False prophets of debt-ceiling doom

By Matthew Melchiorre

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If I didn't know any better, I'd be on the lookout Tuesday for the Four Horsemen of the Apocalypse. With Aug. 2 just around the corner, President Barack Obama, Treasury Secretary Geithner, and not-so-fiscally-conservative Republicans warn of Armageddon if they don't get their spending fix on time.

Yet the American people aren't buying what they're selling.

Voters are realizing what Washington hasn't - that the debt crisis stems from a compulsive spending problem. A new Gallup poll indicates that, among Americans who follow the debt-ceiling debate "very closely," 53 percent oppose increasing the limit; 37 percent favor an increase. A majority of Americans now seems to realize that the fear-mongering going on in Washington.

Contrary to what spendthrift politicians have been saying, reaching the federal debt ceiling does not automatically trigger default. The debt limit simply caps the amount of debt that the U.S. Treasury may issue. The Treasury has the ability to prioritize its payments to bondholders and sell off assets (like TARP funds and gold) to avoid a default situation. Debt interest payments total $214 billion for 2011 - that's less than 10 percent of $2.2 trillion in expected tax revenue this fiscal year.

Obama's claim that seniors may not receive their Social Security checks for August is dubious, given that the program's annual cost is $727 billion - 33 percent of revenue. Medicare and Medicaid combined come in at $846 billion - 38 percent of total tax inflow. Paying interest on the debt and providing entitlements still leaves more than $400 billion in unspent tax revenue, plus $2.4 trillion in assets left over to cover remaining government obligations, according to Veronique de Rugy and Jason Fichtner of the George Mason University Mercatus Center. The argument that America won't be able to pay its bills without a debt-ceiling increase is simply incorrect.

Another oft-raised bogeyman is the possibility that not raising the debt ceiling will cause a downgrade of America's AAA credit rating and spark a selloff of Treasury bills in international bond markets. Those fears are also unfounded. In fact, three rating agencies - Egan Jones Ratings Co., Weiss Ratings, and Dagong Global

Credit Rating - have already lowered their assessments of U.S. debt, and interest rates have not moved.

Egan-Jones, a Nationally Recognized Statistical Rating Organization with the Securities and Exchange Commission, changed its rating of U.S. government debt July 16 to AA-plus from AAA. It released a statement explaining its decision: "The major factor driving credit quality is the relatively high level of debt and the difficulty in significantly cutting spending. We are taking a negative action not based on the delay in raising the debt ceiling but rather our concern about the high level of debt to GDP." In short, investors are more concerned about Washington's spending problem than they are about the Treasury being able to issue more debt.

Weiss went much further, lowering its rating from an already dismal C to a C-minus. It explained: "Our downgrade today is not contingent on the outcome of the debt-ceiling debate in Washington. It is driven exclusively by the numbers, which indicate that, in addition to a decline in the long-standing weaknesses we noted three months ago, the U.S. has already lost the golden halo that helped guarantee liquidity and acceptance of its government securities in global markets." In April, Weiss listed among those weaknesses the fact that, "[The United States] ranks 44th in terms of its debt burden, primarily because of its large deficits."

More importantly, Egan-Jones has been right when it mattered. As the Cato Institute's Mark Calabria notes: "It would be easy to dismiss these agencies as irrelevant and attempting to simply grab attention, but at least one of these agencies, Egan-Jones, has a track record of correctly predicting problems at such companies as Enron, WorldCom, Global Crossing, Bear Stearns and Lehman Brothers that the major rating agencies missed until it was too late."

Raising the ceiling for the 11th time since the start of the new millennium tells investors that the U.S. government is not serious about controlling its spending addiction. Instead, curbing the issuing of more debt and cutting spending will signal to bondholders that the government is finally trying to address the problem that created a debt crisis in the first place.

Prioritizing debt payments as they mature and selling assets are merely temporary measures that the Treasury can take to stave off default. Ultimately, our government must curb spending, or else the country will be in an even worse situation in a not-so-distant future. Raising the debt ceiling is akin to an alcoholic having one last drink - sooner or later, the government needs to admit that it has a problem. No amount of doomsaying can change that reality.

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