The Price of Empire – On "Trade Wars Are Class Wars"

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On *Trade Wars Are Class Wars: How Rising Inequality Distorts the Global Economy and Threatens International Peace* by Matthew C. Klein and Michael Pettis. Yale University Press, 2020, 288 pp.

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A few years before the global financial crisis of 2008, future Federal Reserve Chairman Ben Bernanke popularized the notion that the world was divided into trade surplus countries like China and trade deficit countries like the United States. Echoing John Maynard Keynes's trade destabilization theory, Bernanke argued that this imbalance was a significant cause of global instability. But whereas Keynes saw instability as a normal product of global trade, the effects of which would be mitigated by international financial agreements putting limits on surpluses and deficits, Bernanke laid the blame squarely at the doorstep of the East Asian and German economies.

Matthew C. Klein and Michael Pettis, co-authors of *Trade Wars Are Class Wars*, are cut from the same Keynesian cloth as Bernanke. Like him, they hold the surplus countries mostly responsible.

Klein and Pettis are not simply recycling Keynes and Bernanke, however. Their key contribution is showing that there is a strong basis for working-class solidarity across borders, because workers in both surplus and deficit countries are exploited by their state-capitalist or private-capitalist classes. The problem is that while they proclaim their adherence to the class perspective, Klein and Pettis often lapse into the national viewpoint.

They see part of the problem emanating from the United States—from Wall Street, job-exporting U.S. transnational corporations (TNCs), and national security and economic bureaucrats in Washington. In their telling, however, these actors come across mainly as accomplices of surplus-country elites who want the United States to absorb their surplus production.

The main villains in Trade Wars are Chinese state capitalists and the German-led European corporate class. They grossly underpay their workers, which makes it impossible for them to purchase the goods they turn out. Instead, surplus country capitalists ship their products to the United States. They then use the dollar reserves derived from the super-profits racked up from selling goods to American consumers to buy U.S. debt instruments, like Treasury bills or mortgage-backed securities. The international demand for high-yield U.S. assets pushes Wall Street to produce the increasingly complex financial products that Warren Buffett famously labeled "weapons of mass destruction," and thus destabilizes the U.S. financial system.

Who Is To Blame?

This narrative may be attractive for some American readers, but it is not convincing. For instance, the claim that Wall Street's hyper-speculative activity has been mainly a response to the surplus countries' demand for complex financial products is historically inaccurate. The creation of subprime and other mortgage-based securities long preceded the emergence of surplus country demand in the mid-2000s. These products of financial engineering became widespread in the late 1980s as a response to demand from U.S. investors for high-yielding assets and derivatives in the face of declining profitability of investment in the real economy. As sociologist Colin Crouch has pointed out, U.S. financial institutions and the Treasury also encouraged increasing levels of debt to make up for the stagnation of real wages—that is, as an instrument of class pacification, and to keep the consumption machine going. U.S. mortgage debt rose from $2.4 trillion in 1990 to $4.8 trillion in 2000 and $7.8 trillion in 2004. When foreign sovereign wealth funds began purchasing a critical mass of debt instruments in the mid-2000s, they were following a well-trodden speculative path carved out by U.S. investors, which culminated in the 2008 global financial crisis.

The "imperial center as victim" scenario is also vulnerable to the criticism that former World Bank chief economist Justin Yifu Lin leveled at Bernanke: the United States was not a passive receptacle for Asian funds. On the contrary, the latter were being pulled in by the dynamics of the financialized U.S. economy and Washington's interventionist military adventures. It is worth quoting Lin in full:

"The combination in the United States of financial deregulation (starting in the 1980s), which allowed higher leverage, and low interest rates (following the bursting of the dot-com bubble in 2001) led to a large increase in liquidity, which fed the housing bubble. The wealth effect from the housing bubble and innovative financial instruments supported excessive household consumption. The consumption surge and the fiscal deficits needed to finance the wars in Iraq and Afghanistan generated large US trade deficits and global imbalances. The United States was able to maintain these severe imbalances for as long as it did because of the dollar's reserve currency status."

When it comes to the book's core concern—trade—in Klein and Pettis's telling, American TNCs have been part of the problem, but it is China that is mainly to blame for the grave trade imbalance that resulted in massive U.S. job losses. TNCs simply could not refuse the Chinese offer of a low-wage labor force. But setting up "runaway shops"—industrial plants relocated to avoid unionized workforces—in Mexico, Southeast Asia, and within the United States itself has been a fixture of U.S. corporate strategy since the early 1970s, long before China became a provider of cheap industrial labor. Exporting jobs to developing countries was one element of the push by U.S. elites to end the compromise between capital and labor in the interest of greater profitability. Chinese workers were simply the U.S. corporate class's latest and most attractive pawn in this broader strategy. Indeed, the "China price difference" became the central element in U.S. TNCs' competitive moves. In this symbiotic relationship, the Chinese state's concern was principally to use cheap labor for developmental objectives; the U.S. corporations' objective, on the other hand, was purely exploitative.

Indeed, this passive image of U.S. TNCs is out of sync with the authors' own portrayal of dynamic American corporations aggressively setting up global supply chains. Companies chose the location of manufacturing and sales operations based on how tax regimes, transport costs, and wage costs would affect overall profitability. Klein and Pettis's discussion of how the technology of containerization facilitated the globalization of the U.S. supply chains is one of the most informative sections in the book.

Apple is the paradigmatic TNC in the era of neoliberal globalization. It set up assembly operations via subcontractors in low-wage China and subsidiaries in low-tax countries like Ireland. Production in a special economic zone in China allows Apple subcontractor Foxconn to import components without paying Chinese tariffs. Even more important, the special economic zone "lets Apple buy the finished phones from Foxconn before they have technically entered China, sell those phones to subsidiaries based in corporate tax havens such as Ireland, and then let those subsidiaries sell the iPhones to the rest of the world after adding its hefty profit margin," Klein and Pettis write. This carefully constructed "value chain" allows Apple "to book the bulk of its profits in countries where it pays the least tax even though the phones are shipped from Chinese ports."

In their broader discussion of trade, Klein and Pettis deploy a narrowly economistic approach that ignores the larger context of imperial hegemony exercised by the United States. To them, Washington favoring Asian producers with benign trade relations was a mistake. However, to exercise its hegemonic leadership in the fight against communism in East Asia, the "hot zone" of the Cold War, the United States had to make certain concessions. Allowing first Japan, then South Korea, and later the Southeast Asian "tiger cubs" to maintain highly protected markets while giving them easy access to the U.S. market was part of an imperial deal, for which the United States in turn received military alliances and recognition of its political leadership. China, though Communist, was also absorbed as an ally in the imperial system following Nixon's visit to Beijing in 1972, in order to isolate the Soviet Union.

U.S. political and economic elites were not victims of China and Germany, owing to some iron imperative that some country must play the role of a deficit economy in order to absorb the products of surplus economies. They were engaged in the complex balancing act demanded by the exigencies of maintaining global hegemony. To say that the United States is the "largest single victim" of the surplus economies falls into the false Trumpian characterization of America's allies as taking advantage of a relationship from which the United States derives no economic, military, or political benefits. It also unwittingly perpetuates the knee-jerk "America First" response to economic crisis that has drawn many working- and middle-class Americans to Trump.

An Alternative Framework

Klein and Pettis's focus on a mechanistic relationship among national economies highlights the limitations of a Keynesian trade surplus/deficit paradigm. It is a perspective that even the most class-conscious analysts find difficult to avoid. What is missing is a more comprehensive theoretical framework that would enable us to understand the dynamics of the contemporary international capitalist economy.

Capitalism is an unstable system, which staggers from one crisis of profitability to another in its drive to accumulate capital. Trade relations are an epiphenomenon of this system. To understand the current role of China, it might be useful to return to Rosa Luxemburg's insight that pre-capitalist or non-capitalist societies are integrated into the system to counteract the decline in the rate of profit by providing an arena for the extraction of super-profits. From this perspective, surplus economies are simply new centers of accumulation in a system where disequilibrium is the normal state of affairs, sometimes mitigated by interventionist reform measures by the state.

Just as Klein and Pettis's surplus/deficit paradigm is inadequate to grasp the dynamics of the international economy, it also falls short as a reform strategy in the era of climate change.

They call for the surplus countries to undertake significant income redistribution to create local demand to absorb their surplus commodities. "Rising consumption would encourage businesses to invest in additional productive capacity to meet demand," they write. "Transferring income to ordinary households would therefore result in both more consumption and more investment. Redistribution, in this case, would lead to higher output."

While redistributing income and wealth is vital, having this take the form of rising consumption in order to trigger additional productive capacity is a big problem, for this can only result in more growth that increases carbon emissions.

As many have pointed out, it is an illusion to think that GDP growth can be "decoupled" from rising carbon emissions. Degrowth, it is increasingly clear, is an imperative for overdeveloped Germany and Europe. China, the world's top carbon emitter, has already cut back its annual growth rate from 11 percent in the 2000s to 6–7 percent in the last few years. A higher growth rate would be a major setback in the effort to reduce emissions.

For the United States, Klein and Pettis propose a combination of income redistribution in the form of reducing payroll taxes, improving the social safety net, increasing government spending on physical and social infrastructure (financed by foreign financial inflows), and government-led efforts to maintain an industrial base. While the authors mention the need for investment in green energy, there is the same emphasis on demand-driven GDP growth.

The Common Challenge

Aside from its anachronistic Keynesian preoccupation with accelerating demand-driven GDP growth in an era of climate emergency, another problem with Klein and Pettis's economic reforms is that they are not anchored in a political strategy. One would have expected their insight that the working classes of trade surplus and trade deficit countries share a common interest to entail a political program to achieve desired economic reforms. What they deliver instead is phlegmatic national-technocratic management from which a class or mass base for reform is absent, much less a cross-border worker-centered program for action.

This prescriptive lacuna is understandable. The unfortunate reality is that the political agents that could have led the working classes to a cross-border unity based on a common reality of exploitation no longer have the capacity to do so. The Social Democrats in Europe and the Democrats in the United States have been compromised by their endorsement of the pro-globalization and free trade policies that destroyed communities and created so much unemployment. Klein and Pettis are right that Trump's solution of a trade war with China and Germany does not make sense, but Trump was right in making an issue about one of the key causes of working-class distress: the policies embodied in the Trans-Pacific Partnership, the North American Free Trade Agreement, the World Trade Organization, and bilateral trade pacts masterminded by U.S. corporate and political elites. Though the critique of globalization and free trade originally came from the independent left, it has been Trump in the United States and far-right parties in Europe that have harvested working-class discontent.

The work ahead is to dislodge the far right from its hold on key sectors of the working class. A progressive cross-border coalition that integrates those workers could be the basis of an alternative to both a dying neoliberalism and the rising extreme right.

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P.S.

• Dissent. Winter 2021:
https://www.dissentmagazine.org/article/the-price-of-empire

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