The Federal Reserve Wages War on the Federal Government Spending Spree

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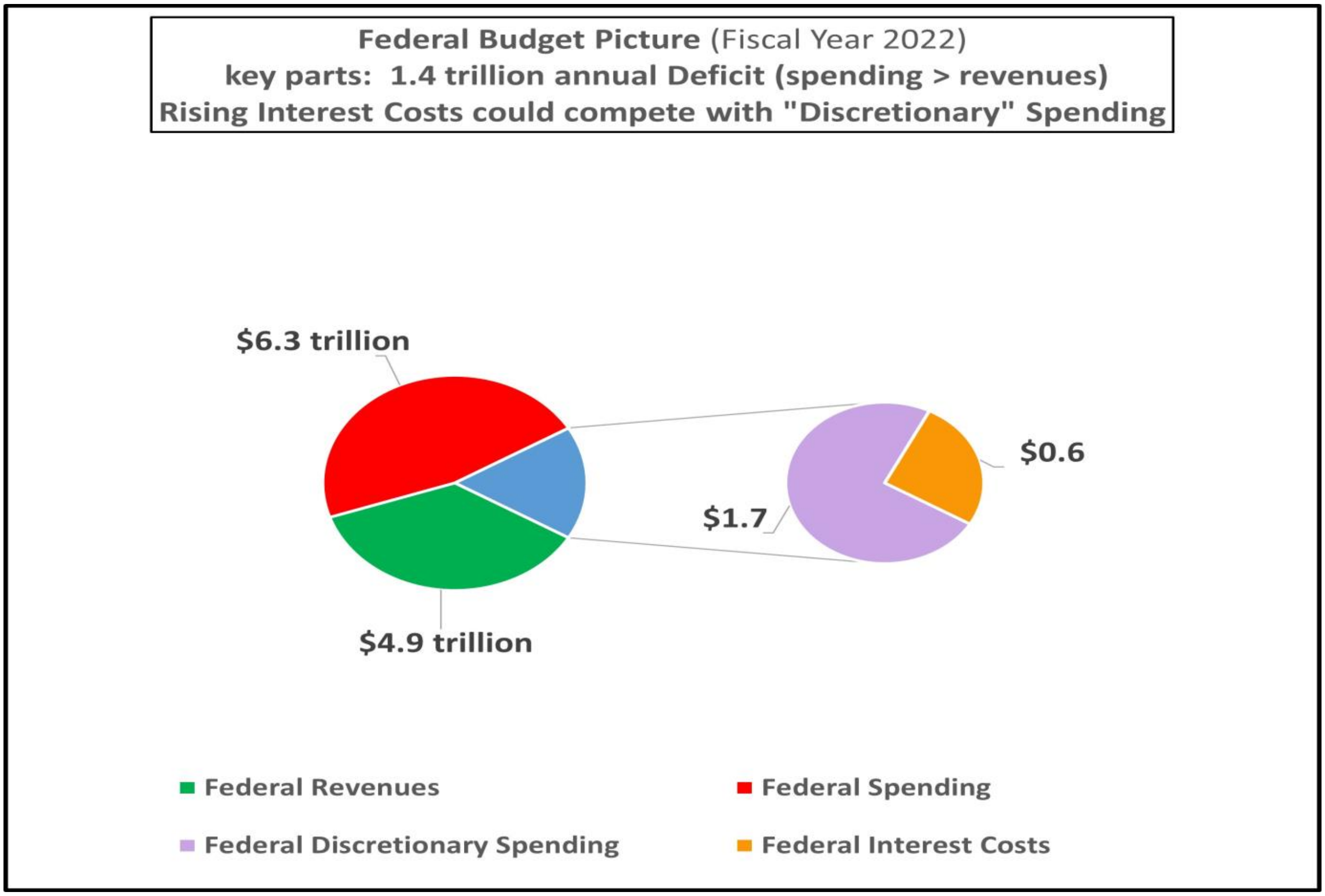

<u>Unchecked federal government spending causes the national debt to balloon.</u>

According to the U.S Department of the Treasury, the federal government spent approximately $6.3 trillion (the red slice in the left pie chart above) and collected in revenue $4.9 trillion (the green slice in the left pie chart) in fiscal year 2022 – making for an annual deficit of $1.4 trillion. * This deficit continues a string of rather large annual deficits that now accumulates into a total federal government debt of over $30 trillion.

The right pie chart above compares the federal government's "discretionary" spending ($1.7 trillion) against the federal government's net interest costs for servicing its debt ($0.6 trillion), in fiscal year 2022.

<u>The sharp rise in interest rates, if sustained, could require painful federal budget changes.</u>

In Fiscal Year 2022, the average interest rate paid by the federal government to service its debt is about 2%. However, interest rates are now spiking to nearly 5% for issuing new federal debt (treasury bills, notes and bonds).

The average maturity of the federal government's debt is said to be six years; and so, if interest rates remain at 5% for the next few years, the federal government's average interest rate for servicing its debt will increase by about 150% - what with its existing low interest rate debt having matured and in need of refinancing.

Consequently, even if the annual federal deficit is reduced to zero immediately, the interest costs on the national debt will still balloon from $0.6 trillion to $1.5 trillion – given the Federal Reserve's current tighter money policies.

<u>What this means is that the ballooning cost of servicing the interest on the national debt could require drastic cuts ($0.9 trillion) to the federal government's "discretionary" spending.</u> (In this case, the purple slice of the right pie chart above shrinks from $1.7 trillion to just $0.8 trillion.)

However, "discretionary" spending is not really discretionary, as most people think of it. This is because the federal government categorizes national defense spending ($0.7 trillion) as "discretionary." It also includes as discretionary its spending on transportation, housing and social services. Note that both social security spending ($1.2 trillion) and Medicare spending ($0.7 trillion) are categorized as mandatory.

<u>The prospect of ballooning interest costs maybe took down House Speaker McCarthy?</u>

The Federal Reserve has orchestrated a rise in interest rates for new federal government borrowing to approximately 5% over the past year and a half. The Federal Reserve is no longer a net buyer of U.S debt (as it has ended its decade long easy money, "quantitative easing program" in which the Federal Reserve lends trillions of dollars at minimal rates of interest to the federal government.) Prospects for sustained 5% interest rates pressure Congress to consider painful budget decisions, if not leadership changes.

House Speaker McCarthy(R) at the "eleventh hour" on Saturday, September 30, 2023, effectively capitulated to the U.S Senate controlled by Majority Speaker Schumer (D) and a short-term continuing budget resolution to keep federal spending far in excess of federal revenue collection is passed with the help of House Democrats. This seems to in part cause Representative Gaetz(R) to almost immediately submit McCarthy's continued speakership to a vote, and on Tuesday October 3, 2023, McCarthy is indeed voted out as Speaker.

<u>Coping with ballooning interest costs on the national debt won't be easy.</u>

There are those who opine that the U.S can inflate its way out of its burgeoning national debt. However, I would note that much of the federal government's spending is indexed to inflation. So, this approach to diminishing the national debt burden seems rather uncertain.

The U.S Congressional Budget Office (CBO) lists numerous policy options for at least partially reducing the annual federal deficit (lowering the rate of growth in the national debt, that is.)

The CBO lists among policy options: reducing Medicaid and Medicare spending, raising income tax rates, and/or imposing a tax on carbon dioxide emissions.

But missing from the CBO list of deficit reducing options is that of paring back regulatory burden. I should think that reducing regulatory burden could allow tax rates to remain unchanged and yet increase federal revenues - unchanged income tax rates applied in a larger economy generating higher earnings for the nation as a whole. Investor's Business Daily reports that economic regulatory burden costs the nation as much a $4.0 trillion per year.

Well, I end by quoting Yogi Berra: "It's tough to make predictions, especially about the future."

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* Please note that the Blue Pie Slice of the left pie chart compares the total amount of federal discretionary and interest spending against the total amount of all federal spending (in red) and the total amount of all federal revenue (green). As such, this blue slice is intended to demonstrate the interplay between total federal spending, revenue, and the two federal spending subcategories – Discretionary and Interest.)