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Heading Toward National Insolvency

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Welcome to America's rocky budget horrow show.

Americans don't need to go to the movies to see a horror picture show. The Congressional Budget Office's latest report on the federal budget should scare everyone. Not that Washington seems to have noticed.

For the fourth year in a row the federal government is running a deficit in excess of $1 trillion. Yet President Barack Obama is lecturing European governments on how to solve the Eurozone crisis. He should be telling them what not to do: stop running up wild and irresponsible debts.

That's what the CBO opined in its latest budget report "The 2012 Long-Term Budget Outlook." The document is a bit dry, but the looming catastrophe it describes could not be more frightening.

Explained CBO: "In the past few years, the federal government has been recording the largest budget deficits since 1945, both in dollar terms and as a share of the economy. Consequently, the amount of federal debt held by the public has surged."

Uncle Sam's 40-year average debt to GDP ratio is 38 percent. At the end of 2008 Washington was up to 40 percent. By the end of 2012 that number will be 73 percent, "the highest percentage since shortly after World War II," said CBO. The recession is responsible for part of this rise but, explained CBO, "the growing debt also reflects an imbalance between spending and revenues that predated the recession."

These numbers disguise worse news, however. CBO does not count intra-government borrowing as part of the national debt. So when the Treasury Department "borrows" money from Social Security, CBO doesn't count it, even though cash will have to be procured -- through more borrowing -- to pay promised benefits to retirees. The full national debt already is 100 percent of GDP, compared to about 84 percent for Europe.

But use CBO's analysis. The long-term still looks truly ugly. There's the so-called "baseline scenario," under which everything goes "right" in the agency's view.

Then debt as a percentage of GDP would fall to 61 percent in 2022 and 53 percent in 2037. That would still be about 30 percent above the 40-year average.

Unfortunately, everything doesn't often go right in Washington. Of course, what is "right" for the CBO is not necessarily "right" for the American people. Under this analysis the CBO figures that taxes would go up dramatically -- as a result of "Taxmageddon," with the expiration of the Bush tax cuts -- which would push the country toward a renewed recession. Even with the tax reductions Americans would be paying a larger share of the GDP to the government than the average over the last four decades. The "baseline scenario" would have Americans turning over a much larger share.

At the same time outlays would fall. A lot. As CBO explained: "under this scenario, government spending on everything other than the major health care programs, Social Security, and interest -- activities such as national defense and a wide variety of domestic programs -- would decline to the lowest percentage of GDP since before World War II."

Essentially CBO said: If only the tooth fairy would pay off the national debt, the Easter Bunny would fund Social Security, Santa Claus would take care of Medicare, and the Great Pumpkin would pay for everything else, life would be fine. Unfortunately, all of these are more likely than Washington politicians controlling their appetite for legal plunder.

Yet that's what would be necessary to save America's taxpayers. CBO observed: "Whether that debt will continue to grow in coming decades will be affected not only by long-term demographic and economic trends, but also by policymakers' decisions about taxes and spending." Social Security, Medicare, Medicaid, and health care expenditures all are expected "to continue rising faster than spending per person on other goods and services for many years." If that happens, "those factors will boost federal outlays relative to GDP well above their average of the past several decades -- a conclusion that holds under any plausible assumptions about future trends in demographics, economic conditions, and health care costs." What a future.

CBO analysts really aren't stupid or deluded, so they offer an "extended alternative fiscal scenario," which from a fiscal perspective is essentially all bad news. Taxes wouldn't rise dramatically, but still stay above the historical average. Social Security and Medicare expenditures wouldn't be controlled. Health insurance subsidies wouldn't be restrained. Other outlays would remain at historic levels, rather than falling dramatically. The result would be not just unpleasant, but truly horrendous.

Explained CBO: "Under those policies, federal debt would grow rapidly from its already high level, exceeding 90 percent of GDP in 2022. After that, the growing imbalance between revenues and spending, combined with spiraling interest payments, would swiftly push debt to higher and higher levels. Debt as a share of

GDP would exceed its historical peak of 109 percent by 2026, and would approach 200 percent in 2037." That's using the agency's discounted debt levels. In comparison, Greece peaked at about 163 percent debt to GDP.

Optimists might dream of living under the baseline scenario, but the agency noted that "many budget analysts" believed the extended alternative was much more realistic. Certainly that is what history tells us to expect.

Unfortunately, rising outlays and debt threaten to create an economic death spiral. Obviously, more borrowing means higher interest payments, that is, more government spending. At the same time, more debt is likely to increase interest rates, since lenders will become ever more worried about Uncle Sam's ability to pay back the loans. Last year Standard & Poors downgraded Washington's credit rating and in early June threatened to do so again if Congress fails to control spending. The result would be even higher interest payments.

Moreover, warned CBO, rising red ink "would reduce national saving, leading to higher interest rates, more borrowing from abroad, and less domestic investment -- which in turn would lower the growth of incomes in the United States." That is, because of excessive government outlays Americans will earn less even as they have to pay the government more. And there's no logical stopping point. As expenditures rise, the cycle will accelerate.

Which leads to an even more frightening prospect: financial panic. Explained the agency: "Growing debt also would increase the probability of a sudden fiscal crisis, during which investors would lose confidence in the government's ability to manage its budget and the government would thereby lose its ability to borrow at affordable rates." In 2008 Uncle Sam wildly bailed out virtually everyone and everything -- except taxpayers, of course. But if the federal government faced a budget crisis, who would bail it out? And if the American government tottered, what would happen to weaker European states, highly indebted Japan, and other nations?

In short, Americans are not just watching but *living in* a potential financial horror show. Unfortunately, President Barack Obama is one of the directors of the program. The CBO's recent separate analysis of the president's budget reported that he would nearly double the cumulative deficit between 2013 and 2022, taking the "baseline" estimate of $3.5 trillion to $6.4 trillion. The annual deficit would fall to "only" $488 billion in 2017, before steadily rising to $728 billion in 2022. Total federal, non-Social Security debt would rise to 76 percent of GDP.

Unfortunately, Republicans share the blame for the looming fiscal disaster. President George W. Bush and the GOP Congress were unashamed big spenders. Putative Republican presidential nominee Mitt Romney promises to be tough on federal spending, but nothing in his past behavior suggests that he takes this promise any more seriously than he has treated the many positions he has cheerfully tossed aside when he thought doing so was to his political advantage. Believing that Republicans, if victorious come November, will rein in Uncle Sam, is, like a second marriage, the triumph of hope over experience.

There is little time left to avoid Washington's looming budget apocalypse. The American people must take control away from politicians, irrespective of the letter after their name. Asked Ronald Reagan in 1980: If not us, who? If not now, when? We must answer these questions today.

About the Author

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