THE STRATEGIC IMPLICATIONS OF THE U.S. DEBT

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THE STRATEGIC IMPLICATIONS OF THE U.S. DEBT

WEDNESDAY, APRIL 6, 2016

U.S. SENATE,
COMMITTEE ON FOREIGN RELATIONS,
Washington, DC.

The committee met, pursuant to notice, at 2:19 p.m., in Room SD–419, Dirksen Senate Office Building, Hon. Bob Corker, chairman of the committee, presiding.
Present: Senators Corker [presiding], Risch, Rubio, Johnson, Flake, Gardner, Perdue, Isakson, Cardin, Murphy, and Markey.

OPENING STATEMENT OF HON. BOB CORKER,
U.S. SENATOR FROM TENNESSEE

The CHAIRMAN. The Senate Foreign Relations Committee will come to order. We want to thank you both for being here.

We were just remarking in the back that, typically, we have witnesses that have generally had some degree of overlap in thinking, and it has really helped our committee develop bipartisan consensus on so many issues. I will say that, today, that is not going to be the case. I really am stunned by the testimony of one of our witnesses today.

The issue of our national debt has been an issue that our top military officials, Presidents on both sides of the aisle, and Secretaries of State on both sides of the aisle have considered to be a major threat to our Nation and limits our ability to respond to crises. I have been in several meetings today where other countries have been concerned about how we are going to be able to react to certain things.

So I really am stunned by the testimony of one of our witnesses today, and I look forward to probing that, having received a summary of those statements.

I think it is bipartisan, the idea that we have to figure out a way to come together and grind through the tough issues that our Nation is facing to ensure that we do not continue with the generational theft that is occurring right now, where we run deficits that future generations will pay.

Again, it has been a significant national security issue. It is something that I think is important for us. And therefore, I am glad we are having the hearing today and certainly the forward to the questioning that will take place.

So with that, I will turn to our ranking member, and I am sure he will have other comments to make relative to what is getting ready to happen.
STATEMENT OF HON. BENJAMIN L. CARDIN, U.S. SENATOR FROM MARYLAND

Senator CARDIN. Mr. Chairman, I am not sure which of the testimonies—[Laughter.]

Senator CARDIN. Mr. Ambassador, I will try to help you out during the course of the hearing.

I want to welcome both of our witnesses here. I am familiar with your statements, and I think there is a lot in both of these statements that is important for us going forward with our national security. And I look forward to this hearing, because there are two sides of the ledger.

Obviously, the amount of debt that we incur every year is a matter of national security. We have to borrow the money. We borrow it from Americans. But we also borrow it from foreign interests, and that should be of concern to the United States. We also should pay our bills. That should be of concern to this country.

But I just point out, on that side of the ledger, when you look at the cost of U.S. borrowing, when you look at the desirability of U.S. security, the international community does not seem to be too concerned about the amount of debt that we are issuing, from the point of view of the attractiveness and the cost of U.S. debt.

Having said that, I agree that we need to do a better job on fiscal responsibility, and we should be paying more of our current expenses, which deal with how much money we spend and how much tax we collect, which brings me to the other side of the ledger dealing with national security.

I think it is critically important the amount of money we, for example, spend for our defense and for our military. That is an important part of national security. The amount of money we invest in diplomacy and development assistance is part of our national security.

So if we were to say, look, we will have less debt, but let’s cut our military in half, and let’s cut our national development assistance in half, I think that would compromise U.S. security. So how do we invest our money?

But the other part of that, Mr. Chairman, is how do we invest in America? How do we invest in our roads, our bridges, our energy infrastructure? How do we invest in education and educating our workforce? How do we deal with climate change, which is presenting an international security issue? All of that requires expenditures on the spending side.

So as we look at national security and the amount of debt that we acquire every year, we have to be concerned about debt. But we also have to be concerned about whether we are spending money at the level we should for the United States to maintain its position as the world’s superpower.

So I think both of our witnesses will give us different perspectives, but I agree with both, in that we have to be concerned about both sides of the ledger.

And I look forward to the testimony, and I look forward to a robust discussion here today.

Now you are shocked with the ranking member.

The CHAIRMAN. I am, actually. So I hate that our distinguished Council on Foreign Relations leader is actually participating in this
the way that it begins, but I do thank him for lending a staff mem-
ber to us to run our committee, and I turn to both of you.

Our first witness is the Honorable Richard Haass, president of
the Council on Foreign Relations. Our second witness today is
Neera Tanden, president and CEO for the Center for American
Progress. I want to thank you both for being here and sharing your
comments.

I think you all know the drill, and that is, we have received your
written testimony. If you could summarize that, and then look to
questions, I would appreciate it.

But thank you both again for being here, again, on a topic that
I thought there would be general uniformity around, but appar-
ently, already, because this may be perceived to be a reflection on
somebody, I do not know—but I do look forward to the testimony.
Thank you very much.

Mr. Haass, if you would begin?

STATEMENT OF HON. RICHARD HAASS, PRESIDENT, COUNCIL
ON FOREIGN RELATIONS, NEW YORK, NY

Ambassador Haass. Thank you, Mr. Chairman. I want to thank
you and the committee for the opportunity to testify.

I just want to make clear that I am speaking for myself and not
for the Council on Foreign Relations.

But I do want to commend you and your colleagues here for hold-
ing this hearing and for considering the issues of debt and national
security an integrated matter. It is important that they are not
seen as distinct. There is an important degree of overlap.

What makes this issue particularly difficult is it is an example
of what I would describe as a slow-motion crisis. Slow-motion crises
tend to be phenomena that are underway and that have potentially
substantial or even devastating consequences that will kick in
gradually or only after the passage of considerable time.

There is good and bad news in this. The good news is that, to
a large degree, we know where things are heading, and we have
time to do something about it. The bad news is that slow-motion
crises tend to generate little or no sense of priority but rather tend
to promote complacency.

The problem then is that we will forfeit the opportunity not just
to prevent the crisis, but we end up denying ourselves remedies
that are not severe.

The debt problem is straightforward, I would think. According to
the CBO and others, U.S. public debt is fast approaching a level,
plus or minus, of $14 trillion. That is roughly equal to 75 percent
of our current GDP. In a decade, debt will probably be between 80
percent and 90 percent of GDP.

It is a question of when, and not if, the debt comes to exceed or
far exceed GDP. That could happen in 15 years or even sooner.

Let me say that this is a problem that not only will not fix itself,
but it will grow worse. The principal driver of spending increases
are entitlements, and that will become more of a factor as Ameri-
cans of my generation retire in large numbers and live longer lives.

Second, interest rates are at or near historic lows and are far
more likely to rise than fall over the next few decades.
Now specific projections as to the size of the debt and what it will cost to finance necessarily vary depending upon assumptions about economic growth, spending, taxation, and interest rates. But the trend is clear, and the trend is not our friend.

There are a good many strategic consequences of our growing indebtedness. Let me just go through them rather quickly.

First, the need to finance the debt will absorb an ever-increasing amount of dollars and an ever-increasing share of the U.S. Federal budget. This will mean proportionally fewer resources will be available for national security, including defense, intelligence, homeland security, foreign assistance, and diplomacy. There will, as well, be fewer dollars available for discretionary domestic programs, ranging from education and infrastructure modernization to scientific research and law enforcement.

Second, our inability to deal with our debt challenge will detract from the appeal around the world of the American political and economic model. It will make others less likely to want to emulate us and more wary of depending on us. The result would be a world that is less democratic and increasingly less deferential to U.S. security concerns.

Third, mounting debt will leave the United States more vulnerable to the whims of markets and the machinations of governments. Already, approximately half of U.S. debt is held by foreigners. China is one of the two largest lenders, as you pointed out, Senator. I am not sanguine that China would not decide to slow or stop accumulating U.S. debt as a signal of displeasure, or even sell debt amidst, say, a crisis over Taiwan or the South China Sea.

Fourth, mounting debt could absorb funds that would otherwise be invested at home or abroad. This will depress already modest levels of economic growth. High levels of debt and debt financing will increase concerns about the government’s willingness to maintain the dollar’s value. This will cause lenders to demand higher returns on their loans, something that will increase the cost of debt financing and further crowd out other spending and further depress growth. This is what we call a vicious, not a virtuous, cycle.

Fifth, mounting debt limits American flexibility and resilience. There is no way of stating in the abstract what is the right level of debt for the United States, or knowing what level of debt is sustainable. But the United States does not want to make high levels of debt the new normal. We need flexibility should there be another financial crisis that requires large-scale fiscal stimulus or an unexpected major national security challenge that demands a costly response.

Keeping debt levels low enough to allow for a surge, essentially to give ourselves some cushion to allow for a surge in spending without triggering an even worse debt crisis, seems to be a prudent hedge and worth paying a reasonable premium for.

Sixth and last, mounting debt will hasten the demise of the dollar as the world’s reserve currency. This will happen as a result of the loss of confidence in U.S. financial management and the related concern that what the United States will need to do to finance its debt will be at odds with what it should be doing to manage the U.S. and, indirectly, the world economy.
And make no mistake about it, a post-dollar world will be both more costly and one of less leverage when it comes to imposing dollar-related sanctions.

Mr. Chairman, I have a number of suggestions as to what should and should not be done to address this looming crisis, one that threatens American prosperity and American national security alike. I look forward to the comments and questions from yourself and your colleagues.

[Ambassador Haass’s prepared statement follows:]

PREPARED STATEMENT OF RICHARD N. HAASS,
PRESIDENT COUNCIL ON FOREIGN RELATIONS

Mr. Chairman, I want to begin by thanking the committee for this opportunity to testify. I should also make clear that I am speaking for myself and not for the Council on Foreign Relations, which takes no institutional position on this or any other matter of public policy. But before I turn to the subject matter of today’s hearing, I also want to commend the Chairman and the members of the committee for holding this hearing. People often talk about issues such as the debt and issues involving national security, but rarely do they bring the two together and talk about them at one and the same time in an integrated manner. What you are doing here today is just what is needed; as I am fond of pointing out, universities have departments but the world does not.

I would add that what makes this issue particularly difficult is that it is part of a class of what I would describe as slow motion crises. Slow motion crises are just that: phenomena or processes that are under way and that have potentially substantial or even devastating consequences that will kick in gradually, or, even if suddenly at some point, only after the passage of considerable time. They are thus fundamentally unlike an infectious disease outbreak or a financial collapse.

There is both good and bad news in this. The good news is that to a large degree we know where things are heading. We also have time to do something about it. We can see the iceberg in our path, and there is ample time to turn the ship around. The bad news is that slow motion crises generate little or no sense of priority but rather tend to promote complacency. The temptation is to put them aside, to focus on today’s crisis, to allow the urgent to take precedence over the important. The problem with this is that we will forfeit the opportunity not just to prevent a crisis from materializing but we deny ourselves those remedies that are not severe. To switch analogies, the medical equivalent would be to ignore the symptoms in the patient when the sickness was relatively easy to treat and to wait to do something only when it became life threatening.

The problem being addressed here today is fairly straightforward. According to the Long-Term Budget Outlook released in June 2015 by the Congressional Budget Office and the CBO’s more recent (January 2016) ten year Budget and Economic Outlook, the public debt of the United States is fast approaching $14 trillion. It now is equal roughly to 75% of GDP and in a decade will reach between 80 and 90% of GDP. Depending upon spending and revenue assumptions, it is a question of when and not if the amount of debt comes to exceed or far exceed GDP. This could well happen by 2030. What it will cost to service the debt will begin to rise rapidly, consuming an ever larger percentage of GDP and federal spending.

I should note that this prediction is not universal, and that there are those who think it too negative based on revenue and rate predictions and above all on larger than expected cost-savings in the medical domain. This is of course possible, but so too is a worse than expected future based on slower growth, higher rates, higher than expected medical costs owing to a larger aging population, and much higher than imagined costs associated with adapting to the many effects of climate change.

The causes of the debt problem are somewhat more controversial but still fairly straightforward. Although the federal deficit is considerably lower than it was just years ago, it is once again increasing, the result of greatly increased spending in select areas and low rates of economic growth. Some would say taxes or rather the lack of them are to blame as well, but U.S. corporate rates are high by global standards and individual rates are not conspicuously low.

All things being equal, the problem will not only not fix itself but will grow worse. There are at least two reasons. First, the principal driver of spending increases, spending on entitlements such as Medicare, Medicaid, and Social Security, will likely become more not less of a factor as Americans retire in large numbers and live
longer lives. Second, interest rates are near historic lows and are far more likely to rise than fall over future decades. Specific projections as to the size of the debt and what it will cost to finance necessarily vary depending on assumptions regarding economic growth, spending, taxation, inflation, and interest rates, but the trend is clear, and the trend is not our friend. Nor is time.

There are a good many foreseeable strategic consequences of growing indebtedness. Let me suggest several:

The most direct is that the need to finance the debt will absorb an ever-increasing amount of dollars and an ever-increasing share of the U.S. budget. This will mean proportionately fewer resources will be available for national security, including defense, intelligence, homeland security, and foreign assistance. There will as well be fewer dollars available for discretionary domestic programs ranging from education and infrastructure modernization to scientific research and law enforcement. What this portends is an increasingly sharp and destructive debate over guns versus butter while the two fastest growing parts of the budget, debt-service and entitlements, remain largely off limits.

Mounting debt will raise questions around the world about the United States. Our inability to deal with our debt challenge will detract from the appeal of the American political and economic model. It will make others less likely to want to emulate U.S. and more wary of depending on U.S. as it will raise questions about this country's ability to come together and take difficult decisions. The result would be a world that is less democratic and increasingly less deferential to U.S. concerns in matters of security. To some extent this is already happening; not dealing with our debt promises to make a worrisome evolution that much more so.

Mounting debt will leave the United States more vulnerable than it should be to the whims of markets and the machinations of governments. Already approximately half of U.S. public debt is held by foreigners, with China one of the two largest lenders. There are those who say not to worry about this, that China will be constrained by its interest in not seeing its own huge pool of dollars lose its value and by its need for the United States to continue to buy its exports. The result, according to this line of thinking, is the financial equivalent of nuclear deterrence. This may be true, but I for one am not sanguine that China would not decide to slow or stop accumulating U.S. debt as a signal of displeasure or even sell debt amidst say a crisis over Taiwan. In such circumstances, Chinese leaders might well judge it was worth paying a financial price to protect what they viewed as their vital national interests. Interestingly, it was American threats aimed at the pound sterling that more than anything else persuaded a British government that was fearful of the need to devalue its currency to back off its ill-fated venture to regain control of the Suez Canal in 1956.

Mounting debt could absorb funds that could otherwise be usefully invested at home or abroad. This will in turn depress already modest levels of economic growth. Making matters worse is that high levels of debt and debt financing will increase concerns about the government's willingness to maintain the dollar's value or worse yet meet its obligations. This will cause foreigners in particular to demand high returns on their loans, something that will increase the cost of debt financing and further crowd out other spending and further depress growth. This is a vicious, not a virtuous, cycle.

Mounting debt limits American flexibility and resilience. There is no way of stating in the abstract what constitutes the right level of debt for the United States or knowing with precision what level is sustainable. But the United States does not want to make high levels of debt the new normal as it removes flexibility if, for example, there were to be another financial crisis that required large-scale fiscal stimuli or an unexpected major national security challenge that demanded a costly response. Keeping debt levels low enough to allow for a surge in spending without triggering a debt crisis seems to be a prudent hedge and, as is the case with preventative medicine or insurance, worth paying a reasonable premium for.

Let me just add one more prediction. Mounting debt will hasten the demise of the dollar as the world's reserve currency. This will happen as a result of loss of confidence in U.S. financial management and the related concern that what the United States will need to do to finance its debt will be at odds with what it should be doing to manage the U.S. and indirectly world economy. It is possible such a move away from the dollar would have happened were it not for the EU's problems and China not being prepared to free up the yuan. But the United States cannot depend forever on the weaknesses and errors of others, and a post-dollar world will be both more costly (as it will require Americans to move in and out of other currencies) and one of less leverage when it comes to imposing dollar-related sanctions.
I understand it may be somewhat beyond the purview of today’s hearing to offer up prescriptions about what needs to be done. That said, I find it impossible to resist laying down a few markers.

A big driver of the debt will be the cost of entitlements. We need to raise the current and projected retirement age so that Social Security better reflects economic and demographic realities. It would also make sense to subject Social Security to a means test and reduce payments to the relatively wealthy for whom by definition such payments are not essential, to moderate cost of living adjustments, and to reform the fast-growing Disability program.

Medicare and Medicaid are even more responsible for the entitlement burden. Some changes that could help here include accelerating the move away from a system based on fee for service and towards one that reflects quality of outcomes, finding a way to better deal with so-called “dual eligibles” who qualify for both Medicare and Medicaid, raising the age of Medicare eligibility, increasing co-payments, limiting malpractice torts, and introducing some means-testing of benefits.

Congress should avoid false “solutions.” The sequester is one of them. It ignores entitlements and favors both spending over investment and the present over the future. It should be jettisoned once and for all. The same holds for threats not to raise the debt ceiling. As every senator knows, failure to raise the debt ceiling does nothing to limit debt already incurred but it does raise major doubts in markets and around the world as to whether the United States is reliable and serious. Ironically, failure to raise the debt ceiling would trigger reactions that would lead to an increase in rates, something that in turn would slow growth and exacerbate the debt burden.

Congress needs to be similarly careful about cutting defense. Current and projected defense spending is around 3% of GDP, far below historic averages. What is more, it is an increasingly dangerous and precarious world out there, and if the world becomes messier, there is no way the United States will be able to wall itself off from consequences partly brought about by our doing less. There is no other country willing and able to make a sizable contribution to order, and the world cannot order itself. Only the United States can play this role. The good news is that we can do so and tackle our debt challenge at one and the same time if we spend our resources wisely.

What would help as much as reducing entitlements would be taking steps to increase economic growth. My list includes better K-12 as well as life-long education, a robust public/private infrastructure modernization program, immigration reform that creates greater opportunities for those with advanced degrees and needed skills to come and stay here, reform of corporate taxes so more money comes back to this country and is put to use, a reduction in so-called tax-expenditures such as the mortgage interest deduction and a decision to tax employer contributions for health care premiums, and passing the Trans-Pacific Partnership and other trade pacts.

Mr. Chairman, let me conclude where I began, by commending you and your colleagues for putting a spotlight on this issue. You will have performed an important public service if this hearing leads to more people in this country viewing our current and future debt not simply as an economic or domestic concern but also as a significant threat to this country’s national security.

Thank you. I look forward to any questions you may have.

Ms. Tanden?

STATEMENT OF NEERA TANDEN, PRESIDENT AND CEO, CENTER FOR AMERICAN PROGRESS, WASHINGTON, DC

Ms. Tanden. Thank you so much, Chairman Corker, Ranking Member Cardin, and members of the committee. My name is Neera Tanden. I am a co-founder of the Center for American Progress, and I am very grateful for the opportunity to testify today.

I do hope we find some areas of common ground. I actually see some areas of common ground on these issues between Ambassador Haass and myself.

CAP is an independent, nonpartisan educational institute dedicated to improving the lives of Americans through practical ideas and actions. At CAP, we believe that a robust middle class is vitally important to growing a stronger and more prosperous econ-
omy. I know that is a matter of concern for every member of this committee.

I deeply appreciate the opportunity to speak to you on the broad topic of America’s standing in the world, and how our economic success is a critical component of that. In fact, I could not agree more that our economic strength as a Nation helps determine our international strength.

Where I may have a different focus is the source of that strength. I believe that the strength of our middle class has long been a key aspect of our international appeal. The American middle class is not only the engine of our Nation’s economic growth, it is a symbol of our ideals, a promise that no matter what you look like or where you come from, you can succeed in the United States.

Indeed, we have served as a bright beacon for economic opportunity. Immigrants from every country, including my own parents, have come to our shores in search of a better future for themselves and their families.

But truthfully, we are at a crossroads. We are failing in many ways to live up to that promise for America’s families.

I do believe that our national debt is a long-term problem that we have to solve. Leadership is needed to address that challenge. But I also believe that the struggles of the middle class and those trying to get into the middle class is an urgent problem, not just an urgent moral problem, but a challenge for economic growth, writ large.

While the recovery from the recession has been important, it remains incomplete. There is, so far, little evidence that U.S. Government debt is currently creating obstacles to further economic growth or threatening our national security.

I want to say again, we do need to tackle the national debt over the long term. The question is, where are our priorities?

When you look at our recovery, it has outpaced the recovery of our allies who have almost exclusively focused on debt. The European Union has grown at a much lower level—1.5 percent compared to the United States’ 2.5 percent—and is projected to continue to grow at a much slower pace than the United States. These are the results of greater austerity.

Now, we have been told time and time again, that the national debt will lead to higher national interest rates. That is usually how it works. However, we simply have not seen those predictions of higher interest rates pan out.

The CBO has been predicting for years that Treasury interest rate increases were just around the corner. In February 2013, for example, CBO predicted that the interest rate on 10-year Treasury bonds would be 4.3 percent in 2016. On April 4, 2016, the interest rate was actually 1.78 percent.

Moreover, we have heard claims that our debt-to-GDP ratio is a sign of impending crisis. But we have not seen that either. We have seen projections that our debt-to-GDP ratio would at this point be hovering over 90 percent. We are now at 74 percent. And we know that other countries have sustained higher debt-to-GDP ratios without experiencing a debt crisis.

Again, the question is not whether we should address these challenges; the question is, “what is the best way to do so?”
When it comes to addressing deficits, CAP believes that we should have a balanced approach. We have proposed a plan to eliminate the deficit over the next several decades to get us to zero, to get to a place where we are actually addressing the debt overall. We’ve proposed a balanced package that requires additional revenue as well as savings in a variety of programs, including savings in the Medicare program.

So in short, I would just like to thank everyone for the ability to participate in this hearing. I think that America’s strength comes, in part, from its economic standing. But as we see in today’s national debate, Americans are concerned about a whole range of issues not just not our ability to address debt, but also how our economy is functioning, how it is producing prosperity, and whether all Americans can share in that prosperity. Thank you all very much.

[Ms. Tanden’s prepared statement follows:]

PREPARED STATEMENT OF NEERA TANDEN,
PRESIDENT, CENTER FOR AMERICAN PROGRESS

Chairman Corker, Ranking Member Cardin, and fellow members of the Senate Foreign Relations Committee. My name is Neera Tanden, and I’m the president of the Center for American Progress (CAP). I want to thank you for the opportunity to testify before you today.

CAP is an independent, nonpartisan educational institute dedicated to improving the lives of all Americans through progressive ideas and action. At CAP, we believe that a robust middle class is vitally important to growing a stronger and more prosperous economy. That’s one of our core priorities, and I know it’s a priority of every member of this committee.

I appreciate the opportunity to speak to you on such a critical topic: how America’s economic success is critical to maintaining our unmatched international standing. Indeed, I could not agree more that it is a central part of our international strength. Where I may have a different focus is the source of that strength. I believe that the strength of our middle class has long been the key to our international appeal. The American middle class is not only the engine of our nation’s economic growth—it’s a symbol of our ideals, a promise that—no matter what you look like or where you come from—if you work hard and play by the rules, you have a fair shot at success.

Indeed, America has served as the world’s brightest beacon of economic opportunity. Immigrants from every country—including my own parents—have come to our shores in search of a better future for themselves and their families.

Today, we’re failing to fulfill that promise for too many American families. While our national debt is a long-term problem that we can and should tackle, the struggles of our middle class and those trying to get into it is an urgent problem—and, I believe, the proper concern of this committee and Congress.

Introduction and Background

The U.S. economy is a vital source of our international power and influence. A strong economy is one that fully utilizes its resources and makes critical investments to increase prosperity for all of its citizens.

In the aftermath of the financial crisis, the U.S. and our allies were pushed to the economic brink, suffering massive losses in jobs, revenue, private investment, and ultimately, growth. Faced with these challenges, our countries had two options: invest in our economy to spur recovery, or enact harsh austerity measures that would shrink growth and burden working families.

The Obama administration acted swiftly to combat this sharp decline in demand with fiscal stimulus, and prevented the U.S. economy from sliding into an even deeper recession—and quite possibly a second Great Depression. The interventions taken by this administration saved entire industries and sectors of the U.S. economy from collapse.
In fact, our recovery has outpaced some of our allies who chose to implement harmful austerity measures. In 2015, the U.S. was the fastest growing G-7 country (Canada, France, Germany, Italy, Japan UK, US), and the International Monetary Fund projects that we will continue to lead G7 growth in 2016 and 2017. While countries in the European Union grew at an average rate of 1.5 percent in 2015, the U.S. economy grew 2.5 percent and is projected to continue to grow a half a percent faster than other advanced economies. Indeed, Federal Reserve Chair Janet Yellen noted last week that while the outlook for the U.S. economy is favorable, its biggest threat is a weak global economy dragging down manufacturing and net exports.

Despite the limits placed on U.S. investment in the recovery, much progress has been made. Millions of jobs have been created, unemployment has fallen dramatically, and long-term debt projections have improved as well. And projections for growth in federal health care spending are down under the Affordable Care Act, even as we addressed a major national challenge by expanding health insurance to millions of uninsured Americans. In fact, the Congressional Budget Office recently published data showing that the total estimated federal spending for major health care programs in fiscal year 2016 will be lower than the FY 2016 projection the office published in January 2009.

While the recovery from the recession remains incomplete, there is no evidence that the U.S. government debt is currently creating obstacles to further economic growth. To the contrary, many economists argue that now is the time to invest significantly in infrastructure, research and development, education, and other productivity-enhancing investments that will boost demand and produce long-term economic returns. That is because despite our broad economic growth rate, a clear problem remains weak demand. And weak demand is in part a product of stagnant wages. Between 2001 and 2015, our economy’s productivity grew about two percent a year. During that same time period, real wages for most workers grew less than one percent per year. Despite the Great Recession, our economy has managed to grow, but the benefits of growth haven’t reached most workers.

Using National Debt for National Strength

The United States is the strongest nation in the world. And when it comes to our economic and national security, we cannot afford to let false assumptions distort our choices. Neither our allies nor our adversaries doubt American strength or leadership. Nor do financial markets treat the U.S. debt as anywhere close to an immediate concern. Some predicted that there would be a sharp reversal in the willingness of creditors to lend to the U.S. government by now. But this thinking assumes that lenders will lose confidence in the America’s ability to repay its debts. Frankly, there is no empirical basis whatsoever for this belief.

Throughout the Great Recession and subsequent recovery, the market has yet to worry about a U.S. debt crisis—except for the manufactured crisis around the debt ceiling. We know this because both inflation and interest rates on Treasury bonds are at very low levels. This includes long-term Treasury interest rates and long-term inflation expectations. In fact, U.S. debt remains the world’s safest investment. Time and again, we have been told that the debt will spell economic doom in the form of high interest rates. And in the fiscal outlook from the Congressional Budget Office, one of the major reasons for increasing deficits in future years is that CBO assumes that interest rates on Treasury bonds will increase to more normal levels.

6 Federal Reserve Economic Database, “Nonfarm Business Sector: Real Output Per Hour of All Persons,” “Average Hourly Earnings of Production and Non-Supervisory Workers,” available at https://research.stlouisfed.org/fred2/series?series_id=?444. Average hourly earnings were deflated with the Personal Consumption Expenditure Chain-Type Price Index.
from their current lows. But CBO has been predicting for years that Treasury interest rate increases were just around the corner. In February 2013, for example, CBO predicted that the interest rate on 10-year Treasury bonds would be 4.3 percent in 2016. On April 4, 2016, this interest rate was actually 1.78 percent.

The budget outlook has improved dramatically as a result of lower-than-expected interest rates. That does not mean interest rates will not rise in the future, but we should not take it as a given that they will rise as quickly or as high as has been predicted. A small difference in interest rates can make an enormous difference in both economic growth and fiscal costs.

 Moreover, we have heard claims that our debt-to-GDP ratio is a sign of impending crisis. This, too, does not square with the facts. In 2015, the U.S. debt-to-GDP ratio was about 74%. Many countries have sustained higher debt-to-GDP ratios without experiencing a debt crisis. Some countries, such as Russia and Iran, have much larger economic problems than the United States while also having lower debt-to-GDP ratios. This ratio does not independently determine the health of an economy.

We should also remember that the U.S. dollar is the global reserve currency, our debt is financed in U.S. dollars, and we maintain sovereign control of our monetary and currency policy.

If there is a surplus of savings in the global economy—as many economists believe—that would explain why interest rates may remain low for a prolonged period of time. A high supply of savings without enough opportunities for productive investment would force savers to accept lower interest rates since they do not have better options to invest their money. This would also mean that we should increase public investment in order to put more of this surplus savings to productive use.

When used to support smart policy choices, the national debt can improve our economy and enhance our national security. When used to support poor choices—like the Iraq War or massive tax cuts for the wealthiest Americans—it harms both our economy and national security.

The Center for American Progress recognizes that debt and deficits are a long term challenge we should take reasonable steps to address. By implementing balanced and gradual policies to address the nation’s long-term fiscal challenges, we can prevent the need for more catastrophic measures and protect the integrity of vital programs like Social Security, Medicare, Medicaid, and SNAP that are fundamental to economic growth and middle-class prosperity. We have proposed eliminating the deficit by 2038. Our plans shows that it is possible to pursue progressive fiscal policies, preserve the basic social safety programs, and adequately fund defense, while maintaining a manageable level of debt. The CAP budget plan made significant investments to strengthen the middle-class and grow the economy. It also gradually balanced the budget, primarily by enacting policies to slow the growth of health care costs and raise an adequate level of revenue to meet the needs of an aging population. By FY 2040, our plan would reduce total outlays by 3.3% of GDP and increase total revenues by 3.7% of GDP, relative to the budget baseline from 2015. This would produce a budget surplus of 0.6% of GDP in FY 2040, which is more than enough to reduce the debt as a share of the economy.

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Numerous bipartisan commissions have recognized that revenues are a necessary element of any responsible long-term budget plan. Instead of signing pledges to oppose any increase in tax revenues, lawmakers must work together to pass a budget that bolsters the middle class and makes critical investments in our country’s economic future.

With new revenue streams and smart investments in the engines of economic growth, we can gradually reduce our debt and ensure future security and stability.

Make Critical Investments in Our Future

For the U.S. to maintain global leadership and ensure national security going forward, we must make smart choices in both foreign and domestic policy, including how to best use U.S. borrowing capacity.

The best ways to promote economic growth is through a strong and stable middle class with growing incomes. At a time when stagnant incomes remain a drag on the economy, we need some investments to foster shared prosperity. Growing the economy will not only ensure future security but reduce the debt burden in the long-run.

Much like a family seeking to buy a car or a house, debt should be viewed as tool to make productive investments today and finance their payment over many years, rather than in a single cash payment. The federal budget is not the same as a household budget, however, and our government has a greater capacity to borrow and finance urgent needs than a family or a business. That is why it is essential to consider debt and deficits from the perspective of the entire economy and the entire nation.

The very foundation of U.S. economic strength and security is a vibrant middle class. In recent decades, the very existence of the American middle class has been threatened by growing inequality and a lack of broadly shared prosperity. With interest rates still near record lows and wage growth still weak, now is the moment to make smart public investments to help restore a strong middle class, support future productivity growth, and enhance America’s standing in the world.

Middle-class prosperity is not simply a consequence of economic growth—it is the engine of economic growth. In today’s economy, strong and sustainable growth comes from the middle-class. A stronger middle-class makes for a more productive workforce and a more stable level of the consumer demand.

Stagnant wages and a lack of middle-class wealth also discourage business formation and contributed to a loss of 1 million entrepreneurs from 2002 to 2008, compared to the rate of business-owner households in the 1990s. More equitable economic policies would grow the economy by helping more people fully participate as workers, consumers, and entrepreneurs. That means higher wages, which lawmakers can achieve by raising the minimum wage, expanding overtime pay, strengthening worker voice, preserving social safety programs, and investing in human capital so that American workers can compete for high-paying jobs in a global marketplace.

But national security can also be threatened by a loss of U.S. leadership economically and scientifically, including a failure to make key investments in infrastructure, education, innovation, and scientific research. Leading the world in these fields is the hallmark of U.S. national power. And training the next generation of American leaders will be critical to maintaining American influence and respect abroad. In fact, it was the Council on Foreign Relations that commissioned a report in 2012 which argued that deficiencies in our education system constitute one of the nation's top national security threats. Even military leaders are concerned that underinvestment in today's young people undermines the military force of tomorrow. Indeed, many military and civilian defense leaders are also concerned about inadequate investment in diplomacy, development, and economic statecraft. The United States needs to lead in the civilian and military tools of foreign policy to remain strong, advance our interests and protect our citizens.


To be sure, sustaining economic growth over the long-run also requires addressing long-term fiscal challenges—including an aging population, rising health care costs, and a tax code that collects too little revenue and includes far too many loopholes for the wealthy and well-connected. We must also confront the fact that a struggling middle class has not always reaped the benefits of economic growth. Growing inequality, corporate short-termism, insufficient power of workers, unfair foreign trade practices, and other structural economic challenges threaten our growth and broadly shared prosperity.

In short, we must ensure that the middle class enjoys the benefits of economic growth, women are able to participate equally in the economy, and young people have the opportunities to succeed without having to take on mountains of debt. That is all part of a strategy to ensure American success at home and in the world.

Conclusion

Our country faces significant economic and national security challenges. These are not far-off problems or possibilities. They are happening right now. Middle class families are struggling to get by on stagnant wages. Indeed, these are the most pressing challenges to our economic standing. That economic strength will help ensure America's global standing in the future.

Thank you, and I look forward to answering your questions.

The CHAIRMAN. Thank you very much for your testimony and being here.

I just want to say, this certainly was not a hearing to talk about the necessary solutions. I agree the middle class has had issues. It is more to talk about the strategic problem of having the debt that we have.

So it seems like maybe there is some agreement. It certainly was not an attempt to attack any administration, but just to point out that, as a Nation, having huge amounts of debt does limit our abilities over time and is something that hurts future generations. So maybe your assignment was misunderstood.

But with that, what I would like to do is turn to our ranking member. I would like to interject, as we move along. I know there will be numbers of questions.

And I want to thank everybody for being here and participating.

Senator CARDIN. Thank you, Mr. Chairman. I thank you for this hearing.

And I do understand the purpose of this hearing, that debt has an impact on our national security. As I said in my opening statement, it has an impact on our ability to directly fund national security budgets, whether it is the Department of Defense or the Department of State. It has an impact on America's confidence and reputation globally. And it has an impact on our reliance on other countries to buy our securities. So it clearly is an area of concern.

I am proud to have been part of the Congress and have cast my vote in the Congress of the United States to balance the Federal budget. And we had a balance, and we did it the hard way, the old-fashioned way. We raised taxes and we cut spending. We did both. People said we could not do both. We did both, and we balanced the Federal budget.

And despite the forecast that this would have a negative impact on our economy, because we were cutting spending and we were raising taxes—in other words, taking money out of the economy—it had a major plus to the economy. The economy grew dramatically after we balanced the Federal budget.

So I agree with the chairman that we need to take a look at the size of the deficit.
The point I bring up, though, is that when we went through the recession in 2007 to 2009, Democrats and Republicans came together and said, look, we have to incur debt. We have to put more money in the economy. We have to cut taxes, and we have to spend money in order to get this economy growing. And we recognized at that point that increasing the debt, although it is something we do not like doing, it was necessary in order to get our economy going.

So I just wanted to make the point that debt and deficits in and of itself, you have to be where you are in the economy and where is it the right time to do what we should do.

I happen to believe today we are wealthy enough and strong enough that we should have a balanced budget. We should be able to get to a balanced budget over a reasonable number of years. I believe that. So I agree with the emphasis.

And it is not worth taking the risk of these large debts, so we are strong enough to be able to deal with it, and we should deal with it.

But I do point out the fact that the United States has had one of the strongest recoveries from the deficit. We have had now I think it is 72 consecutive months of 14 million job growth. In 2014 and 2015, we saw over 5 million private sector jobs that grew in our economy.

When you compare that to some of the countries in Europe that went through austerity, and Great Britain is a good example, they went through austerity after they thought they had recovered from the recession only to find that they were back in, basically, a recession.

So the one thing we do not want to do for national security is be in a type of economy where middle-class families cannot do well, and we are, basically, in a recession losing jobs. That is not in our national security interests.

I think that was the only point we were trying to make in regard to the size of the debt.

But we are in agreement. We are in agreement that we should have a game plan today to bring our budget, certainly with less debt, annual deficits, but, clearly, to try to balance the Federal debt.

So I do not know if I have any specific questions, but I will ask both, where do you see a disagreement or do you agree with what I just said, as far as the debt not being a one-dimensional issue as it relates to our national security, that it is a tool has to be used at times, depending on our economic conditions?

Ambassador Haass, do you disagree with that?

Ambassador HAASS. Senator, as is often the case, the devil is probably in the details. I do not think anyone would make the argument or should make the argument that deficits or debt, per se, is bad. It depends upon the scale of it, the absolute scale, the trajectory, what sort of assumptions you plug in about where the economy is going.

I also never heard anyone say we ought to do something dramatic overnight, that we ought to, for example, try to bring down a 75 percent of GDP debt to something like 50 percent or 25 percent. There is no reason to do things dramatic that would destroy economic growth.
I think the real question is less where we are, sir, than our trajectory. What worries me is about the trajectory, and where we are heading.

I simply make two points. Again, it is all assumption-driven, but all things being equal, I think there is a powerful, powerful probability, overwhelming probability, that, all things being equal, the debt problem will get significantly worse with the passage of time. I find that hard to challenge.

And secondly, the good news is, if we were to do some fairly modest things—I understand from Chairman Corker, this is not a conversation about remedies. But the good news is we have not reached a point of crisis, and there are things that we could and should do now that would not be all that dramatic that would put us on a much more sustainable trajectory.

Again, I think it is really important not only that we avoid crisis, but that we give ourselves cushion. Look what happened after 9/11. We had enormous spending needs in national security. And after 2008, we had enormous spending requirements in order to jumpstart the economy.

Part of the lesson of that is we never quite know when we may have to do somewhat similar things again for economic or strategic reasons. So why would we want to allow ourselves to assume a trajectory that would deny us those options if and most likely when we once again have enormous needs that come somewhat out of the blue?

So I think the opportunity for Congress and for whoever is in the White House and the rest is to begin to put this country on a trajectory that is sustainable and is responsible. That is what this is about.

Senator CARDIN. I agree with everything you just said. There are two major factors that we can control, and that is how we spend money and how we raise money. Yes, a lot will depend on deficits and economic circumstances, some of which we control, some of which we do not control. And certainly, the Congress is not in the position of trying to control economic growth, even though we think we can.

So the two areas where we can do our most good is how we spend our money and the amount we spend, and how we collect our revenues.

Although we are not talking about remedies today, if we had a tax code that made some sense, it would be a lot easier for us to be able to match revenues and spending, which has been one of our challenges going forward.

Ms. Tanden, I will give you a chance. You have 1 minute to respond before I lose my time.

Ms. TANDEM. I guess I would broadly agree. I would point out that we can take steps to address the long-term debt challenges that we have. We obviously have to address the deficit as well.

I should note, though, that the deficit has come down dramatically. We have essentially reduced deficit projections by two-thirds. Now, I don’t agree with all of the steps we have taken to do that, but we have reduced those projections. So Congress can act and make an impact.
One particular area that I think is important to note is that we have saved considerable amounts of money from Medicare savings. So, Congress has taken steps—some in very bipartisan ways, some in less bipartisan ways—that have actually had a positive impact on these issues. And I hope that we can have a balanced approach going forward as well.

Senator CARDIN. Thank you.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you.

Senator Johnson?

Senator JOHNSON. Thank you, Mr. Chairman.

When I took over the chairmanship of the Senate Committee on Homeland Security and Governmental Affairs, the first thing I did was we developed a mission statement. It is pretty simple: to enhance the economic and national security of America. I think they are inextricably linked.

The subject of this hearing is the strategic implications of U.S. debt. Ronald Reagan I think taught us that you achieve peace through strength.

Mr. Haass, I just want to talk to you about, as we take a look around the world, every one of these situations has its own root cause. But if we were economically stronger, if we were not on this unsustainable debt path—by the way, we just held a hearing in the Budget Committee. One of the things I have talked about is the 30-year projected debt, according to the CBO, is $103 trillion, $10 trillion the first decade, $20 trillion the second, $65 trillion the third. Net private asset base of America is $116 trillion. I mean, there is the magnitude of the problem.

But would China be pushing the South China Sea, would Russia have been so bold to take over Crimea and push into Eastern Ukraine, would Iran be rattling its saber as much as it is, if America were stronger?

Ambassador HAASS. Senator, it seems to me that strength is always a reflection of two things. One is existing capacity and the other is the political consensus and will to make use of it.

I think that the perception around the world is less one of a question about American capacity and more to what extent we are willing and able to use the capacity we have. And that is the conclusion that I draw from conversations with people around the world.

Some of it stems from what the United States has chosen to do and more important not to do in the Middle East. Some of it also stems, quite honestly, from elements of what is seen as American political dysfunction. High on my list is, for example, the inability to get a consensus to deal with things like TPP, which if not passed is ultimately as strategically damaging in Asia as what we did not do in Syria was strategically damaging for the United States in the Middle East.

Predictability and reliability are the currency of the realm, if you are going to be a great power. And I think there are real questions now about the United States.

My hunch is China is doing what it is doing in the South China Sea largely as a function of Chinese strategic assertiveness. There is an interesting debate going on amongst the people I hang out
with. It is how much the Chinese are turning to foreign policy and, to some extent, satisfying nationalism, because it can no longer be satisfied with high rates of economic growth. There is a big debate going on about that.

But my general sense is the debt problem is not linked. I do not think you can link it to the challenges that we are facing in the world now. What worries me, again, is trajectory and future, that it will raise questions about capacity, reliability, and will.

So it seems to me it is part of a package of looming questions over America’s ability to lead and act in the world.

Senator JOHNSON. Again, you talked about willingness and capacity, and they are two different sides of a similar equation, though.

Isn’t it true that our adversaries—let’s hope they do not become our full-blown enemies—sense a growing weakness? And doesn’t that embolden them?

Ambassador HAASS. Absolutely. Again, people are constantly taking our measure, and they are taking our measure about what it is we are able to do, what it is we are prepared to do. This is everything from international things we do in the world to things we do at home. And I think that what you always want to do with countries that are either existing or potential adversaries is you want to let them know if they act in certain assertive or aggressive ways, they are going to be frustrated, shall we say.

On the other hand, they do have other options. What you want to do is steer, say whether it is a country like China or Russia, toward a constructive pattern or behavior, rather than overthrowing or overturning the applecart. They would say that would be a mistake, and instead, they are going to, at least in limited ways, cooperate.

What that suggests to me is you need a combination of strength to push back, basically a hedging strategy. On the other hand, you want to have diplomatic openings available that are reasonable. You need the combination in how you approach any country.

Senator JOHNSON. But it is definitely true not only is our willingness reduced, but our capacity, our capability, has been reduced, correct? We used to have almost an 800-ship Navy. Now we are under 300. And our adversaries, our potential enemies, know that.

Ambassador HAASS. There is no substitute for local military capability. If we are talking about a rebalancing towards the Asia-Pacific, we need to have the air forces and naval forces on the scene.

You never want to put the Commander in Chief in a position that something happens and your only response is either delay or escalation. You do want to have local responses available. It is the best way both to deter, but also to respond in a way that does not need to be something much bigger than you would really would like to see.

Senator JOHNSON. I think your third point was leave the United States more vulnerable to the machinations of government. Go through a scenario of what your concern would be. Let’s say China decided to take $1.2, $1.3 trillion worth of its debt and start selling it.

Can you kind of go through that scenario for me?
Ambassador Haass. That is basically it. Where you have a situation where—we will use China as the example—there is confrontation between the United States and China over the South China Sea, over Taiwan, something between Japan and China, we have alliance relationships that would likely bring us in. I would never want to see the Chinese think one of the ways they could leverage us and get us to think twice about taking certain actions potentially on behalf of allies, thinking about the economic pressure they could put on this. It would not take necessarily that much, in terms of an announcement they were not going to continue to acquire debt or an announcement that they were maybe going to sell some.

I understand there are people on the other side of this debate who would say they would never do that. It would mean they were shooting themselves in the foot twice over because they are large owners of American dollars and they would not want to see their holdings devalued. They obviously have a stake in their continued ability to export to us. But we should not kid ourselves.

If the Chinese saw a vital national interest like Taiwan at stake or something with Japan in the South China Sea, they may very well calculate it is better to take a short-term economic hit and protect its nationalist interests, as they see it, than think about their own long-term economic health.

Senator Johnson. And the harm that would cause America, if somebody starts flooding the market with bonds, that is potentially going to drive up the cost of interest, which again starts taking away resources for other things in America.

Ambassador Haass. It is not just a matter of a crisis where you have geopolitical overtones. I do not want, if you will, the world to wake up where markets basically decide the United States is on an unsustainable trajectory, and then people start demanding higher returns in order to continue to lend us money.

I used the phrase before, that is a vicious cycle, not a virtuous one, because it gets more expensive for us to borrow. That, in turn, slows down the economy. And that is exactly the path we do not want to get on.

Again, the good news is we can avoid putting ourselves in that position, but we have to take action. It is not going to sort itself out by itself.

Senator Johnson. Thank you. Thank you, Mr. Chairman.

The Chairman. Senator Murphy?

Senator Murphy. Thank you very much, Mr. Chairman and Ranking Member.

Welcome to our guests. Count me amongst those who think that this is a very important hearing to have. Count me amongst those who are worried about the trendlines of American borrowing and debt.

Certainly, as the father of a 7-year-old and a 4-year-old, I think every day about the burdens that we are leaving to the next generation, if we do not make smart decisions about both spending and revenue.

But I also feel as if we have been having this discussion over the course of 30 years, that we have been told about the apocalyptic global implications of American debt for a very long time, and I
think you can make a fairly serious argument that we have yet to see those predictions come true.

I wanted to just posit an alternative scenario to both of you, as to how to read the last 5 to 8 years of American economic and political experience. It certainly has been a time of rising debt. Well, deficits have been declining. Debt, certainly, has been expanding. So there is no way around that.

But there is also the story of truly exceptional economic and political flexibility that is exceptional relative to the way the rest of the world has dealt with the economic fallout of the Great Recession. It was this country alone amongst equals that was able to engage in pretty classic countercyclical economics, driving deficits up to 10 percent of GDP and then, through a combination of spending discipline and tax increases, driving them down to 3 percent of GDP.

It was this political infrastructure, as dysfunctional as it is, that was responsible for saving two major industries, the auto industry and the financial industry.

You can tell a story of the risk presented to the American model, I think as Mr. Haass put it, the risk that we detract from the appeal of the American political and economic model, purely through the prism of debt. But I would argue that as much as we still have to pay attention to that underlying liability, that the story of our economic recovery and of our relative political flexibility to deal with major challenges, frankly, over the course of the past 10 years, has been a pretty good advertisement for the American model, warts and all.

That is my theory. Let me ask you, Ms. Tanden, and you, Mr. Haass, to reflect on what the global community, in particular market makers around the world, have taken from the story of America’s economic recovery, and whether or not that does provide a pretty substantial counterbalance to risks that come from increased debt, in terms of the attractiveness of the American economic model. I am not talking about some of these other questions about what the logistical concerns are regarding other countries holding our debt.

In terms of the attractiveness of the American political model, isn’t there another story here?

Ms. TANDEN. I would agree. I would say that, first and foremost, there is a way for markets, not governments, but markets, to assess the risk of our national debt. It is long-term interest rates, so we have that sense, day-to-day.

And I want to note, once again, that long-term interest rates are currently at very low levels, both in the U.S. and around the world. But, to speak to your broader point, I think the reality is that if you look at the United States vis-a-vis our competitors and allies, where there is often a lot of overlap, the United States has been more flexible.

That is one of the reasons why—unlike some of our allies—we are currently attracting investment. We have ways to determine how the global economy is looking at the United States. And the levels of investment in our country compared to other economies is one of them. That is a positive story.
Europe has taken steps toward austerity. Their growth rate is lower. But beyond Europe, we are also seeing issues in the developing world.

China's position this year, and the steps it took vis-a-vis its stock market, has created a real lack of confidence in the world. Whereas, the United States has a free and open market.

I think it’s hard to argue that our political institutions function very well all the time. But if you look at our position on the global scale—if you zoom out and look at it from a 60,000-foot perspective—the United States has taken stronger steps that have created more support for growth than many other countries over the last several years.

Ambassador HAASS. Senator, I actually think many aspects of the U.S. response to 2008 was both, in absolute and relative terms, admirable. Some of the individuals involved did fairly heroic things, from Secretary Paulson to Ben Bernanke, Tim Geithner and others.

The debt, though, is a different issue. The debt is a long-term issue, and there are two things that really concern me.

One is demographics. Demographics are supertankers. You can see where they are heading, and we are heading to a society where the ratio of elderly and retired, vis-a-vis those who are working age, is going to move in a direction that we do not necessarily want to see. In self-interest, I am happy about it because, hopefully, I will be one of those elderly people. But the future is one of working people who are going to have to support a large number of retirees.

And the big driver of debt is going to be entitlements. You look at Medicare even with slowing down of the curve or bending of the curve on cost increases, the day is going to come where Medicare is going to drive out a lot of other spending. Social Security will contribute to it.

And secondly, rates. We are not talking about where rates are now or in 3 years or 5 years. But just by historic terms, rates are much closer to lows than they are to highs. It would not take a big upward movement in rates to have a tremendous impact on the burden of debt financing.

So again, it may be that people like me are wrong and that we are exaggerating the potential risk. It is a little bit like fire insurance or preventive medicine. My instincts are, let’s think about what would be a sensible premium. On the off chance I am right, and when we think about the obligation to the future, I think it would be criminal as a society—or negligent, I will use a better word—for us not to do certain sorts of things to put us on a safer trajectory.

If it turns out the debt problem is not as bad as people like me think, we will not have paid a great deal. We will not have bankrupted ourselves. We will not have killed off American economic growth. But on the chance that people like me are closer to being right than wrong, then I think it would be seen as an extraordinarily wise investment to do something about it.

Senator MURPHY. Mr. Chairman, I would just recommend to everyone a simple table that talks about the average age of the United States and all of our competitor countries relative to today and 2030, because demographics is certainly something we should
be concerned with, but is actually another success story of the American political and economic model. Between now and 2030, we age by 2 years, and we actually go from being 4 years older on average than China to 4 years younger than China. Our European competitors are going to be in average ages of the high 40s and 50s.

So I agree that Medicare is an enormous liability, but our history of immigration policy is also part of something that should make us feel pretty good about our model.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you.

I have my first interjection. These hearings sometimes surprise you. I thought that likely there would be an agreement that, strategically, for our Nation, having large amounts of debt over time is a problem. I am hearing that as long as you can outrun the slowest runner when a bear is chasing you, you are in great shape.

This hearing is of great surprise to me. Certainly, how you solve the problem, there could be some disagreement. But the fact that we have people sitting on each side of the dais, some of whom perceive that ad infinitum debt with the demographic changes that are taking place is not a strategic foreign policy issue, not a strategic national security issue, is stunning to me.

So this is quite an awakening moment to me. It is somewhat depressing, but quite awakening.

Senator Perdue?

Senator MURPHY. To be fair, Mr. Chairman, I am not sure that I would paraphrase my remarks in the same way that you did.

The CHAIRMAN. I am paraphrasing a number of comments, including a witness.

But again, I would think that most Americans would agree that having the amount of indebtedness we have with the trajectory we are on is a problem for our Nation, not just from the standpoint of the middle class and economic growth and the lack of productivity that comes with lots of debt over time. We might disagree with how to solve that. I would expect that, of course. That is the debate that we have not had that our Nation should have, and the purpose of this hearing is to bring awareness to the fact that it is a national security issue, too. It is not just an issue relative to our balance sheet and deficits.

But generally speaking, I do hear a lack of concern about that, which is somewhat surprising.

Senator Perdue?

Senator PERDUE. Well, thank you for this hearing.

As was mentioned earlier, we had a budget meeting this morning. The head of the GAO came in and talked about the budget, the process. And we will see another estimate coming from them tomorrow on certain aspects of our Federal spending.

But I want to put this in perspective. I think the country faces two very serious crises right now, and they are interrelated. One is we have a global security crisis, and I see it on several fronts, five major levels that we are facing as a country.

One is we have the rise of traditional powers, Russia and China.
Second, we have the terrorist rise. ISIS right now has relationships around the globe, and they have a reach around the globe that we just have not seen in modern history.

The third is this threat of nuclear proliferation among rogue nations. With the collaboration between North Korea and Iran right now, the JCPOA notwithstanding, they both are moving in that direction.

The fourth is cyber. What we see going on in cyber warfare right now, with what Russia is doing in Eastern Europe, is profound. What we see on our own shores with cyber warfare is not to be ignored.

And then last, the thing that we do not really talk about, is the arms race in space.

So all these things create a pressure on our ability to deal with the global security crisis.

I just got back from a week in the Middle East, and I can tell you, things are not getting better there. They are getting much worse on a humanitarian level as well as a security level. Development is taking a backseat.

You talk about the middle class. The middle class is evaporating in the Middle East. It is not just declining. It is evaporating. Eleven million people in Syria are on the road going somewhere.

So we have a huge problem there. The very time that we face this increasing threat to our country and the free world, by the way, we are spending less on the military than we have in 50 years as a percentage of GDP, 3.1 percent. If that were to compare to just the 30-year average, adjusted taking the surge out, that is about 100 basis points less than the 30-year average, which is about $200 billion today.

Now, I am not espousing that we are spending $200 billion less. I would like to see some efficiency made in the military, but I think it is really important to note that we are sitting on the smallest Army since World War II, the smallest Navy since World War I, and the oldest and smallest Air Force ever. I just do not understand it.

Even Secretary Gates, in his last budget, for fiscal year 2016, he proposed a budget that is some $66 billion greater than what we are spending right now. Now, those are real numbers.

I have just seen, personally, how it affects our ability to affect the mission we have. Let me just give you an example very quickly.

In Moron, Spain, we stood up 1.5 years ago, a Marine contingent to defend our Embassies in Africa. That is their only mission in life. They have 12 Osprey, V–22 airplanes. They are self-contained. They are mobile. They can get there in a matter of hours. The problem is that by having 12 planes over there and the delay in buying future V–22s, we now have to move six planes back. That cuts their ability in half. That means they can only defend one Embassy at a time in Africa.

What that means is, if someone has a minor incident and they mobilize and go down to them, effectively what we need to do in most other Embassies is evacuate, because we do not have the ability to back up our defense. We can talk about JSTARS. We can talk about the human capital issue.
But I think the bottom line is that we have increased threats. We have a question about if we are spending on the right priorities to defend our country and really to protect alliances around the world.

At the same time then, as you have a global security crisis, you have a debt crisis. I am sorry. I am just a business guy, but here the realities. I mean, I do not understand why this is even a debate, honest to God, I do not. I mean, $19 trillion in debt, we talk about 75 percent of GDP. I feel like the Federal Government owes Social Security and they owe the trust fund for Medicare those dollars. Those are not to be ignored.

So I talk about it being over 100 percent of GDP today and over $100 trillion in future unfunded liabilities that nobody wants to talk about.

The interest rate today is so arbitrary. In 7 years, we have not adjusted interest rates. We had one in December, the first time the Fed has adjusted interest rates in 7 years, unprecedented.

And that quarter-point increase in the interest rate effectively means $50 billion each year of new interest—$50 billion. Imagine what that would do to AIDS. Imagine what that would do to Alzheimer’s or cancer research, or to help build the middle class with economic development.

Ms. Tanden, I agree 100 percent. Our goal right now is to build the middle class. It is under great jeopardy. It is in great jeopardy. Our economy is suffering through the worst recovery in 70 years. I understand the number of months of positive GDP growth, et cetera, et cetera. But there is no denying this economy is sitting down. $4.5 trillion the Fed has put into the economy is not working. Why? Because of our fiscal policies from this place here in Washington.

I am a business guy. I can go on all day about why this economy is not growing, but I want to get to the question, very quickly.

In the last 7 years, Dr. Haass, we borrowed 35 percent of what we spent as the Federal Government. We spent $25 trillion running the government. We borrowed $9 trillion. In the next 10 years, the CBO says we are going to add another $9 trillion in debt, which is about 25 percent of what we will spend.

So the bottom line, it says that mandatory spending is 70 percent of our budget. That means that every dollar we spend on discretionary spending, that is military and nonmilitary discretionary, in my definition is borrowed, because the first dollars that come in go to mandatory.

We cannot sustain that. There is no way this is sustainable.

You have the best characterization that I have heard it, and I want you to expound on it. It is a slow-motion crisis. I have never heard anybody else talk about that. But you said the bad news is that slow-motion crises generate little or no sense of priority, but rather tend to promote complacency. Combine that with political gridlock here in Washington, and you can see why the approval rating of this body is 7 percent. You can see why Bernie Sanders and Donald Trump are doing what they are doing in the presidential race.

So my question is, as an outside adviser, how do we break through to create the sense of urgency? And are we charting the
right course, relative to debt being a threat to national security, from foreign policy?

This is a bipartisan committee. I think we find common ground, that, economically, we are going to help the middle class. But I think the realization that we have to come to is that this is not just a crisis for our kids and grandkids. I am telling you right now, it is here right now.

So I am asking you, as an adviser who has a picture of this thing, if interest rates were to go up to their 50-year average of 5 percent, we would be paying $1 trillion in interest. There is physically no way on a $4 trillion budget to do that. So please help us with some advice about how to break through here.

Ambassador Haass. I feel like the kid in class who just got asked the toughest question. I will pick up on one thing that you said, and then I will do my best to answer it.

I think it is important, and it gets back to some of the previous exchanges, we are not just like everybody else. We have responsibilities in the world. To say that we have come out of the recession slightly better than others, or our demographic picture is not as bad as others, that does not give me a lot of comfort.

We have a role in the world, which is qualitatively different. There is no other country that plays such a role in the world to promote global order, and there is no alternative to us. This is not bragging. This is not saying we can do it alone. But we do have a unique role.

So we have to have capacities that others do not have to have. The dollar plays a role that no other currency plays. The U.S. is a model that no other country is.

So I think the United States is to some extent sui generis. It is one of the reasons the debt problem and the trajectory worries me so much.

I do not think it is fair or smart to say we are better off than others. The question is where we are and are we heading where we need to be.

Senator Perdue. I am sorry to interrupt. We are also subsidizing our allies who are spending, on average, much less than 2 percent of their GDP as well.

Ambassador Haass. That is true. But when it comes to our allies, we have to remind ourselves that one of the reasons we support our allies is not as a favor to them. It is a favor to ourselves. I believe we have gotten extraordinary return on our investment in Europe and Asia.

Senator Perdue. I agree.

Ambassador Haass. When I look at the history of the last 75 years, essentially, it is remarkable history from the vantage point of American national security, both in what has happened and what has not happened. One of the reasons is that we have been so supportive of our allies.

To answer your question, though, about how we change the conversation, I actually think it is part of a larger conversation, sir. I think it is part of a conversation where we take some of these issues like debt, and we connect it to national security, which is the logic of this hearing today. It involves a larger, pardon the expression, public education role about why the world matters, how it af-
ffects us, and the future of this country, what happens, if you will, to the 320 million Americans, how it is not something that we alone are going to determine.

We are going to be dramatically and directly affected by what happens amongst the other 95 percent of the people in the world, what happens in questions of regional stability, the ability of the globe to deal with some of the challenges you mention, from cyber to proliferation.

So I think the way to have an informed public debate on the consequences of our debt and its trajectory for national security is really to embed it in a larger debate about the consequences of what happens in the world for the welfare, the prosperity, and the security of the United States.

What worries me is Americans often just do not see the connections between what goes on out there and what goes on and will go on here. I think it is actually a public education challenge for people in your position and for people in mine and others.

Senator PERDUE. Thank you.

Ms. TANDEN. May I respond, just briefly?

Senator PERDUE. Please.

Ms. TANDEN. I just want to make the broader connection between the decisions Congress makes or can make, and the issue of economic growth.

So just as an example: large-scale investments in infrastructure generally—as you see in other countries—improve productivity of the economy and help foster economic growth. While I absolutely agree that we do have to address the long-term debt in the United States, we should do that in a reasonable way, and I would agree with Ambassador Haass that there are ways to do that.

But we also have to think about how the decisions Congress is making today are affecting economic growth and productivity. For example, on issues like the investments we can make in infrastructure, where there has been continued bipartisan support, investment actually improves productivity and over the long run helps address the long-run challenges around deficits and debt.

The stronger the economy is, the faster it is, the more heat there is to the economy, and that affects our debt numbers as well. So, I would just point out that there are decisions we all make today that can have that kind of impact.

Senator PERDUE. May I just quickly?

The CHAIRMAN. Sure.

Senator PERDUE. I could not agree more. We have been looking for common ground, and here it is. There is an interconnectivity between growing the economy and the debt. You are not going to solve the debt crisis over the next 30 years just by growing economy, but you are not going to do it without doing it as well.

You have to deal with Social Security and Medicare, which is 800-pound gorilla in the room, which also affects the economy itself. The drain on resources to support that takes away from investments in infrastructure. We see it right now in this very budget that we are dealing with today.

So I see this as a very major part of a long-term plan.

You said it best, Dr. Haass. This is not something that is going to be solved in next year's budget. We got here over 70 years. It
is going to—actually, in the last 15 years is when we created it. In the year 2000, we had $6 trillion of debt. Under the Bush administration, we added $4 trillion. It went to $10 trillion. Now we are up to $19 trillion.

There are no innocent parties up here. We are all guilty of this. Someone said in testimony that we have seen the enemy and it is you guys, talking about us. And it is right.

So the way out of here, I believe, is to save Social Security and Medicare, get the economy growing, solve this budget process, fix that, and get at the underlying cost of health care, which is driving the Medicare costs so dramatically. So I think there is common ground here.

In this committee, what I am worried about is the interconnectivity with this national security issue that we have as a Nation and to fulfill our mission around the world to protect our national interests, but also our security here at home.

Thank you both.

The CHAIRMAN. Before moving to Senator Flake, I will make another interjection.

I could not agree more on the infrastructure issue. And, unfortunately, what both sides of the aisle have been willing to do is to build infrastructure, but not pay for it. So we create these gimmicks. This last go-round was pretty remarkable in its gimmickry.

I would just say, again, if it is important to have infrastructure, and as I believe it is, and if it is one of those things that actually drives the economy, would it not make sense that we actually paid for it? It is that fecklessness, that unwillingness to face up to the importance of things like that and pay for it that is, to me, creating this significant, down-the-road crisis that is happening over time for national security issues.

Ms. TANDEN. I just want to point to another area of comity where we very much agree that we should pay for infrastructure.

The CHAIRMAN. And, of course, I am sorry, here in Congress, we run from those issues. And we are creating, unfortunately, I believe, a crisis down the road.

Ambassador HAASS. One thing about infrastructure really quickly, because one of the things I really like about this hearing is it takes an economic issue and blends it with national security.

Infrastructure is the same thing. Beyond what it may do for jobs, it does two other things. It enhances American competitiveness, which is a national security issue. It also makes us much more resilient. It does not matter whether it is a manmade terrorist-type thing, or it is a storm, infrastructure enhances American resilience.

It is a national security issue. And I think when Congress looks at it, it needs to look at it I think as much through that prism as it does through any budgetary prism.

The CHAIRMAN. Again, just to add to it, we decided to drain our Strategic Petroleum Reserve, which is here for our national security, and to make up a number, that we were going to sell this oil for $89 a barrel down the road. We just made it up.

Again, it is just us creating this slow-motion crisis that is occurring.

Senator Flake?
Senator Flake. Thank you, and thanks for calling this hearing. I appreciate the testimony.

Ambassador Haass, you articulated my greatest fear that I often express when people ask what my concern is about the future. It is that we will wake up some morning and the financial markets will have already decided that they are not going to buy our debt, or we will have to do it a premium. And interest rates will go up, and then we are in a vicious circle, and we are Japan for decades or generations, just lost economic growth, and it is just impossible, given the austerity measures we would have to implement and what we would have to do, to have the economic growth that we need.

But let me just turn to one aspect of the inability to have the resources with regard to soft power. We generically call it foreign aid. It is one of the least popular things to defend here.

But if you can talk a little bit about that, not just funding our national security commitments abroad, but ensuring that we are in a position to defend those interests abroad.

Say, in Africa, much of our ability to go in and help countries combat Boko Haram or al-Shabaab is because of our willingness in prior years to help them with the AIDS crisis through PEPFAR, or to help with other initiatives.

Can you talk a little about that, how important that is, our engagements around the world, not just in national security but prior to that?

Ambassador Haass. Thank you, sir.

The first thing to say about foreign assistance is you would think we were spending a lot more on it than we are. The controversy or the reputation that it has is at variance with the facts, as you know, and as everyone sitting up there knows. We spend quite modest amounts on it.

I also think it is useful to differentiate among various types of humanitarian aid. I think it is one of the things that again, as an American citizen, I feel best about.

It is interesting that you mentioned PEPFAR. What an extraordinary initiative that was. It is good, old-fashioned humanitarian aid. It has kept a lot of people alive who would not otherwise not be alive. That is just the sort of thing we should be doing as a government. We also do more of it as a society than any other country in the world. That is something Americans can be proud of.

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I differentiate that from developmental kind of aid. It is a little bit more complicated, but I think the Millennium Challenge effort was a really important and useful intellectual and political innovation, because it became much more conditional in linking assistance for countries that were, as you know, adopting certain types of governance reforms, which, again, I thought was good, all of which is different from security aid, whether it is in the economic form, ESF, or military aid.

But we need to do all of it. I actually thought, when I was in government, one of the most valuable and cheapest forms of security aid were things like IMET, the military training and educational assistance. For very small amounts of money in absolute and relative terms, we could bring people in midcareer levels over to the United States staff schools. They would get exposed to American
theories of civil-military relations, to professionalism. They would go back and in many cases rise through the military ranks or through the political ranks, they would have significant influence within their own societies.

It was a tremendous investment in promoting rule of law and respect for civil-military relations.

So I actually think, all things being equal, that foreign assistance, writ large, turns out to be a pretty good return on investment for the United States.

And it comes back to what we are talking about here, it is one of the things you do not want to see crowded out. It is too easy for a lot of things to get crowded out, because by the time you are paying interest on the debt, and you are dealing with entitlements, national security and discretionary domestic spending, they are the collateral damage, if you will, of where we are heading on debt, and we have to figure out ways to protect them.

The only way I know how to protect them is some combination of dealing with the drivers of debt and adopting policies that accelerate economic growth.

Senator Flake. I appreciate that. It is often humorous to hear this discussion about building a wall on the Mexican border and having the Mexicans pay for it. Some are saying let’s just cut off foreign aid, if they will not. That was talked about, foreign aid to Mexico. There really is none, other than some cooperation on drug initiatives and things like that.

So it is often misunderstood and is often assumed that is a lot larger than it really is.

But I appreciate the comments in this hearing. I do have a huge concern. This is bigger than any concern out there, in terms of terrorism or nuclear proliferation, because if we do not deal with this, we will not be able to respond to any of those threats. So it is the root of all of it.

I do worry that we are really on borrowed time here. The point at which other countries will have hit that point where the financial markets decide, we have passed that. We are just the best house in a bad neighborhood.

And I do not know how much longer we can go. But what I do know is that, once we wake up that morning when the markets have already decided, it is too late then without a good deal of pain and suffering for a number of years. So I hope we reach the realization before it to deal with this.

And everyone knows what it is going to look like, at least the broad parameters. We have to bring in more revenue, not necessarily by raising rates, but by closing loopholes on the tax code. We have to do some kind of chained CPI on Social Security, or limit the growth thereof. Medicare, it is going to be some big reforms and means testing.

I mean, any real solution is going to have those broad contours, at least. I just wish we would get to it sooner rather than later.

Thank you, Mr. Chairman.

The Chairman. Yes, if I could, just again, since I did not use my time on the front, most entities in the world try to protect themselves from the market fluctuations that occur. What I hear so many people in this hearing saying is, well, the market has been
good to us, so what do we have to worry about? The fact is that a great nation or a great company or a great entity is constantly thinking about those things that could occur and trying to ensure that they have done everything they can to protect themselves from it. On the other hand, what we are doing is just rolling along and saying these guys have been good to us and we are faster than the slowest other country in the world, so we are going to be okay.

I just never expected that to come out of this hearing today.

Senator Rubio?

Senator Rubio. Thank you. First, I am glad you are holding this hearing. It is a very interesting issue that I think brings into focus the broader narrative that Mr. Haass spoke about.

One of the things that is happening in this country that has led to some of this turmoil and vibrant debate in this political cycle has been that the world has changed dramatically. We used to be a national economy and to some extent still are. But we are deeply impacted more than ever before by global currents, global markets, what is happening halfway around the world.

Foreign policy is economic policy more today than it has ever been. I think someone used the statistic 5 percent of the world. We are 5 percent of the world population, 40 percent of its economy, but 5 percent of the world population.

And the good news is that there are millions of people around the world that were once starving who now buy things, and they want to buy things from us and trade with us and travel. This is an extraordinary development. It is positive, but it has implications.

And it is one of the things that has been so disruptive in the political debate, that we no longer fully control everything that happens in our economy, because so much of it is tied to something that happened in some remote place halfway around the world, and the debt is a part of that there.

The second is this issue of debt. Look, if we were any other country looking at these numbers, we would be in a debt crisis. The reason why we are not is because the world still has confidence in America, because they believe Winston Churchill's statement that Americans always get it right after they have tried everything else first. And they believe we will ultimately get this right, and we will always pay our bills, and we will get this straightened out.

So the stability of our political process, and its ability to solve problems, has implications on this as well.

And I agree with you, Mr. Chairman. I do not know how this could be a question that the debt is not an issue, because if you think about what happened to Greece, if that were the United States, or what is happening in Puerto Rico as a territory happened in the broader country, the world would freak out. I do not know if this is scientific term for that, but I can just tell you the world would flip out. If the U.S., the most important and indispensable nation, were to have a debt crisis that would call into question its ability to pay its bills, it would have dramatic global implications. So this is a major issue.

I would also say that you do not run up an $18 trillion debt with one party. This is a bipartisan debt. People say there is no bipartisanship in Washington? There most certainly is. There is an $18
trillion debt to prove it. Both parties have had control at different
times, and they have written checks that they could not cash, and
we are facing the consequences of that.

But part of this debate has led us to this point, and I think Sen-
ator Flake alluded to it when he talked about foreign aid, this con-
cept somehow that if only we did less around the world, we could
take care of this issue. Foreign aid is the one I always hear about.

When I explain to the people, I think it is 1 percent of our budg-
et, maybe? It may be even less. People always use foreign aid. “If
you just cut foreign aid, we can pay for” and you fill in the blank.
It just does not add up.

But we never talk about the costs of not engaging in the world
beyond foreign aid. So now you basically have someone—I do not
want get into all that.

Let me just say you, have a major voice in American politics
today saying we can save a bunch of money, let’s just get out of
NATO. We can save a bunch of money, let’s just get out of our rela-
tionship with Japan and South Korea, and put them in charge of
their own security.

I guess what I would ask both of you to comment on is, what
would the world look like for America—let me just back up to one
more point. I do not mean to take up all this time, because I want
you to be able to answer this.

But part of this economic growth that we benefited from would
never have happened had the U.S. not helped Europe in the after-
math of the Second World War. It would never have happened had
there not been a NATO.

It would never have happened had there not been a U.S. sup-
porting South Korea for all those years where South Korea’s econ-
omy at one point, and I believe as late as the 1970s, was smaller
than the North Korean economy. Today, they are the ninth largest
economy in the world, I believe, and they are a contributor to for-
ign aid. They are a donor, not a recipient.

Japan is another successful story, a nation we went to war with
and then helped rebuild, and today is one of our strongest alliances
in the world.

So my question is, what would the world look like now, what op-
portunities would we not have, because none of this growth that we
have had up to now would have been possible without those rela-
tionships and without that stability? What would the world look
like economically and ultimately for our ability to pay our debts
long term, if America were to walk away from its security agree-
ments with Japan, with South Korea, and with NATO? Each of
these are separate.

Let me close with this, just to be clear that I am on the record.
I think South Korea this year will contribute $800 million in de-
fense. The Japanese have stepped up in what they are doing in col-
clective self-defense capabilities. And of course, NATO needs to be
repurposed and modernized to face new threats, but the truth is,
they are an indispensable part of the U.S. role around the world.

So what are the economic costs and ultimately the impact on our
ability to pay off the debt if the United States alliance with NATO,
South Korea, and Japan is called into question?
Ambassador HASS. Let me just say I would predict that any near-term savings would be overwhelmed by medium-term and long-term costs. It would be penny-wise and pound-foolish.

One is, your basic premise, Senator, is right, which is there has been an enormous economic dividend of global stability. If one looks at the last 75 years, the relative absence of great power conflict compared to the previous century has been a tremendous advantage for ourselves and others. The fact that you did not have proliferation by Japan, which would have changed the entire dynamic of Japanese-Chinese relations; the fact that the Cold War ended peacefully and ended in the way it did, with NATO and the West winning and the Warsaw Pact and the Soviet Union essentially losing; that all created the conditions for the extraordinary economic success of these decades.

I understand that economics feeds into security, but security is even more of a prerequisite, I would argue, for economic success. So calculations of our, quote, unquote, "savings," even if the host nation support and offsets you mentioned did not exist, I think are way too pinched. It ignores the larger historical truth and the dynamics that, if we were to do less, others will do more. And that would probably be more than the circuits diplomatically could handle.

I do not want to see Europe get interesting again. I do not want to see the Asia-Pacific get real interesting. The part of the world that is all too interesting is the Middle East.

That is the part of the world where the United States is now doing appreciably less than it has done in recent history. That ought to be something of a strategic warning to us. When we are not prepared to play a significant role, the vacuum tends to get filled by others who are going to have agendas that may be very, very different from our own.

So yes, it costs us 3 percent, 3.5 percent of GDP to do what we do in the name of national security, defense, plus intelligence and so forth. It is a bargain. It is a bargain, given the strategic and economic benefits.

I think we have to understand it, and we have to explain it.

Ms. TANDEN. I would just add to that. I completely agree with Ambassador Haass. I would just add, perhaps to make it a tad more pointed, that withdrawing from NATO, creating deep military insecurity in the Asia-Pacific region, could have devastating economic impacts at any given point. The reality is that the United States deeply benefits from stability in Europe and in Asia, as does the global economy.

Asia is a growing source of economic growth. The United States is still the strongest area of growth. These are areas in which having that security blanket keeps real disruption at bay. And the idea that we would withdraw, particularly from the Asia-Pacific region at a time where China is taking actions that are hard to explain, seems to me would create deep economic challenges over the next several decades.

So, I would say, again, I think there is broader agreement on addressing the national debt, but that kind of withdrawal would lead to fundamental problems for any aspect of the U.S. economy that relates to trade and globalization.
Senator Rubio. My point in asking that question is that I want to be clear that doing all these things that I just mentioned will do nothing to deal with the debt, but would, in fact, trigger a worsening debt, in my opinion, because of the additional costs that would be imposed on our economies. Thank you.

The Chairman. It seems like you felt the need to express yourself based on comments you have heard over the course of the last several months.

Senator Rubio. Not only that, but also just kind of seeing the world’s reaction to this stuff. I mean, they are asking us, is this really going to happen? It is having an impact on people’s psyche. They are wondering where America is headed, and they just want some reassurance that this is not going to happen.

The Chairman. Thank you. Thank you so much.

Ms. Tanden. I am glad you can provide that assurance.

The Chairman. Senator Markey?

Senator Markey. Thank you, Mr. Chairman.

And thank both of you for being here today.

The way President Obama has viewed his term of office is that he has tried to look at areas where there could be a pruning in the Federal budget, but at the same time, there has to be an investment strategy in health care, in education, in infrastructure, in the future.

That is pretty clearly the only way in which we can compete in the long run with our economic rivals around the world. They each have a business plan. China has a business plan. Japan has a business plan. So we need to be able to say we have a business plan as well in our country.

So if we are not investing in the clean energy sector, if we are not investing in NIH, if we are not investing in cyber technology, if we are not investing in all of the areas that have been identified as growth areas, and if we are not educating our population, especially since 15 percent of it is going to be minority, and we pull back from those sectors, well, we are playing right into the hands of our enemies or our rivals, our adversaries, economically. It is just as simple as that.

So while I hear, philosophically, that people want the defense budget to be untouched, but, at the same time, the Federal deficit has to be reduced dramatically, well, there is another word for that. That is the future that you are talking about. That is how we project our power. It is through this incredible economic resource that we represent to the rest of the world.

Now, I would just like to move for second, if I could, over to the defense budget. There is a proposal to have $1 trillion of new nuclear weapons systems in our country over the next 20 years. That is a crazy number, from my perspective. We already have more than enough in order to accomplish those goals.

So I would ask if either of you, since that is kind of the context of this discussion, we are in the Foreign Relations Committee, the projection of power by nuclear weapons capacity has clearly now injected itself into the presidential campaign.

And I guess my question is, is that a good expenditure for the United States, Ms. Tanden, for us to put another $1 trillion into nuclear weapons? Are we really going to buy ourselves $1 trillion
worth of additional security in our country? Or is it just going to be added on to the already unnecessary expenditures in that nuclear area, when we should be trying to reduce the number of nuclear weapons that the U.S., Russia, China, and others have?

Ms. TANDEN. We definitely believe that we can maintain our military strength with a reduced stockpile, so that is not an area in which we think we need major expansions.

But I do want to touch on your broader point. I hope that there is also broader agreement on this topic.

I think it makes sense to think of the decisions we make from a competitiveness standpoint. And from that standpoint, in my opinion, investments in infrastructure, investments in research—at NIH research and in other areas, have led to economic competitiveness—from the growth of the pharmaceutical industry to other areas where we have made technological advancements. The broad point I would make in this hearing is that we should undoubtedly address deficits and the long-term debt as a challenge for this country.

And we believe we can take balanced steps to do this. I agree with Senator Flake that it does mean additional revenue as well as additional savings, in particular areas.

But the challenge around the debate about debt, over the last several years, is it has often meant that we do not make those investments necessary to keep our country competitive.

And I completely take your point that that is, in my view, exactly the wrongheaded approach, that we should not forsake investments that lead to competitiveness for the U.S. economy over the long term because of our concerns about the national debt threatening that competitiveness.

I believe we can actually take smart, balanced steps in Congress today to address deficits, while maintaining those critical investments. In fact, the Center for American Progress has laid out a strategy to get to zero debt.

Senator MARKEY. So I ask this question in the context of the world in which we are living, looking at the Middle East——

Ms. TANDEN. Yes.

Senator MARKEY.—looking at other flashpoints around the planet. And from my perspective, we just have to learn how to work smarter not harder when we are making defense expenditures, when our history has been “all of the above, please,” just keep checking it off.

So right now, again, the Pentagon wants an air-launched nuclear cruise missile. My question is, do we really need a new air-launched nuclear cruise missile? Is that going to add to our defense, if it comes out of the kinds of programs that we need in a modern world where nuclear weapons are not usable?

We just had a good referendum in America on that issue, because if we actually needed to use them, we have plenty right now.

So can you deal with that, Mr. Haass, in terms of budgetary priorities from the defense perspective for our country over the next generation?

Ambassador HAASS. I would be happy to, Senator.
First, all things being equal, I do not think the defense budget is the place to go if you are thinking about resolving the debt issue, point 1. We are talking about just over 3 percent of GDP.

To use your number, if we are talking about spending $1 trillion over 20 years on nuclear systems, we are talking, in 10 years, about spending over $1 trillion a year on Medicare. The spending that is driving the debt will not be defense. It is going to be entitlements. Let's not kid ourselves.

Within defense, if you told me I have to make a choice where to put a marginal dollar, I would much prefer to put it on various types of conventional systems, sure. I would want to think about what we need to maintain, in particular, an adequate air and naval presence in the Asia-Pacific, what we need to maintain a sufficient air and ground presence on the European continent, enough Special Operations Forces to deal with counterterrorism in the Middle East and around the world.

I have not done, Senator, enough of an analysis so I could say $500 billion as opposed to $1 trillion or $300 billion on nuclear would be sufficient. I am just not up-to-date enough on it, so I cannot tell you that.

All I would say is I do not think the basic debate necessarily is this form of defense spending as opposed to that form of defense spending. I think we have to look at defense, which is one form of discretionary as opposed to other discretionary, and even more as opposed to nondiscretionary spending.

And a lot of the conversation here today has been about the two largest forms of nondiscretionary spending, which is the financing of the debt, given rates, what it costs us to pay for the debt, and second of all, entitlements. Those are going to be the real drivers here, much more than discretionary domestic or national security.

Senator Markey. I would say, if I may, Mr. Chairman, that when you are going over to entitlement programs, you are talking about grandma and grandpa, and you are saying they are the ones that must sacrifice. They are the ones that have to take the cuts. And if you are looking over at Medicaid, increasingly Medicaid is a program for grandma or grandpa to be able to stay in nursing homes with Alzheimer's, with Parkinson's, with these diseases. That is the fastest growing part of the Medicaid budget.

So as we talk about this, we are talking about education, health care, infrastructure on the discretionary investment side. And if you are looking at nondiscretionary, you are looking at grandma and grandpa.

And realistically, it is not going to happen. People are not going to step up and say we are going to dramatically slash either Social Security or Medicare or the kinds of Medicaid programs that are going to grandma and grandpa in our country. So just a realistic discussion about it, and accepting expert opinion that this debt that we have is not actually, right now, a threat to our country is I think a more realistic and honorable way of talking to the American people about it, because we are able to honor our obligations.

At the same time, however, we have to look at the programs that should be re-examined. I would actually put the nuclear weapons programs in a very high category.
I am going to make amendment on the floor before the end of the year on a lot of these nuclear programs. It will be a continuation of kind of the debate that we have been having in the country over the last 2 weeks about them, because it is a good way for the American people to access how the defense community views the kinds of weapon systems that they are believing that we need to protect America in the years ahead.

I think we all saw the horrified reactions of the American people when they thought that nuclear weapons were going to become more usable in the years ahead. This is something that I think is unrealistic, not going to happen, and not anything the American people want to have happen.

But we thank both of you for all of your fantastic service to our country.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you.

Senator Isakson?

Senator ISAKSON. Thank you, Mr. Chairman. It is a fascinating hearing. Thank you for calling it.

I apologize. I did not hear your testimony, but I read it. Listening to the questions, and I am kind of reminded of a story about a South Georgia Baptist deacon and his city flooded. He got the warning call that if he did not get up on his roof, he was going to die. So he got up on the roof of the house in the middle of the night and the waters kept rising.

A boat came by from the Red Cross in a few minutes and said, “Come on, jump in the boat. We’ll save you.” He said, “No, the Lord is going to save me. I’m not worried.”

A few minutes later, another boat came by and said, “Come on, jump in the boat. We’re going to save you.” He said, “No, I don’t have to worry. The Lord is going to save me.”

Then pretty soon a helicopter came over and dropped down a harness and said, “Please get on. The river is about to go over your house. You’re going to die.” He said, “No, don’t worry about that. The Lord is going to save me.”

A few minutes later, he was at Saint Peter’s gate. And when Saint Peter came out, he said, “What in the world are you doing here?” He said, “Well, I drowned. The water went over my roof.” Saint Peter said, “Well, we sent two boats and a helicopter to save you. Why didn’t you get on?”

I think sometimes we are not looking at the boats that are passing us by to save ourselves.

I would respectfully disagree that the debt is not a crisis. It is a major crisis. One of these days, the water is going to go over the roof, and we are going to be caught bad.

Mr. Haass, you have a great paragraph in here, which I will build on for my single statement and a question. You all call this a slow-motion crisis, which is like the waters rising and finally getting the Baptist deacon. But there are solutions.

In your testimony, you said that sequester is not one of them. It ignores entitlements and favors spending over investment and the present over the future.

With regard to Senator Markey’s statement a minute ago about Medicare reform and Social Security being about grandma and
granddad, that is not true. In 1983, when I was 39 years old, Ronald Reagan and Tip O'Neill made a deal. They said Social Security is going broke in 2015, unless we save it, and they came and said, okay, anybody who was born after 1943, you are not going to be eligible for Social Security until age 66, not age 65.

I was 39 in 1983. I was born in 1944, so they took away my first year of eligibility for Social Security. Then I did not know I would live to be 65, first. Second, I did not think the government was going to have any money left then anyway. So I did not really miss it. When I got to age 66 and finally qualified, I did not realize I missed a year.

So the savings and significant contribution you can make to the debt is not about grandma and granddad today. It is about my grandchildren and my children.

Just as the eligibility for Social Security will go to 67 in a couple more years because that reform, eventually it is going to need to go to 68 and then 69 and then to 70. We need to reform and calibrate the formula as people live longer and they are more productive.

And the savings are astronomical. Senator Corker was with a group that went to the White House. Remember when Ron Johnson did the calculation about the true value of the debt a few years ago, the debt at that time was $18 trillion. But if you take entitlements and leave them to go on their own and you do not raise a single dollar in taxes, or spend any more money on discretionary spending, the $18 trillion debt went $104 trillion in 10 years.

The time value of money and the compounding of interest is what all of us have to recognize in this solution. So we have to do spending reforms. We have to do revenue, as you said, things like that.

But we need to wake up to the reality that our long-term obligations factored now can ease the pain for grandma and granddad today but save Social Security for my grandchildren in the future.

Ambassador Haass. Thank you, Senator. I am glad you gave me a chance to respond to some extent also to Senator Markey. Senator Markey is a good friend, but I do not think framing the issue as grandma and grandpa is fair.

We want to make sure Medicare and Social Security are there for grandma and grandpa but also for their kids and grandkids. That seems to me that we keep in mind certain statistics.

If you are 65 years old today, the average American is going to live for at least another 20 years. Seventy-five years ago, if you were 65, you did not have anything like that kind of lifespan ahead of you. So we have to continue to raise eligibility ages for both Medicare and for Social Security.

We have to means test it. It is ridiculous that people who are relatively well off, someone like myself, would be in a similar position for someone who was impoverished.

So I think we need to take a look at these programs so, for the people who are truly needy, it is there. That is part of the social contract. I get it. That is just what we owe these people.

But we have to, again, take into account changing demographic realities. We have to take into account questions of income and
wealth. And then we can adjust these programs, so we have the coverage we need as a society.

That has to be part of the conversation. It cannot be all or nothing. These programs are going to have to be adjusted.

The good news is they can be adjusted so the bulk of these programs are there for those Americans who really need them. That has to be the goal.

Ms. TANDEN. May I respond?

Senator ISAKSON. Sure. Absolutely.

Ms. TANDEN. Is that okay? To the issue of health care costs, in particular, and Social Security.

I think that we should recognize with some note of optimism that we've actually seen real changes in the Medicare program. If you looked at CBO's projections in January 2010 versus what they are currently this decade, they show $1 trillion of savings in the Medicare program.

That is because we have had lower national health expenditures. And I think that is partly, although not purely, driven by the payment reform changes in the Affordable Care Act.

I think it is important to note that there are more reforms we can make to the Medicare program to ensure that beneficiaries are not bearing all of the burden of those changes.

I think we have put forward ideas at the Center for American Progress that address the way we pay for the Medicare program. Those are important parts of a discussion to ensure that we have savings over the long term in the entitlement programs.

I think the question is how we balance all of these issues together. Certainly, I will say again, that I think it is important to address these challenges. But it's also important to think about the impact of the decisions Congress makes when it chooses to reform entitlements or not invest in education; it's important to recognize how these decisions impact real people in our country. And Social Security is a good example.

Retirement savings are dwindling in the United States. Fewer people have the same level of savings that they have had in previous generations. So when you make a decision to change the Social Security system or cut Social Security for beneficiaries, that, you are doing so at a time when the majority of Social Security beneficiaries have less of a retirement cushion than they have had in the past.

So my view is that no topic should be off the table. Of course, we should address all of these issues. But we should also consider how these decisions impact people in the context of society.

Just one last point. Raising the Medicare age, I should note, actually increases the national health expenditures because it shifts costs to the private-employer system and increases costs in that way. So I think that is a strategy that is not particularly useful to help lower health care costs overall.

Senator ISAKSON. I will just add a comment. But, and this is my important point here, we already means test Medicare premiums. You pay your Medicare premium, the amount of your premium that you pay to Medicare is in part based on your income in the previous tax year. The better your lifestyle was, as Mr. Haass, your revenue was, the higher the premium you pay. I think it is up to
almost $1,000 a month, if you are a very wealthy person, versus under $125, if you are not. Those are approximate numbers.

My only comment was, discretionarily, we spend about $1.1 trillion a year in entitlements and benefit programs and the safety net, none of which I am opposed to. We spend about $2.6 trillion.

We have to be willing to do in the future what Tip O’Neill and Reagan did 33 years ago, and that is look at the out-years, the time value of money and the compounding interest, and the miracle of discipline. There are a lot of things we can do that will not hurt Granny or Granddad, will not hurt the sick and elderly, will make our future a lot brighter, and our debt and deficit a lot lower.

We cannot do the whole enchilada on that, but we can do a significant part of it because it is the largest contributor to the overall debt that we have.

Thank you very much for your time.

The CHAIRMAN. Thank you.

I have one question, and then I am going to summarize.

Ms. Tanden, we have people up here all the time talking with us about investments to make our economy stronger and our country stronger—infrastructure, education, things like that. You would agree, I would hope, that our unwillingness to deal with the entitlement issues thus far is what is crowding out much of that investment, would you not?

Ms. TANDEN. I guess I would just point out that Congress has made a series of decisions that actually have produced savings in entitlement programs.

The CHAIRMAN. First of all, on the Social Security issue, I agree that there are seniors who are very dependent upon that and have put forth policies to say for people like me who had some good fortune in life, that mine should not increase nearly as rapidly as those people who are more fully dependent upon it. That is one way of making this work better for people.

I agree with you 1,000 percent that the decisions that we make here affect real-life people, and we all know people that are very dependent upon this, and we need to take that into account.

But let me go back to the competitiveness issue. I do not see how anybody could debate that our unwillingness to solve with actuarial changes, not draconian changes—our unwillingness to deal with the entitlement issues thus far iswhat is putting the pressure on those things that many people think would make our Nation stronger.

It is our unwillingness over here because of the types of comments that Senator Markey made that were heartfelt, but it is that that is keeping us from doing much of what you would believe, I think, would be things that would make our country stronger.

Ms. TANDEN. I actually think that Congress has had a great deal of difficulty having an honest discussion about revenues. If you go through the last few budget debates, it does seem that there was more agreement on issues around entitlements than there was on revenues.

But I have to say I am an outside observer to that process and the committee would know better than I. But as an outside observer, it has seemed that it has been more difficult for the Congress to address the issues around revenue and a balanced ap-
proach, and I appreciate that Senator Flake and others have talked about it in this room. It seems like that has been a difficult issue, as well as perhaps entitlements.

The CHAIRMAN. Just for what it is worth, having been in the center of those conversations at the White House, and I think Senator Isakson was a part of that also, I think the issue has been that there is more than an openness on the revenue side, as long as people feel that there is a real solution being proposed on the other side.

I think what people do not want to see happen is an increase in revenues without commensurate actuarial changes to try to solve the other issue. I think people want to put forth a solution, not something that is a Band-Aid.

Did you want to make a comment, Ambassador? I was getting ready to summarize, but you look like you wanted to?

Let me say this, I have had fun jousting with you a little bit, Ms. Tanden.

Ms. TANDEN. And here I am.

The CHAIRMAN. You have a very warm personality and have some degree of humor, and I appreciate you being here.

Ms. TANDEN. Other people say it is more than that.

The CHAIRMAN. I am sure if I knew you better, I would be saying the same thing.

Before coming in, I expected that we were going to have a hearing where there was a central agreement over the fact that our national debt is a strategic problem for our country. And, by the way, it is such a privilege to serve in this body. Every day is like getting a Ph.D. in multiple topics. We have incredible access to information here.

But I thought your testimony, in some ways, was going to be fringe testimony, somewhat crackpot in some ways, relative to the debt. I am just being honest. I thought it was not going to aid the discussion.

But what I found in listening today is there truly is a difference—a huge difference, I might add—on each side of the aisle relative to the importance of us not having the kind of indebtedness that we have today. That is something that I have learned today.

I am shocked by that, in many ways. It discourages me, relative to our Nation actually solving this problem.

Typically, we have an agreement on the problem; we have a disagreement on how to solve the problem. Today, what I find is that we have a disagreement as to whether there is a problem or not. I find that incredibly discouraging.

So I want to apologize to you, because actually your testimony represents, it appears to me, a widely held view on one side of the aisle, which is something that I just did not expect out of this meeting.

Senator CARDIN. I know you want to close, but could I just impose upon your good humor from one more moment.

That is, I disagree with that summary, and I just want the record to reflect that. I have done some very unpopular things to reduce the deficit, including cutting spending, voting for spending cuts that were popular, and voting for tax increases, which are
never popular, in order to reduce the deficit and to bring our budget into balance.

I do not like deficits, particularly when you are wealthy enough and strong enough to be able to pay for it. And I think America is strong enough and wealthy enough to pay our bills. So I do not like deficits.

But the point, I think, that some of us on the Democratic side have been making is that how you deal with the deficit is just as important as the deficit. If the consequences of dealing with the deficit is to deny the governmental sector, which is a critical part of the economy, to function, you can hurt the economy and your country. Where if you do not make the investments, and it could be in soldiers, it could be in guns, it could be in schools, it could be in border infrastructure, if you do not make those investments, you are compromising America’s security.

But I do not want you to leave with the impression that the Democratic side of this committee is insensitive to the deficit. We are not. Some of us served in Congress when we voted to balance the Federal budget, and we actually got it balanced.

I fully agree that you have to take a look at all aspects. Nothing should be left off. You have to look at spending.

I think you have to look at the tax code, if you want to know the truth. I think our tax code is terribly inefficient. As I have shown by a proposal that I made on progressive consumption tax, you can have the lowest marginal rates in the industrial world, and have a more progressive tax code than we have today and bring in the revenues you need in order to pay our bills.

So there are ways that we can do this working together. So I would hope that, in regard to budget issues, that Democrats and Republicans could learn from each other. We are both concerned about the debt and deficit.

I think Democrats are very concerned that there be adequate revenues in order to be able to make the investments that we think are important for the growth of our Nation. I think Republicans are very concerned that we do not hide the cost of spending, particularly on mandatory spending, and that we have reasonable, foreseeable, affordable programs in the future.

I think we can listen to each other and learn from each other and pass a blueprint that would not only provide for the economic growth of our country, but deal with the security issues that you have raised, and the reason why we are having this hearing, because large, uncontrollable debt can compromise America’s security, no question about it.

The CHAIRMAN. I would just say that I appreciate you saying that. I have been in meetings with you. I remember one of the first meetings we had, when I barely knew you, was over fiscal issues one evening, and I was surprised, actually, because of the State you represent, by your seriousness about that issue.

I will say again—you didn’t hear some of the questioning that took place—I was somewhat surprised by some of the commentary here, and the thinking that the markets are treating us well, we really do not have an issue here that is particularly important, as was laid out in Ms. Tanden’s testimony.
I am just saying to you, after listening to the entire session today, I never would have thought that there would have been a difference—sure, as to how to solve it, I got that. That is the tough work that has to be done, and both sides are going to have to give. And I agree both sides can learn from each other.

But I leave here today with a sense that there is also a significant difference among members as to whether this is a strategic issue or not. And that is not what I expected to come out of this hearing.

But I thank you both. You have actually spurred one of the most interesting discussions we have had here. I appreciate your testimony.

If possible, we would like to leave the record open until the close of business Friday. If you could do your best to respond to written questions, as soon as you practically can, we know you both have day jobs.

Thank you for your testimony again, and this meeting is adjourned.

[Whereupon, at 4:06 p.m., the hearing was adjourned.]