“Worries Rise on Size of U.S. Debt”

[This is my introduction to an article from the *New York Times* which I forwarded to friends on May 4, 2009. –S.H.]

Hi everybody,

The Federal debt is going up by leaps and bounds, and will likely increase by around $2 trillion dollars this year alone. (It has already gone up by $1 trillion over the past 6 months.) This does NOT include the many additional trillions that are supposedly only being loaned to banks and financial corporations by the Federal Reserve.

Some of the worries in the article below are just foolishness, such as the familiar bourgeois economic notion that government borrowing can “crowd out” private investment. Any *credit-worthy* business can obtain all the credit it needs. Those people with lots of money are actually desperately seeking good (and safe!) places to invest it.

But the fact is that there is a whole lot for the ruling class to worry about here. The only way the government has to prop up the economy in the present situation is to run really massive Keynesian deficits. The deficits they are running this year will probably be enough to at least halt the further economic decline for some months in the second half of this year. But if they ease off in this deficit financing next year (as they are currently planning on doing), the decline will resume. This is why it is reasonable to expect a long string of further bursts of Keynesian deficits as the effects from the previous ones peter out.

At this point the U.S. economy can only be kept from sinking into outright depression conditions by:

1) Permanently continuing the massive Keynesian deficits, and
2) Further *increasing them* as time goes on.

This cannot possibly be done indefinitely, and that is why it is correct to view this current period as being a “developing new depression”. We ain’t there yet, but we are on the road into it, and it is a road that the ruling class cannot turn off of.

This means that not only is there a new depression developing, but as part of that, there will be at some point a collapse of the U.S. currency, and extremely serious inflation. But both of these things are still down the road a ways. Perhaps y’all can see them in the distance as we careen at ever increasing speed toward them!

Scott

The New York Times

(May 4, 2009)

Worries Rise on the Size of U.S. Debt

By GRAHAM BOWLEY and JACK HEALY

The nation's debt clock is ticking faster than ever — and Wall Street is getting worried.

As the Obama administration racks up an unprecedented spending bill for bank bailouts, Detroit rescues, health care overhauls and stimulus plans, the bond market is starting to push up the cost of trillions of dollars in borrowing for the government.

Last week, the yield on 10-year Treasury notes rose to its highest level since November, briefly touching 3.17 percent, a sign that investors are demanding larger returns on the masses of United States debt being issued to finance an economic recovery.

While that is still low by historical standards — it averaged about 5.7 percent in the late 1990s, as deficits turned to surpluses under President Bill Clinton — investors are starting to wonder whether the United States is headed for a new era of rising market interest rates as the government borrows, borrows and borrows some more.

Already, in the first six months of this fiscal year, the federal deficit is running at $956.8 billion, or nearly one seventh of gross domestic product — levels not seen since World War II, according to Wrightson ICAP, a research firm.

Debt held by the public is projected by the Congressional Budget Office to rise from 41 percent of gross domestic product in 2008 to 51 percent in 2009 and to a peak of around 54 percent in 2011 before declining again in the following years. For all of 2009, the administration probably needs to borrow about $2 trillion.

The rising tab has prompted warnings from the Treasury that the Congressionally mandated debt ceiling of $12.1 trillion will most likely be breached in the second half of this year.

Last week, the Treasury Borrowing Advisory Committee, a group of industry officials that advises the Treasury on its financing needs, warned about the consequences of higher deficits at a time when tax revenues were "collapsing" by 14 percent in the first half of the fiscal year.

"Given the outlook for the economy, the cost of restoring a smoothly functioning financial system and the pending entitlement obligations to retiring baby boomers," a report from the committee said, "the fiscal outlook is one of rapidly increasing debt in the years ahead."

While the real long-term interest rate will not rise immediately, the committee concluded, "such a fiscal path could force real rates notably higher at some point in the future."

In some ways, ballooning deficits should not matter. Deficits are a useful way for governments to use public spending to stimulate the economy when private demand is weak. This works as long as a country closes its deficit and pays back its borrowings after its economy starts to recover.

The trouble is that government borrowing risks crowding out private investment, driving up interest rates and potentially slowing a recovery still trying to take hold. That is why the Federal Reserve announced an extraordinary policy this year to buy back existing long-term debt — $300 billion over six months — to drive down yields. The strategy worked for a while, but now the impact of that decision appears to be wearing off as long-term interest rates tick up again.

Then there is the concern that the interest the government must pay on its debt obligations may become unsustainable or weigh on future generations. The Congressional Budget Office expects interest payments to more than quadruple in the next decade as Washington borrows and spends, to $806 billion by 2019 from $172 billion next year.

"You're just paying more and more interest and having to borrow more and more money to pay the interest," said Charles S. Konigsberg, chief budget counsel for the Concord Coalition, which advocates lower deficits. "It diverts a tremendous amount of resources, of taxpayer dollars."

Of course, no one is suggesting the United States will have problems paying the interest on its debt. On Wednesday, even as it announced its huge financing needs for the latest quarter, the Treasury said financial markets could accommodate the flood of new bonds. "We feel confident that we can address these large borrowing needs," said Karthik Ramanathan, the Treasury's acting assistant secretary for financial markets.

One worry, however, is that there are fewer eager lenders to buy all that American debt. Most of the world is in recession, and other nations have rising borrowing needs as well. As other nations' surpluses turn to deficits, America will face competition in global financial markets for its borrowing needs.

For the moment, the United States is actually benefiting from a flight to quality into Treasuries brought on by the global financial crisis, which helped reduce rates to record lows this winter. But the influx will not continue forever.

China has lent immense sums to the United States — about two-thirds of its central bank's $1.95 trillion in foreign reserves is believed to be in United States securities — but it has begun to voice concerns about America's financial health.

To calm nerves and fill the deficit hole, the government is getting creative. The Treasury is ramping up its auction calendar, holding more frequent sales of government debt and selling the debt in expanded amounts. It is now holding sales of its 30-year bond each month, up from four times annually.

It is also resuscitating previously discontinued bonds, such as the seven-year note and the three-year note, to try to mop up any available money all along the yield curve. There is even talk of issuing billions of dollars of a new 50-year bond, though the idea has not won official approval.

On a second front, the Treasury and the Federal Reserve are trying to bolster the mechanics of the market — to make sure every auction goes smoothly. With such enormous sums involved, every extra basis point on the interest rate the government pays could mean extra billions of dollars for the taxpayer. Earlier this year, when demand was hesitant at a Treasury auction and when a British bond auction went poorly, investors grew nervous that the government might struggle to sell its mountain of debt.

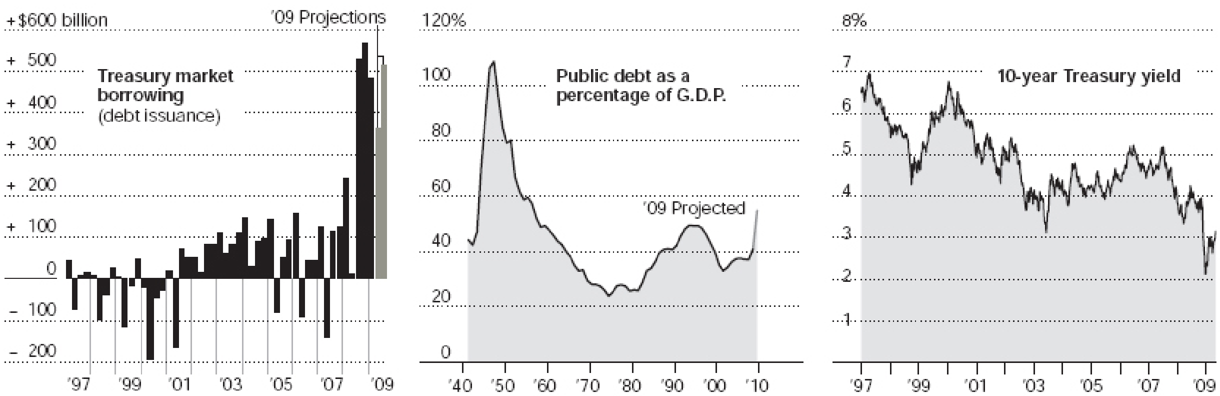
To avoid such an outcome and to keep borrowing costs low, the government is trying to expand the group of firms that bid at Treasury auctions. After the demise of such names as Lehman Brothers, the number of these firms, called primary dealers, has shrunk to 16, the smallest since this elite club was formed decades ago. Now the government is in discussions with smaller firms like Nomura and MF Global to persuade them to join.

The New York Times

The Rising Government Debt May Benefit Some Investors

Because of its soaring budget deficit, the government may need to borrow about $2 trillion in 2009, pushing the public debt to its highest level since the 1950s.

Investors are wondering if they will get higher returns as the interest rate on the debt has started to creep up.



Sources: Wrightson ICAP; Congressional Budget Office; Office and Management and Budget; Bloomberg

THE NEW YORK TIMES