

Statement of Senator Kent Conrad
Democratic Policy Committee Hearing on the Budget Deficit

January 20, 2004

Thank you Senator Dorgan for convening this hearing on the first day of our return. I think it is most appropriate given the importance of the subject.

I've been reading excerpts of the book that you referenced about Secretary O'Neill and it reminded me vividly of some of the events of 2001 when Chairman Greenspan came to my office and told me what he intended to testify to the next day. And I urged him to think again. And I urged him not to unleash what I described at the time as the 'deficit dogs' because I told him that if he testified as he intended to that he would unleash all of those who want to continue tax cuts beyond what was prudent and to unleash those who wanted to spend in an unrestrained way.

And unfortunately all of that has come to pass. We now see deficits that are truly out of control. I think it is very important for people to understand it's not just deficits in the short-term that is the great concern. Obviously, we're a powerful nation. We're a wealthy nation. We can afford to run deficits in the short-term. We could even afford to run modest deficits for a longer period of time. What we can't have is deficits that are growing dramatically in comparison to the growth of the economy. That's what puts all of this at risk.

And most of the econometric models that I have seen show very clearly that if we continue on this course – the course the President has recommended – that it will put upward pressure on interest rates, that it will slow economic growth, and in fact retard all that we hope for in terms of job development.

Mr. Chairman, I do have a few charts. I think it might be useful to go back to the history and see what President Bush inherited and what his policy has provided. We see that when he came to office we had the biggest budget surplus in the history of the country and he's now turned that into the biggest budget deficit in the history of the country, and by a wide margin.

Let's go to the next chart which shows the historic trend of deficits since 1969 and you can see the deficit that we are now anticipating for 2004 according to various administration spokesmen will approach \$500 billion, maybe something less than that, but his spokesmen are saying now that it will approach \$500 billion. We see the previous record in 1992 before last year's new record went all the way back to 1992 in the previous Bush administration.

Some have been telling us, don't worry these deficits are small in relationship to the size of our economy. I've tried to do a reality test on that and this chart shows if you exclude Social Security – in other words if you don't jackpot all of the funds of the federal government, if you treat Social Security separately as it should be treated in my judgement – what you see is that even as a share of our national income, even as a share of the size of our economy, these deficits are at near record levels. The only one higher as a percentage of gross domestic product was back in 1983. In 1983, there was virtually no Social Security surplus. This year the Social

Security surplus will be about \$160 billion, and under the President's plan every dime of Social Security surplus will be taken – not to pay down debt, not to prepay the liability – every dime will be taken to pay for tax cuts and other expenses of government.

Perhaps the most alarming thing is where all this is headed in the long-term. And not according to my projections, but according to the President's own projections. These are the numbers that come right out of his budget document of last year. This is his projection of what happens if we adopt his policies – his spending plan, his tax plan – and what it shows is that we're in the budget 'sweet spot' now, even though we are having record budget deficits. We see in the next few years there will be modest improvements, but then as the baby boomers begin to retire and the tax cuts, which the President recommends be made permanent, explode. What we have is an exploding deficit as well. And deficits that are much larger than anything we have ever seen before in this country. And that is an untenable circumstance for the country. We simply can't have budget deficits of the magnitude the President is projecting.

One of the things that is most alarming about what the President proposes is that it is coming at the worst possible time, right before the baby boomers begin to retire. The baby boom generation, the leading edge, begins retiring in 2008 and you can see the green part of these bars is the Social Security trust fund; the blue part is the Medicare trust fund; the red is the cost of the tax cuts. And just at the time the trust funds go cash negative in the next decade, at that very time, the cost of the tax cuts explode, and as a result we are driven right off the fiscal cliff.

Some, in analyzing the deficit, say it is simply a spending problem. Well it is in part a spending problem because deficits arise from the imbalance between spending and revenue. We also have a revenue problem. This chart shows that revenue as a percent of gross domestic product will be the lowest since 1950 in 2004. So we not only have a spending problem, we've got a revenue problem.

The results of these fiscal imbalances are always hard to see in the near term because the effect of deficits and the build up of debt – that reveals itself over time. But there are warning signals and the first warning signal is the drop in the value of the dollar. The dollar has dropped nearly 30 percent over the last 18 months in relationship to the Euro. That's a warning signal. That's the world markets telling us that they have less confidence in the dollar, less confidence in the U.S. economy.

Let's go to the next chart which is what Federal Reserve Board Chairman Greenspan has warned us. He said, "The...relatively optimistic short-term outlook for the U.S. economy is playing out against a backdrop of growing longer-term concern in financial markets about our federal budget."

And I think unfortunately we will see that play out through this year and into next year and the following year because the concern about our financial markets and their stability can only grow when we have fiscal imbalances of these magnitudes.

Finally, not only is Chairman Greenspan warning us, not only are others warning us, but now the

International Monetary Fund is warning us and they're warning us that the buildup of deficits and debt not only threaten our own economic security, but threaten global economic security, and their concern is that these massive deficits, both the budget deficit and the trade deficit, are going to put upward pressure on interest rates and choke off economic growth and economic opportunity and job creation, not only here but around the rest of the world as well. That is a serious warning, one that we ought to listen to. And as a party, I think once again it will fall to the Democratic party to be the party of fiscal responsibility, to bring back some sanity to our long term fiscal condition.