide a fiscal stimulus to boost the economy, even if it does at the same time increase inequality and disproportionately favour the rich. But the second outcome is far more likely than the first. As of now, the precise tax proposals that the Trump administration itself favours are not known; but the version being pushed by the Republicans in Congress led by Paul Ryan is supposedly “revenue neutral”, in that it balances tax cuts in some sectors and categories with reduction of deductions in the same or others. The overall macroeconomic benefit of this would obviously be limited, although it may well imply a further redistributive shift away from working and middle class families in favour of the country’s corporations and rich individuals.

In any case, tax cuts alone are known to have limited impact – even the IMF has recently estimated that the multiplier effects of tax cuts generally tend to be much lower than increased public spending, regardless of the beneficiaries of such cuts. Reagan’s strategy “worked” in the 1980s because of the massive increases in military spending that generated new investment by the military-industrial complex, which in turn had spillover effects in other sectors and in terms of technological change. But it is not at all clear that Mr Trump is actually planning such significant increases in government expenditure. The big increases in military spending in his proposed budget are counterbalanced by equivalent cuts in other spending, particularly spending on social programmes. And even these increases may be diminished by the Congressional process.

Much of what Trump has talked about as public investment actually comes in the category of “Public Private Partnerships” (PPPs), in which the government does not invest directly, but underwrites a significant part of the private investment or enables the securing of cheap loans for private investment. There is good reason why this strategy has had such a bad press recently: most countries that have relied heavily on it have found that the actual levels of investment turn out to be much lower than anticipated or planned for, while the fiscal costs tend to be much higher and more prolonged, because the user charges that would cover costs typically turn out to be so high that they are politically impossible to enforce. In other words, these PPPs in most cases have not delivered in terms of actually providing the required physical infrastructure. So a heavy reliance on PPPs may suit several of Mr Trump's cronies and those (including in real estate, a sector of particular personal interest to the US President) who would benefit from certain infrastructure investments, but they are unlikely to generate the kind of increase in investment rates that is being apparently being anticipated by the over-enthusiastic stock markets.

In any case, another political reality that President Trump will have to contend with is the continued presence of the Tea Party as a major lobby affecting both Congress and government functioning. In a peculiar way, the Republicans now seem to have tied their own hands because of the political predilections they created when in opposition. This group is so viscerally opposed to any increases in deficits that any real change in fiscal stance towards a more expansionary role would have to be achieved through subterfuge, if at all it is to occur. This political constraint has not appeared so clearly yet, but it definitely still exists, especially as so many Republican Senators and Representatives have been elected on precisely such a platform.

So the fiscal expansion that has been so eagerly anticipated (not just in the US but even globally) on the basis of the declarations of the US President is not likely to be all that significant. And it will come in combination with a monetary policy "shock" in the form of higher interest rates, in an economy that has grown used to near-zero interest rates for nearly a decade now. This could well attract mobile capital back to the US – and thereby cause different degrees of discomfort or crisis in many emerging markets – but that in turn will cause an appreciation of the US dollar, which too must affect profitability in the tradeables sector. In purely macroeconomic terms, it is hard to see how this combination can deliver significantly higher economic growth or employment.

What then of the other strategies, the physical and trade walls both designed to protect US residents from the depredations of foreigners? The infamous wall along the Mexican border has already overrun cost expectations even before work on it has started, from Trump's original estimate of $10 billion to around $15-20 billion or even more now. But while that may seem expensive for an ugly and offensive piece of landscaping, if it is seen only as a Keynesian stimulus, it would not amount to very much. And the economic effects of that spending for the US would in any case be questionable, since reports suggest that Mexican workers (both legal and illegal) are far more likely to be employed in the work of building it.

The other wall – the imposition of high punitive tariffs on goods coming from Mexico and China, as well as from other countries seen as "threats" to US production – may well get a few dramatic and highly symbolic gestures in its direction, and may mess up trade relations for a while. How serious and sustained this attempt at protectionist nationalism in trade terms will be is not yet clear, but certainly it will be less emphatic than the cronyism that is already so evident. It is more than likely that the President's basic and well-known instinct for pushing business and profit, irrespective of the impact on workers or consumers, will win over the protectionist rhetoric that helped him get elected. In any case, punitive tariffs against one set of countries would simply divert trade rather than generate local production. Wider protection, sufficient to really alter the trade balance, is not really on the cards. But for well-known reasons, it would do very little to bring manufacturing jobs "back" to the US, and technological changes will continue to erode the employment possibilities of such production at an ever-increasing pace. So the workers and other non-traditional voters who installed Trump in his current position are unlikely to get even some of the benefits they expect, regardless of statements to the contrary. Instead, they are more likely to experience a worsening of material conditions because of spending cuts and other changes in institutional conditions that reduce their entitlements.

Mr Trump's policy stance will, however, mean that the United States – which has been providing less and less of a positive demand stimulus to the rest of the world economy ever since the Global Financial crisis – will continue to shrink its import demand and add to the forces that are making global trade decelerate and even decline.

What does all this mean for developing countries? First, that those who are worried are right to be worried, but perhaps not for the reasons most commonly cited, such as the threat of trade protectionism. Rather, Mr Trump presents a disruptive force in an already febrile and volatile global economic environment, which is weakened not by his election, but because global capitalism had clearly reached the limits of pushing that particular strategy of accumulation. This was increasingly evident in the "secular stagnation" that seemed impervious to massive injections of liquidity and near zero or even negative interest rates, and in economic trajectories that no longer seem to generate stable and regular employment. In turn, the disruption that Mr Trump generates in turn is only partly because of his actions, and probably even more because of the very impact that his statements and the surrounding chatter have on expectations, both in financial markets and in real economic activities.

The most immediate likely concern is that of capital leaving emerging markets once US interest rates are raised, and the potentially disorderly situations this can create. Developing countries have already experienced this several times in the past decade, and have learnt the hard way that policy decisions taken and economic processes in the US are far more significant in determining capital inflows and outflows from their own countries than any measures taken within. The resulting volatility is likely to be compounded by further financial deregulation that will spread from the US to other countries. Since the already inadequate re-regulation of finance that occurred after 2008 in the US is on its way to being dismantled, this will create pressures for associated deregulation even in other developed countries, and add to similar tendencies in emerging markets. This is doubly dangerous for many "emerging markets" because many of them had responded to the global crisis by allowing massively leveraged expansion, and much of that is currently in the process of winding down. Asset markets – particularly of land and real estate – are experiencing a downswing in most countries, rendering them especially vulnerable to financial crises that could originate from an initial outflow of capital to the US.

Obviously, this would be exacerbated by the disruptive impact on global trade that several proposals of the Trump administration are likely to have. The ongoing slowdown in international trade is likely to get worse, and also more uncertain with the unpredictability of US moves. Conflicting signals coming from different elements of the US Government, and even from its leader over time, only add to confusion and reduce the incentive for even medium terms investment in tradeable sectors. Export of commodities from South to North, which powered the expansion of some economies and provided much cheaper goods to consumers in the North, is unlikely to be an engine of growth in the immediate future. This sounds like bad news for many developing countries, and will be so in the short term, but it need not be so bad if it forces a different approach from one that focusses on exports to the North (and therefore treats wages only as a cost), to one that looks at potential in domestic markets and regional arrangements (and therefore treats wages also as an important source of demand).

Certainly, no tears should be shed for the Trans Pacific Partnership. It was a bad deal, that did little to enhance desirable trade; instead it provided inordinate power to corporations, through stringent and unwarranted acceptance of tight intellectual property rights monopolies, reducing possibilities of public regulation in the interests of workers, the environment and the health and other human rights of citizens; and allowing investor-state dispute settlement in wide-ranging cases. These would definitely have harmed workers and consumers in all the member countries. Developing countries that had put so many eggs into that particular basket will now be forced to think more creatively about both trade and policy options, which would not be an adverse outcome. The danger is that – despite the breakdown of this agreement – such deregulation and greater power to corporations will be granted anyway by the Trump administration, and sheer competitive pressure will then force governments across the world to fall in line. Avoiding this worst-of-all-worlds scenario will require constant public vigilance and mobilisation in all countries.

Similarly, financial markets will definitely be more unstable and volatile, and countries across the world may well have to brace themselves for another round of financial crises. This time, the implications may be worse because of the difficulty of using the same old solutions of large publicly funded bailouts to rescue banks and other financial institutions. The global race to environmental destruction pushed by further deregulation in the US and egged on by international competition in trade and investment, will also have to fought with public pressure in all countries.

Another concern for developing economies comes not from the economic policies of the Trump administration but from its foreign policies. Clearly, those who in the period prior to the election had seen Hillary Clinton as a greater threat to global security than Trump because of the extreme hawkish position on Russia had got it wrong. President Trump has assembled some of the most hawkish of military characters in his team, including those who were proponents of the Karl Rove version of "the new American century" under George Bush, and has already engaged in one military operation (however botched) and proposed others in the Middle East. His attitude to Russia may be confused, but that to China is more definitively aggressive. Global conflagrations need not start with direct engagements between the great powers; rather through history they have begun with more minor conflicts that explode out of proportion as the big powers get drawn in. Such possibilities are hugely possible with this US administration, and once again the danger for developing countries is that the wars will be fought on our territories and between our peoples. The propagation by the current US government of a sullen, petty-minded pseudo-nationalism is already finding echoes in too many other governments, including in the developing world where this attitude also similarly involves the suppression of any kind of domestic dissent. This is not just bad for internationalist co-operation and for democratic space within countries: it also affects economic flows and processes between countries and therefore within them.

So is it all bad news, with the gloom and doom justified? Not entirely. Periods of disruption are unpleasant and do throw up all sorts of outcomes, often mostly bad. But they are all periods when the older certainties are thrown aside, and some of these deserve to be discarded. The belief in "free" trade and globalised capital being all that is required for development was always wrong, but now it simply cannot be entertained. This must force more creative thinking about economic strategies in different parts of the world. Such thinking about economic strategies will have to come out of both the intellectual and the institutional straitjackets into which they had been put over the past decades. The confusion and disarray in the multilateral economic organisations that will definitely come about during this US administration and the resulting free-for-all in global economic architecture are certainly likely to reduce the possibilities of international co-operation significantly. But they may also open up policy spaces for developing countries seeking to change their position in the international division of labour, and generate more possibilities for autonomous industrialisation and development. This is not going to be easy, and obviously requires changing political economy configurations in many countries – but then, through history, the various paths to progress have never run smooth.

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