BUSINESS**FORWARD**

7 THINGS BUSINESS LEADERS KEEP TELLING US ABOUT AVOIDING DEFAULT

Over the past 10 years, Business Forward has helped more than 270,000 entrepreneurs, executives, investors, and small business owners work with local media, lobby Congress, publish op-eds, submit testimony, and advocate online. More than 1,200 mayors, governors, Members of Congress, and senior Administration officials have participated in one of our briefings (including three presidents).

We have organized hundreds of briefings that covered our national debt, budget negotiations, and fiscal cliffs. Here are seven points our business leaders tend to make, which you should consider as we approach yet another fiscal cliff on June 1.

1. THERE'S A GOOD REASON FOR 60+ YEARS OF BIPARTISANSHIP ON RAISING THE DEBT LIMIT: ANYTHING ELSE COULD DAMAGE OUR CREDIT, CAUSE A RECESSION, AND DESTROY MILLIONS OF JOBS.

To understand what's at stake, consider how much we all benefit from being the world's "safe harbor." The U.S. is a reliable partner (with reliable courts and rule of law) that pays its bills. That's why foreign lenders offer our governments, businesses, and consumers easier, cheaper credit. Foreign investors also favor our stocks, real estate, and other assets, boosting their value. Foreign governments and businesses prefer to transact deals in dollars, which boosts demand for dollars, meaning your dollar is worth more and it is cheaper for Americans to import goods.

If we default, a number of bad things happen all at once – and those things start amplifying one another immediately. First, lenders will reduce exposure to U.S. debt, which means our governments, businesses, and consumers will have less capital, and they'll pay more for the capital they get. Foreign investors will lose interest in U.S. assets, relative to assets in Europe or Asia, meaning prices for U.S. stocks, real estate, and other assets will fall. The dollar, no longer safer than other leading currencies, will weaken, which means we all pay more for imports.

Next, U.S. businesses and consumers, stung by what happens above, will pull back on spending and investing. Lenders will grow even more cautious, and asset prices will fall even further. This hurts investment, which hurts employment, which hurts spending, and so on.

It's never a good time to default on your debt, but this is a particularly bad time to test the system. Our financial system is still recovering from disrupted supply chains, war in Ukraine, and the ongoing threat of bank runs.

2. WE HAVE A PROVEN PROCESS FOR FIXING OUR BUDGET: IT'S CALLED "THE BUDGET PROCESS."

Anyone arguing that this is our last chance to cut long-term spending should remember that Republicans control the House and the budget process. Republicans and Democrats have come together to increase the debt limit 78 times since 1960 because tough questions – like whether to cut veteran's care, border agents, and air traffic controllers – are best resolved by a comprehensive appropriations process that forces the House to agree on priorities and cuts they can negotiate with the Senate and White House.

The House failed to enumerate two-thirds ($3.2T) of the $4.8T in cuts it promises, because Republicans can't agree on what gets cut[1]: And we have only weeks to figure out what they meant. Should President Biden negotiate with the Republicans who voted to cut veteran's care by 22% and are proud of it, or the Republicans who voted to cut veteran's care by 22% and deny it? Cuts to veterans, border security, and air traffic safety are tough questions that divide both parties. Threatening to default on our debt without addressing those questions is irresponsible.

3. SOME PEOPLE CONFUSE DEFAULTING ON OUR DEBT WITH SHUTTING DOWN THE GOVERNMENT. BOTH CAN CAUSE MARKET SELL-OFFS, BUT ONLY DEFAULT RISKS A FINANCIAL CRISIS.

When Congress and the White House can't agree on future spending, it can "shut down the government." It's a big deal, but contained. They've forced our national parks to shut down and non-essential workers to stay home. But essential government services, like border security and air traffic control, have always continued. Payments to households (like social security checks) and businesses (payments for companies fixing bridges) also continued.

When Congress refuses to honor U.S. Government (USG) "checks" it just "wrote," which messes with $17B in daily payments, credit ratings affecting $31T in national debt, and the financial world order. Past government shutdowns caused market selloffs, but they did not create financial crises. Defaulting on the debt is more likely to cause one.

4. AMERICAN BUSINESSES ARE COUNTING ON THE PROGRAMS AND INVESTMENTS SOME IN CONGRESS WANT TO CUT.

Abrupt cuts to government investments Congress approved last year could blow up (much larger) private sector investment. For example, in response to incentives and investments from Washington, automakers plan to invest hundreds of billions in new U.S. electric vehicle plants, battery supply chains, and workers. But those investments depend on the USG to help jumpstart the mining of critical minerals here in the U.S., build more charging stations, and make good on the purchase incentives Congress approved last year. If we cut the USG's contribution, automakers' investments will fail.

Similarly, proposed cuts to air traffic control could cause two-hour delays at airports this summer, on average. Worse, those cuts would reduce the number of air traffic controllers, causing smaller airports across the country to close. Manufacturers rely heavily on those airports.

5. THE DAMAGE DEFAULT COULD DO TO OUR ECONOMY – AND YOUR FAMILY – COULD OUTWEIGH ANY SAVINGS FROM CUTS TO GOVERNMENT PROGRAMS.

By causing a prolonged default, Republican negotiators could start $750B in the hole, relative to where they'd start if they stick with the budget process their House majority controls. Economists at the Brookings Institution project $750B in added orrowing costs over the next 10 years[2]: That's about $6,500 per household in additional spending that adds nothing to our lives.

The difference between a "clean" debt limit increase and a prolonged default? 8.9 million jobs. If we follow established budget procedure, our recovery continues, and we create another 900,000 jobs over the next few quarters. If we allow a prolonged default, we destroy 8 million jobs in the next quarter alone[3].

Consider what default does to American businesses and families. Saving $4.8T over 10 years may sound good on its face, but prolonged default could destroy 8 million jobs[4] and cause our stock markets to fall 45%[5], while a new homeowner obtaining the average new 30-year mortgage ($364K) on the median home ($455K) could pay an additional $130K more in interest costs[6].

And rocking the global financial system when it's weak (like it is now) could lead to scarier possibilities, like "mass liquidation events."

If Uncle Sam bounces checks, millions of businesses and consumers could bounce their checks, too. The U.S. issues about $17B in payments a day, on average. If those checks bounce, the creditors, vendors, and employees depending on that check could end up bouncing the checks they have written to their creditors, vendors, and employees – multiplying the damage.

6. MORE CREDIT (AT LOWER RATES) BUILDS WEALTH; LESS CREDIT (AT HIGHER RATES) DESTROYS WEALTH.

Spain is a great country, but it's not as reliable as the U.S., so lenders offer Spain less credit – and charge Spain more for each dollar (or Euro) it borrows: Becoming less like America and more like Spain is expensive. Moody's rates America's credit AAA, the highest given, while Moody's rates Spain A3 (below most of Europe, but ahead of Mexico and Russia). America pays lenders about 4.25% on our 10-year bond. Spain has to offer investors 4.63%. That's nearly $4B more each year to borrow $1T. Our current debt is about $31T. Brookings estimates a default could add $750B to our debt service costs over 10 years. That's about $5,800 per U.S. household.

Consider Tom and Sue. Sue and Tom each earn $150K/year. Each wants to purchase a $400K home. Sue who has good credit, can borrow up to $526,000 at 6%/year. Tom, who has bad credit, can borrow up to $450,000 at 8%/year. If Sue buys the same type of house Tom buys, she'll spend $484 less per month for the same size mortgage. That adds up to $174,240 over 30 years. But Sue can also invest those savings in her IRA, which could grow to $570,570 (at 7%/year). Over time, the difference in wealth between Sue and Tom grows.

7. TOUGH TALK ON DEFAULT ISN'T CHEAP, BECAUSE IT'S NOT REALLY A "FISCAL CLIFF." WE'RE ALREADY RUNNING DOWNHILL.

Pain has already started; brinkmanship has already hurt growth. We have started a gradual descent (scare tactics, bad faith negotiations) that has already increased our government borrowing costs.[7] This could be followed by a nasty cliff (a "technical default" that lasts hours or days), which could be followed by an even nastier cliff (if default lasts days or weeks). In 2011, S&P downgraded America's debt before the X-date. That same year, our stock markets fell 17% before the X-date, primarily due to concern over default.

1. THE WALL STREET JOURNAL "GOP'S DEBT-CEILING PROPOSAL: WHERE DO REPUBLICANS WANT TO CUT SPENDING?" HTTPS://WWW.WSJ.COM/ARTICLES/GOPS-DEBT-CEILING-PROPOSAL-WHERE-DO-REPUBLICANS-WANT-TO-CUT-SPENDING-366A29B6
2. BROOKINGS INSTITUTION, "HOW WORRIED SHOULD WE BE IF THE DEBT CEILING ISN'T LIFTED?" HTTPS://WWW.BROOKINGS.EDU/2023/04/24/HOW-WORRIED-SHOULD-WE-BE-IF-THE-DEBT-CEILING-ISNT-LIFTED/
3,4. MOODY'S ANALYTICS, "GOING DOWN THE DEBT LIMIT RABBIT HOLE," MARCH 2023.
5. CEA, "THE POTENTIAL ECONOMIC IMPACTS OF VARIOUS DEBT CEILING SCENARIOS," MAY 3, 2023. HTTPS://WWW.WHITEHOUSE.GOV/CEA/WRITTEN-MATERIALS/2023/05/03/DEBT-CEILING-SCENARIOS/
6. THIRD WAY, "THE DOMINOES OF DEBT LIMIT DEFAULT," DECEMBER 2022. HTTPS://WWW.THIRDWAY.ORG/REPORT/THE-DOMINOES-OF-DEBT-LIMIT-DEFAULT
7. CEA: THE POTENTIAL IMPACTS OF VARIOUS DEBT CEILING SCENARIOS, MAY 3, 2023. YIELDS ON SHORT-DURATION TREASURY BILLS AROUND THE EXPECTED X-DATE HAVE INCREASED 1 PERCENTAGE POINT, OR 20 PERCENT. THE COST OF INSURING U.S. HAS ALSO RISEN.