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On All Levels of the Economy, Concern About the Impasse

Losing Top Rating Could Cost Growth And Job Creation

By JULIE CRESWELL
and LOUISE STORY

Economists and analysts are trying to gauge the costs to the economy and consumers if the United States loses its solid-gold credit rating — a move that appears more likely now that the standoff in Washington over government spending has calcified.

Some economists say the effects of lowering the federal government's credit rating to AA from AAA can be measured in the billions of dollars in increased borrowing costs for the government, and in

QUESTIONING THE AGENCIES

Officials of the ratings agencies are to testify before Congress on Wednesday. Page 4.

What Rating?

How the AAA rating of the United States and the current interest rate on long-term debt compare with some other countries.

STANDARD & POOR'S SOVEREIGN			
	RATING	OUTLOOK	10-YEAR GOVERNMENT BOND YIELD
Switzerland	AAA	Stable	1.5%
Germany	AAA	Stable	2.7%
United States	AAA	Watch Neg.	3.0%
Spain	AA	Negative	6.0%
Japan	AA-	Negative	1.1%
Italy	A+	Negative	5.6%
Mexico	BBB	Stable	6.8%
Brazil	BBB-	Positive	12.6%
Portugal	BBB-	Negative	11.1%
Greece	CCC	Negative	14.7%

Sources: Standard & Poor's; Bloomberg

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the billions more that consumers, corporations, states and municipalities will have to pay for their credit. It could also erode consumer and business confidence, slowing even further the economy and job creation.

The prospect of a downgrade by one of the credit rating agencies once seemed almost unimaginable.

But the impasse in Washington over the government's deficit and \$14.3 trillion debt limit has led some global financial players to expect the change.

A downgrade on debt issued by the United States would have less severe consequences than a default, which takes places when a

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**Every one percentage
point increase in
interest rates adds
\$1.3 T to deficits
over ten years.**

Source: CBO

Note: Increase in interest rates above current baseline levels.

Problems with Boehner Plan

- Repeats default crisis in 6 months
 - continues uncertainty and puts economy at risk
- Includes less deficit reduction than Reid plan
- Provides no hard firewall between security and non-security spending
 - likely resulting in deep cuts in domestic priorities
- Requires vote on irresponsible Balanced Budget Amendment

S&P Warns Against Repeated Debt Ceiling Debates

“...[W]e would be concerned if we thought that the debt ceiling debate would come back and be open and we’d have to go through all this again and again and again.... That would be a negative in our view.”

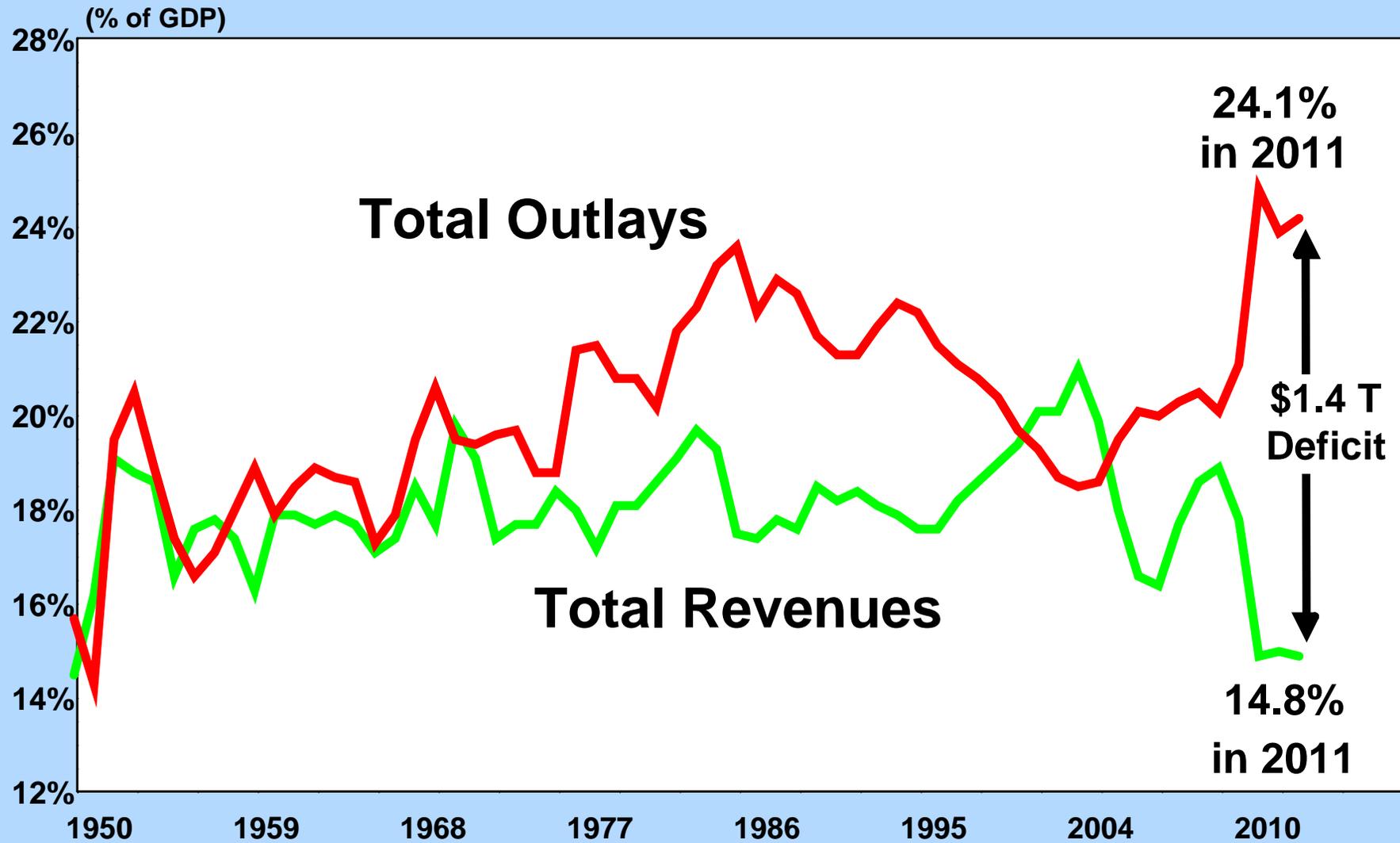
**– David Beers, Standard & Poor’s Global
Head of Sovereign Ratings
Interview on CNBC’s *The Kudlow Report*
July 26, 2011**

To Avoid U.S. Credit Rating Downgrade, S&P Wants to See Bipartisan Debt Reduction Effort

“... [W]e will measure [the deal] on a number of parameters. One is... is it credible? And credibility, among other things, means to us that there has to be some buy-in across the political divide, across both parties, because politics can and will change going forward. And if there’s ownership by both sides of the program, then that would give us more confidence.... It’s not just about the number. It’s about the all-in intent.”

**– David Beers, Standard & Poor’s Global Head of Sovereign Ratings
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Spending and Revenues



Sources: OMB, CBO

Problems With Republican Balanced Budget Amendment

- **Restricts ability to respond to economic downturns – compounds declines**
- **Uses Social Security funds to calculate balance and subjects program to same cuts as other federal spending**
- **Shifts ultimate decisions on budgeting to unelected and unaccountable judges**
- **State ratification process could take years to complete – need long-term debt reduction plan in place now**

**Turn Recession
into a Depression**

American Enterprise Institute Scholar Calls Balanced Budget Amendment a “Really Dumb Idea”

“Few ideas are more seductive on the surface and more destructive in reality than a balanced budget amendment. Here is why: Nearly all our states have balanced budget requirements. That means when the economy slows, states are forced to raise taxes or slash spending at just the wrong time, providing a fiscal drag when what is needed is countercyclical policy to stimulate the economy. In fact, the fiscal drag from the states in 2009-2010 was barely countered by the federal stimulus plan. That meant the federal stimulus provided was nowhere near what was needed but far better than doing nothing. Now imagine that scenario with a federal drag instead.”

**– Norman Ornstein, Resident Scholar
at American Enterprise Institute
“Four Really Dumb Ideas That Should
Be Avoided,” *Roll Call*
January 26, 2011**

The Washington Post

FRIDAY, JULY 15, 2011

A bad idea returns

Rewriting the Constitution is the wrong way to deal with the debt.

AMENDING THE Constitution to require a balanced budget is a bad idea that never dies. It's not surprising that the current avalanche of debt has inspired renewed calls. Given that the political system appears unable to discipline itself not to spend more — trillions more — than it takes in, why not tie lawmakers' hands to prevent them from piling ever more debt on the national credit card?

The answer: The constitutional cure, while superficially tempting, would be worse than the underlying disease. A balanced-budget amendment would deprive policymakers of the flexibility they need to address national security and economic emergencies. It would revise the Constitution in a way that would give dangerous power to a congressional minority.

The latest push from lawmakers advocating the amendment is to couple a vote on the proposal with an agreement to raise the debt ceiling. On the surface, this argument seems benign enough: Why not give states the chance to decide whether the Constitution should mandate a balanced budget? But policymakers have an independent responsibility to assess whether an amendment is wise. This one, especially in its latest incarnation, is not. It would require a

two-thirds vote in both houses of Congress to run a deficit in any year. The same supermajority would be needed to enact any tax increase. Compare those hurdles to the version of the amendment that passed the House in 1995, which called for a slightly lower three-fifths vote in each house to pass an unbalanced budget or increase the debt ceiling and a mere majority vote to increase taxes.

Worse yet, the latest version would impose an absolute cap on spending as a share of the economy. It would prevent federal expenditures from exceeding 18 percent of the gross domestic product in any year. Most unfortunately, the amendment lacks a clause letting the government exceed that limit to strengthen a struggling economy. No matter how shaky the state of the union, policymakers would be prevented from adopting emergency spending, such as the extension of unemployment insurance and other countercyclical expenses that have helped cushion the blow of the current economic downturn. The 18 percent cap on spending is so severe that House Budget Committee Chairman Paul Ryan's economic plan would violate its strictures. So would any budget passed under President Ronald Reagan. With health-care costs rising and the number of retiring baby boomers increasing, it

would be next to impossible to keep spending to that low share of the economy.

Both houses of Congress are expected to vote on the amendment next week, but a responsible lawmaker's obligation does not end at voting against this version. Even a less draconian rendition — without the spending cap or with lower thresholds for approving tax increases or running deficits — would be the wrong approach. If a balanced-budget amendment had been in place when the economy crashed in 2008, Congress would have been unable to respond with a stimulus package or efforts to stabilize banks and auto manufacturers. Even if you believe that was the wrong policy response, it is important that Congress retain the flexibility to craft the correct one.

The fiscal situation is perilous. It's commendable that members of Congress are trying to right it. The balanced-budget amendment remains a deeply flawed approach to achieving a noble goal.

Senator McCain on Republican Balanced Budget Amendment Proposal

“What is amazing about this is, some Members are believing we can pass a balanced budget amendment to the Constitution in this body with its present representation, and that is foolish. That is worse than foolish. That is deceiving many of our constituents.... That is not fair to the American people to hold out and say we will not agree to raising the debt limit until we pass a balanced budget amendment to the Constitution. It is unfair. It is bizarro. Maybe some people who have only been in this body for 6 or 7 months or so believe that. Others know better....

“It is time we listened to the markets. It is time we listened to our constituents. Most of all, it is time we listened to the American people and sit down and seriously negotiate something....”

**– Senator John McCain (R-AZ)
Senate Floor Statement
July 27, 2011**

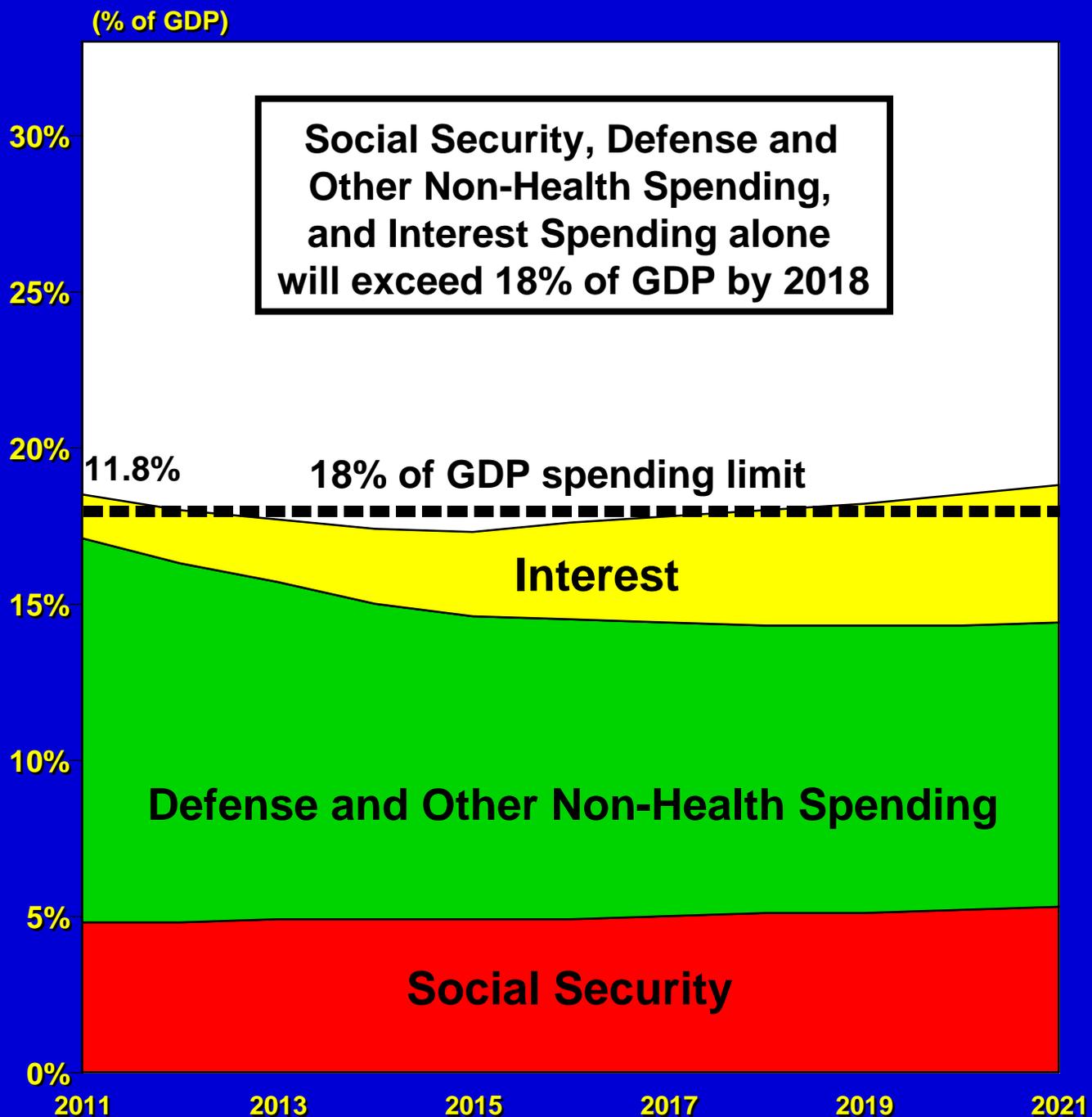
Former Reagan Economic Advisor on Republican Balanced Budget Amendment

“I have previously explained the idiocy of right wing advocates of ... a balanced budget amendment. However, the new Republican balanced budget proposal is especially dimwitted....

“In short, this is quite possibly the stupidest constitutional amendment I think I have ever seen. It looks like it was drafted by a couple of interns on the back of a napkin. Every senator cosponsoring this POS should be ashamed of themselves.”

**– Former Reagan Administration Economic
Advisor Bruce Bartlett
Capital Gains and Games Blog, “Dopiest
Constitutional Amendment of All Time?”
March 31, 2011**

Balanced Budget Amendment 18% of GDP Spending Limit is Draconian and Unrealistic



Source: CBO

Note: Social Security, Defense and other non-health spending, and Interest spending under CBO Alternative Fiscal Scenario.

Five-Story Cayman Islands Building That 18,857 Companies Call Home



Reid Deficit Reduction Package

- Prevents default
 - saves nation from immediate economic crisis
- Provides significant downpayment on deficit reduction
- Creates structure to do more
 - Joint Congressional Committee to find additional savings