



# How Are We Going To Pay For All This?

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The largest federal budget deficit since World War II came back in 2009, as slower growth and increased government spending during the subprime-mortgage financial panic pushed the deficit to 9.8% of GDP. This year's the budget deficit will, quite simply, blow that record out of the water.

The Congressional Budget Office recently totaled up all the legislative measures taken so far - as well as the effects of a weaker economy (payments for unemployment benefits would be going up even with the recent law) - and they estimated this year's budget deficit at \$3.7 trillion, which they forecast would represent about 18% of GDP.

As if that weren't enough, the House of Representatives just passed a bill that would add another \$3 trillion to the debt. Although a detailed year-by-year cost estimate isn't yet available on the spending provisions, and the bill is dead-on-arrival in the Senate, which isn't going to rubber stamp that proposal, it's likely Congress and President Trump will end up compromising on some sort of additional measures that drive the deficit even higher. As a result, we're guessing the budget gap for the current fiscal year ends up closer to \$4 trillion, or about 20% of GDP, the highest since 1943-45.

Given the economic crater generated by the Coronavirus and related shutdowns, as well as the heavy-handed legislative response, budget deficits will be enormous in the years ahead, too.

In spite of these sky-high numbers, it's important to recognize that the US government is not about to go bankrupt. The debt, while large (and growing), remains manageable. Before the present crisis, the average interest rate on all outstanding Treasury debt, including the securities issued multiple decades ago, was 2.4%. Now, our calculations suggest newly issued debt is going for about 0.25%, on average, which applies to both the recent increase in debt as well as portions of pre-existing debt coming due and getting rolled over at lower interest rates.

When debt that costs 2.4% gets rolled over at around 0.25%, that's a great deal for future US taxpayers. The problem is, the Treasury Department has been decidedly stubborn about not issuing longer-dated securities – think 50 and 100-year bonds – that would allow taxpayers to lock-in these low interest rates for longer, making it easier to spread out the cost of the extra debt incurred throughout the crisis.

As a result, if (or more like when) interest rates go back up, the interest burden generated by the national debt could go up substantially.

The best move the Treasury Department could make would be to use the recent surge in debt to overhaul the kinds of securities it issues. One idea that deserves exploring is replacing all securities with a maturity of over, say, 2 years, with "perpetual" or "interest-only debt." No principal would ever have to be paid on these instruments; they'd just pay the same nominal amount of interest twice per year. If we want to mix it up a bit, some debt could pay interest with gradual adjustments for inflation, just like TIPS.

This is not a new idea. The British issued perpetual bonds starting in the 1750s, and the last ones were retired in 2015. And although they're called "perpetual" bonds, and they're not callable, the Treasury Department could always buy them back at market prices to retire them.

Liquidity should not be an issue. Every time the government needs to issue longer-dated securities, it could simply re-open that very same security. Then the private sector could slice and dice them, on demand. If someone needs a 10-year zero-coupon Treasury note, just take the interest payment due in ten years and package that into a stand-alone security. Want something like a traditional 30-year? An investment firm can package a stream of interest payments over the next 30 years and tie it to a big package of payments due in *exactly* thirty years.

But it's not only the debt generated by recent fiscal measures that will burden future generations. Overly generous

unemployment benefits are disincentivizing many unemployed workers from re-joining the labor force, which slows the process of accumulating skills. Widespread government-mandated closures also hinder skill-formation, as well as risk destroying some (or all) of the know-how embedded in business's operations.

Yes, the debt is a burden on future taxpayers. In this way, the fiscal response magnifies the effects of other responses to the Coronavirus. So far, the age of the typical person who has died with the virus has been about 80 years old. Right or wrong, our government - and society in general - has taken enormous measures to contain the virus to save the lives of our elderly population, and these moves have imposed enormous costs disproportionately borne by the younger generations who are out of jobs, school, and business opportunities. The very same group who will be paying the costs well into the future.

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