Following the Economic Lead of a Third World Country

The BBC reported on April 14 that one city in Egypt, Damietta, still has zero unemployment in these difficult economic times. That's surprising, but what makes this even more surprising is that the city specializes in manufacturing furniture, often high-end furniture, for export. This isn't just micro-manufacturing in a small town either. It is estimated that there are over 60,000 furniture shops in the city.

Considering that such an accomplishment is a rarity in the world nowadays, even in — especially in — a Third World country like Egypt, to what does Damietta owe its success? An excellent work ethic, high skill levels, business acumen, and a hands-off approach by government. In BBC interviews Damietta's populace made clear to the reporter that hard work is expected of all its residents; no one expects otherwise. Successive generations of furniture builders learn building techniques from their forefathers and then try to improve upon them. The residents of the city, being in the Nile Delta, have been trading throughout the settled world basically forever, and the Egyptian government, not wanting to interfere with a wealth-producing segment of society, has removed all tariffs on the area.

In the United States, the politicians are taking the opposite route, binding wealth-producing industries in an iron strait-jacket. Besides imposing the highest, or second highest, corporate tax rates in the world (depending on each state's corporate tax rate) and causing government-generated costs that account for more than 31 percent in additional manufacturing costs above our nine largest trade partners, the U.S. government is actively trying to halt U.S. wealth production.

Take the Democrats' proposed new mining law, H.R. 699, The Hardrock Mining Reclamation Act of 2009, which miners are fighting because it imposes costly new regulations on mines, even on small-scale mines that have been operated safely for years, closes off large areas of the United States to mining, and imposes royalties (taxes) on mine production, among other measures. If the politicians were simply ensuring that miners were good stewards of the land, that would be one thing, but this crosses that line by a large margin and is just another example that shows that politicians do not truly appreciate the economic mess we are in or understand what to do about it.

U.S. politicians, as we all likely know by now, believe they can spend our way to prosperity with newly created U.S. dollars. Such seemingly illogical behavior is defended by politicians (and some economists) who spout the "supply-side" economic mantra that "deficits don't matter" — that importing far more than we export doesn't matter. But though there may be an underlying bit of truth behind this mantra — if a country mines precious metals at home to mint as money in order to pay for foreign goods, trade imbalances don't really matter — supply siders have twisted this truth to the point of absurdity: they believe that the United States can print paper dollars, which have no intrinsic value (they are just bits of colored paper, after all), to pay for foreign goods, and that trade imbalances still don't matter. Likewise deficit spending doesn't matter.

But they do matter, very much.

Just as an individual's wealth or material value is determined by the goods or abilities he is in possession of that others need or covet, a country's wealth is determined by the goods or services that it can and does provide, things that people in other countries need or covet.

Because gold that has been minted into money is coveted, it has intrinsic value and people accept it as payment for goods and services. When it is traded to other countries, they do not expect more as payment at a later date for those same goods and services, and the gold money can be traded with no ill effect on a nation's economic health. U.S. paper dollars, conversely, are reluctantly accepted worldwide, in lieu of a precious commodity like gold, because the U.S. government guarantees the foreign recipients of those dollars that if they give the dollars back to us later, we will then give them goods and services. The dollars we give for goods and services, therefore, "represent" goods and services in the United States that we will give up at a later time.

U.S. dollars are intrinsically worthless, so our U.S. trade imbalances that are based on the payment of dollars must lead to an ill effect in our economy: because the paper dollars are essentially promises to provide something of value to another country in the future in return for accepting the dollars now (we're promising that in the future we will give the foreign country a product or service that they covet or need when they give the dollars back to us), the dollars quickly lose their value as they are increasingly printed because the United States has a limited supply of goods or services that we can turn over to foreigners when they give us our dollars back. If foreigners returned our dollars en masse, which is an increasingly real possibility as foreigners realize they have to return them soon in order to get anything of value for their dollars, citizens of the United States would quickly realize how poor they have become as a result of trade imbalances based on paper dollars.

Likewise, domestic spending deficits are impoverishing Americans. As the United States creates new dollars, two major things happen: the cost of goods in the United States rises because the dollars now "represent" less in the way of valuable goods and services (price inflation), and we get closer to the time when the foreigners decide to cash in their dollars for goods and services because foreigners actually temporarily take on — "buy" or give us money for — our domestic debt (U.S. government IOUs) in return for interest payments on the debt. Each day, we get closer to the time when foreign investors realize that we have issued an abundance of IOUs as compared to the amount of assets and services that we have and they want to acquire. A mass return of our dollars also becomes more likely because through creating vast amounts of dollars, we are repudiating our debt. We have promised to give foreign investors interest on the debt they "bought" from us as a reward for temporarily taking on our debt, but as we increasingly create money, the interest paid to foreigners can't keep up with price inflation, making the purchase of U.S. debt a losing proposition.

That brings us back to the beginning of the story. To generate wealth in this country and turn the economy around, we must do as Damietta in Egypt is doing; we must create goods and services that the rest of the world needs or covets. And because most service-type work will increasingly be provided by low-wage, low-living standard countries like India or China or Egypt, the U.S. government must do everything in its power to allow U.S. companies, farmers, miners, etc. to produce goods the rest of the world wants.

We cannot stake our country's future prosperity on, as President Obama, Democrats in general, and many Republicans seem to insist, massive government spending on infrastructure projects and projects aimed at living up to the slogan "reduce, reuse, recycle." Massive government spending actually reduces wealth production in the United States because it reallocates money from the private sector to the non-wealth-producing public sector, and it will fail sooner or later — in fact, it's failing now.