

“Don't Get Caught Holding Dollars When The U.S. Default Arrives” by Addison Wiggin July 23,2011

Greece can't solve a problem of too much debt by taking on even more. We will note, however, that by some measures, the United States is even more deeply in hock than Greece.

Greece's debt-to-GDP ratio is 143%. America's is officially 97%. But the \$14.3 trillion national debt, stacked up against a \$14.7 trillion economy, doesn't tell the whole story. Look at these numbers:

- \$14.3 trillion: “official” national debt
- \$5 trillion: Amount Uncle Sam is on the hook for Fannie Mae and Freddie Mac
- \$62 trillion: Total liabilities and unfunded obligations for Social Security and Medicare

That doesn't count the black box of bailouts.

We know how much the Federal Reserve doled out in emergency loans: \$16.1 trillion between Dec. 1, 2007, and July 21, 2010. We know that because yesterday the Government Accountability Office completed its first-ever audit of the Fed, made possible largely through the persistence of Rep. Ron Paul (R.-Tex.) making that audit, however incomplete, the law.

What we don't know is how much of that has been paid back. “We have literally injected about \$5.3 trillion,” said Dr. Paul earlier this month during his questioning of Fed chief Ben Bernanke, “and I don't think we got very much for it. The national debt went up \$5.1 trillion.”

Bernanke did not challenge those figures.

“To get our overall fiscal gap under control,” writes Boston University professor Laurence Kotlikoff in Bloomberg, “the U.S. must cut spending or raise tax revenue by \$20 trillion over the next decade, far more than either the president wants or the House Republicans seek.”

Yep: The latest number we see bruited in Washington is \$3 trillion. Whatever the final number -- and there will be a last-minute deal; there always is -- it will be substantially less than \$20 trillion over 10 years. The can will be kicked as it keeps getting kicked in Greece.

We note here that the total of outstanding credit default swaps on U.S. Treasuries crested \$4.8 billion this week. Uncle Sam has now surpassed Greece in this category.

Measured in year-over-year change, America is number one: Net notional CDS outstanding grew 109%. That means there's double the bets out there on a U.S. default compared with a year ago.

“You may not know this, but the U.S. has actually defaulted a number of times already,” writes Chris Mayer this morning. He cites five instances:

- 1779: The government was unable to redeem the continental currency issued during the Revolutionary War
- 1782: The colonies defaulted on the debt they took out to pay for the war
- 1862: During the Civil War, the Union failed to redeem dollars for gold at terms stated by the debt contracts
- 1934: FDR defaults on the debt issued to finance World War I, refusing to redeem it in gold. The dollar is devalued 40% against gold
- 1979: A bureaucratic snafu results in interest going unpaid on some small bills.

“With the exception of 1979,” Chris says, “which was mostly due to administrative confusion -- the U.S. simply ran out of money each time. The end result was the dollar had to be devalued. Meaning it lost significant purchasing power.

“My guess is that the U.S. will default again. It may not technically be called that, but the only way for the U.S. to meet its financial obligations is to print a lot of money.”

What does that mean in practical terms? In Greece, professor Savas Robolis at Panteion University in Athens reckons that by 2015, the average Greek employee and pensioner’s standard of living will have fallen 40% compared with 2008.

Even now, Americans are turning to their credit cards to pay for groceries and gas. According to First Data Corp., the volume of gasoline purchases put on credit cards jumped 39% over the last 12 months.

You don’t want to be the average American in a default scenario, whenever it arrives. Ray Dalio, the head of Bridgewater Associates, the world’s biggest hedge fund, puts that day in “late 2012 or early 2013.”

<http://news.yahoo.com/dont-caught-holding-dollars-u-default-arrives-191153227.html>