BOHANON & CUROTT: Big spending is needed, but this deficit won’t go quietly

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Does the COVID-19 pandemic mean we no longer need to worry about federal deficits or national debt? The $2 trillion stimulus package passed Congress with a lone dissenting vote. The most ardent fiscal hawks in Washington are in agreement on the major components of the plan.

The funds for the stimulus package will apparently be financed by floating 30-year U.S. bonds. The interest rate on those bonds is expected to be around 1.44%. That makes the additional interest payments on the new debt about $29 billion a year. That’s less than 0.14% of the country’s 2019 GDP of $21.4 trillion, and less than 0.83% of 2019 Federal Tax Revenue of $3.5 trillion.

The economy is being wrecked by the pandemic. This is precisely the time and precisely the reason to use the federal government’s clout in financial markets to smooth things over. So, it’s unanimous—let’s not worry about it.

Well, not quite. To quote Harvard economist Ken Rogoff, “Ramping up debt is not without risk.” Rogoff is one of the world’s top scholars on how national debt interacts with national economies. Back in December, before he or any of us suspected the coronavirus crisis was in the making, there were calls for expanding the national debt because rates on government debt were at historic lows. Rogoff advised caution. The biggest risk is that interest rates on government debt might rise.

U.S. Treasury debt at the end of 2019 was $17 trillion. The amount to be refinanced in the next five years is $11.3 trillion, or 68% of the total. If the interest rate the United States has to pay on that rollover is just 1% higher, annual debt service payments rise $113 billion. This does not include the additional interest payments on new debt that emerges from continued deficit spending. Add to this future Social Security and Medicare obligations that far exceed their expected revenue.

The day of reckoning comes when the U.S. Treasury has to choose between paying the interest on its bonds or paying its obligations to its pensioners, whom Rogoff deems “the junior debt-holders in the 21st-century welfare state.” Stiff the senior debt-holders and interest rates skyrocket. Stiff the pensioners and get political chaos. Impose austerity and generate a downturn. It is not a pretty picture.

As much as the $2 trillion package might be needed, let’s not kid ourselves—it brings the day of reckoning that much closer.•

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