

The Fiscal Times
May 20, 2011

Democracy Abroad: Costly and Further Out of Reach
By LAWRENCE HAAS

President Obama's call for the United States to assist the Middle East and North Africa's transition from authoritarianism to democracy reflects a longstanding U.S. foreign policy goal. His reluctance to spend much to achieve it was something different, however.

It shows how U.S. fiscal troubles will continue to limit Washington's ability to achieve its goals both at home and abroad.

"It will be the policy of the United States to promote freedom across the region, and to support transitions to democracy," the president said, echoing Harry Truman's call to "assist free peoples to work out their own destinies in their own way," John F. Kennedy's call "to assist free men and free governments in casting off the chains of poverty," and George W. Bush's call for America to "seek and support the growth of democratic movements and institutions in every nation and culture."

The United States has long sought to advance freedom and democracy for moral and selfish reasons. While U.S. efforts on this score reflect America's values, they also nourish a more peaceful and prosperous world, which makes the United States more secure and creates markets for U.S. goods.

Freedom and democracy don't come cheap, however. Truman created the Marshall Plan in the late 1940s to rescue Western Europe's economy and strengthen its democracies, and the plan allocated \$13 billion over four years at a time when the entire budget was between \$30 billion and \$45 billion a year.

Bush replaced dictators with more democratic regimes in Afghanistan and Iraq after September 11 in hopes that they would serve as models for the region - efforts that total hundreds of billions of dollars to date.

Obama's vision of a more democratic region will not be easy to achieve. Though protests have toppled autocrats in Tunisia and Egypt, dictators are fighting back in Libya and Syria, raising questions about where the "Arab Spring" is going.

"Our message is simple," Obama said. "If you take the risks that reform entails, you will have the full support of the United States."

The dollars, however, do not back up the words. Obama proposed to relieve Egypt of \$1 billion in debt and guarantee another \$1 billion in borrowing for infrastructure and job creation. He also proposed to create Enterprise Funds to stimulate private investment in Tunisia and Egypt, and he noted that the Overseas Private Investment Corporation will provide \$2 billion to strengthen private sectors across the region.

So, rather than the enormous direct aid of the Marshall Plan, Obama proposes a few billion dollars in aid, debt forgiveness, and guarantees - at a time when the federal budget this year will total \$3.5 trillion to \$4 trillion.

Obama outlined a bold vision for advancing freedom and democracy. But, with the government swimming in red ink, he was hard-pressed to make a financial investment that does justice to the rhetoric. "The reality is that there just isn't much money around for this project," a top Obama aide told the New York Times."

It's a sad sign of the times, one that Washington will revisit frequently until policymakers address our fiscal challenges.

The Fiscal Times
May 16, 2011

Can We Afford a 'Technical Default' on the Debt?
By LAWRENCE HAAS

The debate over raising the federal debt limit - which the government reached today, according to Secretary Timothy Geithner - has morphed into a question of "compared to what."

In the Wall Street Journal's "Weekend Interview," Wall Street legend Stanley Druckenmiller argued that what he called a "technical default" - a delay of several days or perhaps a week or two before the federal government paid bond investors - would be better than having policymakers raise the debt limit in time to avoid a default but fail to also take serious steps to control spending.

The Wall Street Journal's editorial page, which argues vociferously for cutting spending, was only too happy to run the interview as well as its own follow-up editorial to heartily endorse Druckenmiller's views.

Let's take a closer look.

Druckenmiller offers a choice of two scenarios. In the first, the federal government is late to pay bond holders but, when it finally does, it also enacts "massive cuts in entitlements" as part of a return to federal fiscal sanity. In the second, the federal government makes its payments on time but doesn't do anything to control spending.

"To me, it's a no-brainer," Druckenmiller said, arguing the first scenario is far superior to the second.

Druckenmiller's analysis, however, rests on two questionable premises.

First, he says investors are sophisticated enough to read the tea leaves in Washington and that, as a result, a "technical default" of a few days would not rattle the bond markets and, in turn, hurt the economy.

Actually, Druckenmiller himself disproves his own contention. He says that, in investing his own money, he bought more Treasury securities in light of House Budget Committee Chairman Paul Ryan's calls to dramatically cut spending, saying, "I heard some serious things that I hadn't heard in a long time."

Did he really think Congress would pass, and President Obama would sign, legislation to turn Medicare into a voucher, turn Medicaid and food stamps into block grants, and reduce the federal government to its smallest size since the early 1950s? If so, then no one should assume markets are very sophisticated.

Second, Druckenmiller talks about the dire need to reduce deficits and debt by dramatically cutting spending. You'd think someone as concerned as he claims to be also would propose tax increases - especially on those who can pay more, especially with top marginal tax rates at historically low levels.

Druckenmiller, the Journal says, is worth about \$2.5 billion but, in his concern about red ink, he didn't volunteer to pay higher taxes.

How concerned can he be? And how seriously should we take his argument?