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Addressing the Economic and National Security Implications of Our Fiscal Crisis

By Paul Schott Stevens

As expressed forcefully by a group of fund industry leaders last November, America's current budgetary overreach has clear and dire implications for the 90 million investors that ICI member companies serve. Today, I elaborated on those implications in a speech before a gathering of the National Strategy Forum in Chicago. What does our recent and unprecedented buildup of debt mean for our economy and our national security?

In examining this question, I have found it helpful to consult our nation's early history and the writings of President George Washington. When Washington announced his retirement from public life in 1796, he wrote a letter now known as Washington's Farewell Address. In part, the letter contained advice on economic issues for his fellow citizens and subsequent generations of Americans.

"As a very important source of strength and security, cherish public credit," he said. By "cherish," he meant, "treat credit as precious"—or, as he hastened to add, "use it as sparingly as possible." When Washington left office the next year, the national debt—largely incurred fighting the Revolutionary War—was $82 million.

Next January, whether President Obama is giving his second inaugural or his own farewell, the debt will stand at more than $16 trillion—103 percent of GDP, and still rising. That debt of $82 million dollars in 1797? Today, Treasury spends seven and one-half times that amount every day just for interest.

The implications of this mounting debt load are many. I'll highlight two key points from my speech.

- **Interest payments may reach destructive levels.** Admiral Mike Mullen, the former Chairman of the Joint Chiefs of Staff, frequently said publicly that "the single biggest threat to our national security is our debt." He liked to point out that interest payments on the debt would soon exceed the budget of the Department of Defense—creating what he called "a bow wave of debt" that could "run over us in a way where our budget must be cut dramatically." I agree with Admiral Mullen. Resources devoted to interest payments are resources that can't be spent on ensuring our national security—or on science, technology, transportation, education, or myriad other purposes. In short, money spent on servicing a growing debt eats away at the fabric of our economy.
- **Faith in the U.S. dollar and U.S. debt could be undermined, with disastrous consequences.** With our debt spree, we are abusing the privilege granted by the dollar's reserve status; we are squandering the good credit built over the last century. As foreign holdings of U.S. debt grow, the risk grows that we are glutting the market. Foreign investors' appetite for the seventh or eighth trillion-dollar batch of Treasury securities isn't likely to match their interest when the debt held overseas was far less. And sentiment can change quickly. History teaches us that financial markets can turn on a dime, that today's favorite investment can be tomorrow's laughingstock. If that happens to the dollar and U.S. debt, we could face a financial and economic crisis that would make the bursting of the tech and mortgage bubbles seem like mere blips.

In Chicago, I addressed another key question: what can be done? There's no simple answer there either. Yet, as they grapple with these difficult issues, policymakers can look to three principles to guide them.

- **Candor:** Our nation's leaders owe it to us to take the debt threat seriously and deal with it in all candor and frankness. On these vital issues, our political leaders should, as President George Washington said, display "firmness and virtue enough to maintain…the most enviable of all titles, [that] of an honest man."

- **Compromise:** Neither of our great political parties has a monopoly on wisdom or integrity, patriotism or national interest. On issues like fiscal policy today that are so critical to our long-term prospects as a nation, there should be no aisle to cross. We must insist that our political leaders stand shoulder to shoulder—and that they act before their hands are forced by our own sovereign debt crisis.
- **Equity:** It is essential to focus on policies that promote sound, long-term economic growth and that promote balance between the promises that government makes and the resources that the private economy can provide to meet them. The sharp increase in government spending that we have seen in the last five years cannot be sustained—but neither can the low level of revenues. Both need to return to something closer to their postwar norms.

Taken together, these principles can form the basis for constructive efforts to place our nation once again on a sound footing of prosperity and strength.

Paul Schott Stevens was President and CEO of ICI.
