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Bond markets reflect the true cost of Obamacare

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Not many people noticed amid the Democrats' struggle to jam their health care bill through the House, but in recent weeks United States Treasury bonds have lost their status as the world's safest investment.

The numbers are pretty clear. In February, Bloomberg News reports, Berkshire Hathaway sold two-year bonds with an interest rate lower than that on two-year Treasuries. A company run by a 79-year-old investor is a better credit risk, the markets are telling us, than the United States government.

Buffett's firm isn't the only one. Procter & Gamble, Johnson & Johnson and Lowe's have been borrowing money at cheaper rates than Uncle Sam.

Democrats wary of voting for the health care bill may have been soothed by the Congressional Budget Office's report that it would reduce federal deficits over the next 10 years. But bond buyers know that the Democrats gamed the CBO system to get a good score.

The realities, as former CBO Director Douglas Holtz-Eakin pointed out in the New York Times, are different. The real cost is disguised by the fact that the bill includes 10 years of revenue but only six years of spending. It includes $70 billion in premiums for long-term care that will have to be paid out later. It excludes $114 billion in discretionary spending needed to run the program. It includes nearly half a trillion dollars in unrealistic Medicare savings.

Holtz-Eakin's bottom line: The bill will not lower deficits but will raise them by $562 billion over 10 years. Treasury will have to borrow that money -- and probably pay much higher interest than it's paying now.

Moreover, once the bill is fully in effect, the Cato Institute's Alan Reynolds points out, its expenses are likely to grow at least 7 percent a year -- significantly faster than revenues. At that rate, spending doubles every 10 years.

No wonder that Moody's declared last week that the Treasury is "substantially" closer to losing its AAA bond rating.

It's not only the federal government that is heading toward insolvency. State governments will have to spend more under the health care bill -- $735 million in Tennessee alone, according to Democratic Gov. Phil Bredesen.

And state governments are already facing a huge problem called pensions. The Pew Charitable Trusts estimates that state government pensions are underfunded by $450 billion. My American Enterprise Institute colleague Andrew Biggs argues in the Wall Street Journal that the real figure is more than $3 trillion.

The reason: State governments set aside cash to invest in pensions, but they typically assume that their investments will rise 8 percent a year indefinitely. They haven't been getting such high returns and are not likely to do so in the future. But they are under legal obligations, which courts won't allow them to escape, to pay the pensions. Retirees get paid off before bondholders, which means that states are going to have to pay more interest when they borrow.

Back in the 1990s, Clinton adviser James Carville said that if he was reincarnated, he would like to come back as the bond market -- "because you can intimidate everybody." Governments, like all organizations, need to borrow routinely. But investors won't lend unless they think they will be paid back. And they will demand higher interest rates as their loans become riskier.

On Sunday, 219 House Democrats, soothed by their leaders' gaming of the CBO scoring process, voted in reckless disregard of what the bond market has been telling them. Some may share Speaker Nancy Pelosi's optimism that the government's looming fiscal disaster can be avoided by imposing a value added tax -- in effect, a national sales tax.

But, as we know from the experience of high-tax Western Europe and relatively low-tax America over the last three decades, higher taxes tend to retard economic growth. Lower economic growth means less revenue for government than in CBO projections. Less revenue means more borrowing -- and at some point lenders are going to call a halt.

Barack Obama's project of transforming the United States into something like Western Europe is, according to the CBO, raising the national debt burden on the economy to World War II levels. I see train wrecks ahead -- as the bond market forces huge spending cuts or tax increases first on states and then on the federal government. It will make what happened in the House on Sunday look pretty.

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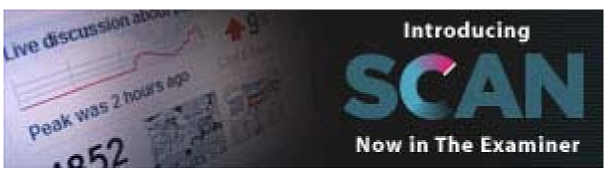

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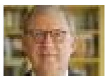
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