The New York Times
nytimes.com

January 8, 2004

I.M.F. Says U.S. Debts Threaten World Economy

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WASHINGTON, Jan. 7 — With its rising budget deficit and ballooning trade imbalance, the United States is running up a foreign debt of such record-breaking proportions that it threatens the financial stability of the global economy, according to a report released Wednesday by the International Monetary Fund.

Prepared by a team of I.M.F. economists, the report sounded a loud alarm about the shaky fiscal foundation of the United States, questioning the wisdom of the Bush administration's tax cuts and warning that large budget deficits pose "significant risks" not just for the United States but for the rest of the world.

The report warns that the United States' net financial obligations to the rest of the world could be equal to 40 percent of its total economy within a few years — "an unprecedented level of external debt for a large industrial country," according to the fund, that could play havoc with the value of the dollar and international exchange rates.

The danger, according to the report, is that the United States' voracious appetite for borrowing could push up global interest rates and thus slow global investment and economic growth.

"Higher borrowing costs abroad would mean that the adverse effects of U.S. fiscal deficits would spill over into global investment and output," the report said.

White House officials dismissed the report as alarmist, saying that President Bush has already vowed to reduce the budget deficit by half over the next five years. The deficit reached $374 billion last year, a record in dollar terms but not as a share of the total economy, and it is expected to exceed $400 billion this year.

But many international economists said they were pleased that the report raised the issue.

"The I.M.F. is right," said C. Fred Bergsten, director of the Institute for International Economics in Washington. "If those twin deficits — of the federal budget and the trade deficit — continue to grow you are increasing the risk of a day of reckoning when things can get pretty nasty."

Administration officials have made it clear they are not alarmed about the United States' burgeoning external debt or the declining value of the dollar, which has lost more than one-quarter of its value against the euro in the last 18 months and which hit new lows earlier this week.

"Without those tax cuts I do not believe the downturn would have been one of the shortest and shallowest in U.S. history," said John B. Taylor, under secretary of the Treasury for international affairs.

Though the International Monetary Fund has criticized the United States on its budget and trade deficits repeatedly in the last few years, this report was unusually lengthy and pointed. And the I.M.F. went to lengths to publicize the report and seemed intent on getting American attention.

"I think it's encouraging that these are issues that are now at play in the presidential campaign that's just now getting under way," said Charles Collyns, deputy director of the I.M.F.'s Western Hemisphere department. "We're trying to contribute to persuade the climate of public opinion that this is an important issue that has to be dealt with, and political capital will need to be expended."

The I.M.F. has often been accused of being an adjunct of the United States, its largest shareholder.

But in the report, fund economists warned that the long-term fiscal outlook was far grimmer, predicting that underfunding for Social Security and Medicare will lead to shortages as high as $47 trillion over the next 70 years or nearly 500 percent of the current gross domestic product in the coming decades.

Some outside economists remain sanguine, noting that the United States is hardly the only country to run big budget deficits and that the nation's underlying economic conditions continue to be robust.

"Is the U.S. fiscal position unique? Probably not," said Kermit L. Schoenholtz, chief economist at Citigroup Global Markets. Japan's budget deficit is much higher than that of the United States, Mr. Schoenholtz said, and those of Germany and France are climbing rapidly.

In a paper presented last weekend, Robert E. Rubin, the former secretary of the Treasury, said that the federal budget was "on an unsustainable path" and that the "scale of the nation's projected budgetary imbalance is now so large that the risk of severe adverse consequences must be taken very seriously, although it is impossible to predict when such consequences may occur."

Other economists said they were afraid that this was a replay of the 1980's when the United States went from the world's largest creditor nation to its biggest debtor nation following tax cuts and a large military build-up under President Ronald Reagan.

John Vail, senior strategist for Mizuho Securities USA, said the I.M.F. report reflected the concerns of many foreign investors.

"I would say they reflect the majority of international opinion about the United States," he said. And he added, "The currency doesn't have the safe-haven status that it has had in recent years."

Many economists predict that the dollar will continue to decline for some time, and that the declining dollar will help lift American industry by making American products cheaper in countries with strengthening currencies.

"In the short term, it is probably helping the United States," said Robert D. Hormats, vice chairman of Goldman Sachs International.

Fund officials and most economists agreed that the short-term impact of deficit spending has helped pull the economy through a succession of crisis. And unlike Argentina and other developing nations that suffered through debt crises, the United States remains a magnet for foreign investment.

Treasury Secretary John W. Snow did not address the fund's report directly. But in a speech to the United States Chamber of Commerce on Wednesday, he said Mr. Bush's tax cuts were central to spurring growth and reiterated the administration's pledge to reduce the deficit in half within five years.

"The deficit's important," Mr. Snow said. "It's going to be addressed. We're going to cut it in half. You're going to see the administration committed to it. But we need that growth in the economy. We had an obligation to the American work force and the American businesses to get the economy on a stronger path. We've done it and we have time to deal with the deficit."

But the report said that even if the administration succeeded it would not be enough to address the long-term problems posed by retiring baby boomers.

Moreover, the fund economists said that the administration's tax cuts could eventually lower United States productivity and the budget deficits could raise interest rates by as much as one percentage point in the industrialized world.

"An abrupt weakening of investor sentiments vis-à-vis the dollar could possibly lead to adverse consequences both domestically and abroad," the report said.