



Reflections On the Budget

On Feb. 1 I testified before the Senate Budget Committee on the national debt. In preparing my testimony, which took place on my daughter Emily's 12th birthday, I reviewed the staggering leaps in the national debt that had occurred since her birth and since I'd served in the Reagan Administration.

When I joined the government in 1984 the \$1.5 trillion national debt (40% of GDP) was already a hot economic issue and political problem. Work was under way on the Gramm-Rudman effort to limit spending, and Fed Chairman Paul Volcker was encouraging deficit reduction, hinting at looser monetary policy if Congress would cut back. The country had survived the inflation crisis of the 1970s—but just barely.

President Reagan wanted to win the Cold War and also eliminate the Departments of Energy and Education. He was able to beat the Soviets but not big government. Jack Kemp, at the time a member of the House Budget Committee, argued for economic growth through lower tax rates, which were at 70% when Reagan took office. Both men believed in the importance of a sound dollar after the disastrous 1970s, which had seen the crash of the greenback, the rise of eurodollars in London and the advent of gas lines as oil prices soared and alternative energy schemes failed as soon as their federal subsidies expired.

Nearly 30 years later the issues are the same, but the national debt has surged through \$6 trillion at the turn of the century, when my daughter was born, to \$14 trillion today. It will soon

exceed the U.S.' annual output, with near-term CBO scenarios of the debt rising to 130% of output under present tax rates and spending policies.

CHIN-DEEP IN DEBT

I now have four young children, so the size of the debt has taken on greater personal significance. Washington has already borrowed \$45,000 for every American. Under current trends the country will owe \$31 trillion—about \$100,000 from each of us—by the time Emily goes to college.

There has also been a rapid increase in hidden debt that's not counted in the national debt. U.S. taxpayers are on the hook for Congress' commitments to moneylosing, government-sponsored enterprises such as Fannie Mae and Freddie Mac and a host of international organizations such as the IMF and the World Bank. They add trillions of dollars to the debt burden, along with the underfunding of the promises to provide cash and medical care to the elderly.

Washington has been compounding the problem in recent decades by adding huge new functions to the federal government, including the home mortgage market, the alternative energy industry and small-business lending, which is now heavily dependent on myriad federal subsidy programs.

Last year we added entirely new concepts of federal government beyond the much publicized takeover of health care. In an unprecedented expansion of its role, the Federal Reserve, in November, began buying back the national debt in an effort to boost inflation. And Congress created a self-contained consumer regulatory agency

inside the Fed—with no funding oversight from Congress or the Fed's board.

Adding to the risk, the U.S. has been shortening the average stated maturity of the national debt from 70 months in the 1980s and 1990s to less than 60 months now. The Federal Reserve's large buy-back of longer-dated notes and bonds—paid for by overnight deposits from commercial banks—has further shortened the effective maturity of the U.S. national debt to under 40 months, which is near the crisis point of the 1970s.

On average we have to roll over the entire national debt every three and a quarter years, no matter the financial climate. That's a risk we should not be taking.

In my Senate testimony I included several policy suggestions aimed at bringing new confidence in the fiscal outlook to businesses and investors.

- Washington should stop the Fed's bond purchases because they distort markets, create a conflict of interest for the Fed's monetary policy decisions and shorten the effective maturity of the national debt.

- Use the upcoming increase in the \$14.3 trillion debt limit to install a permanent ceiling on the marketable debt-to-GDP ratio at 50% and a floor on the average maturity of the debt at five years, enforced by escalating penalties on Washington when the limits are violated.

- Rather than waiting for a grand package to tackle the budget deficit, Washington needs to go on an immediate diet. Cut a billion dollars every day and it won't be long before it amounts to real money, even by Washington's standards. 