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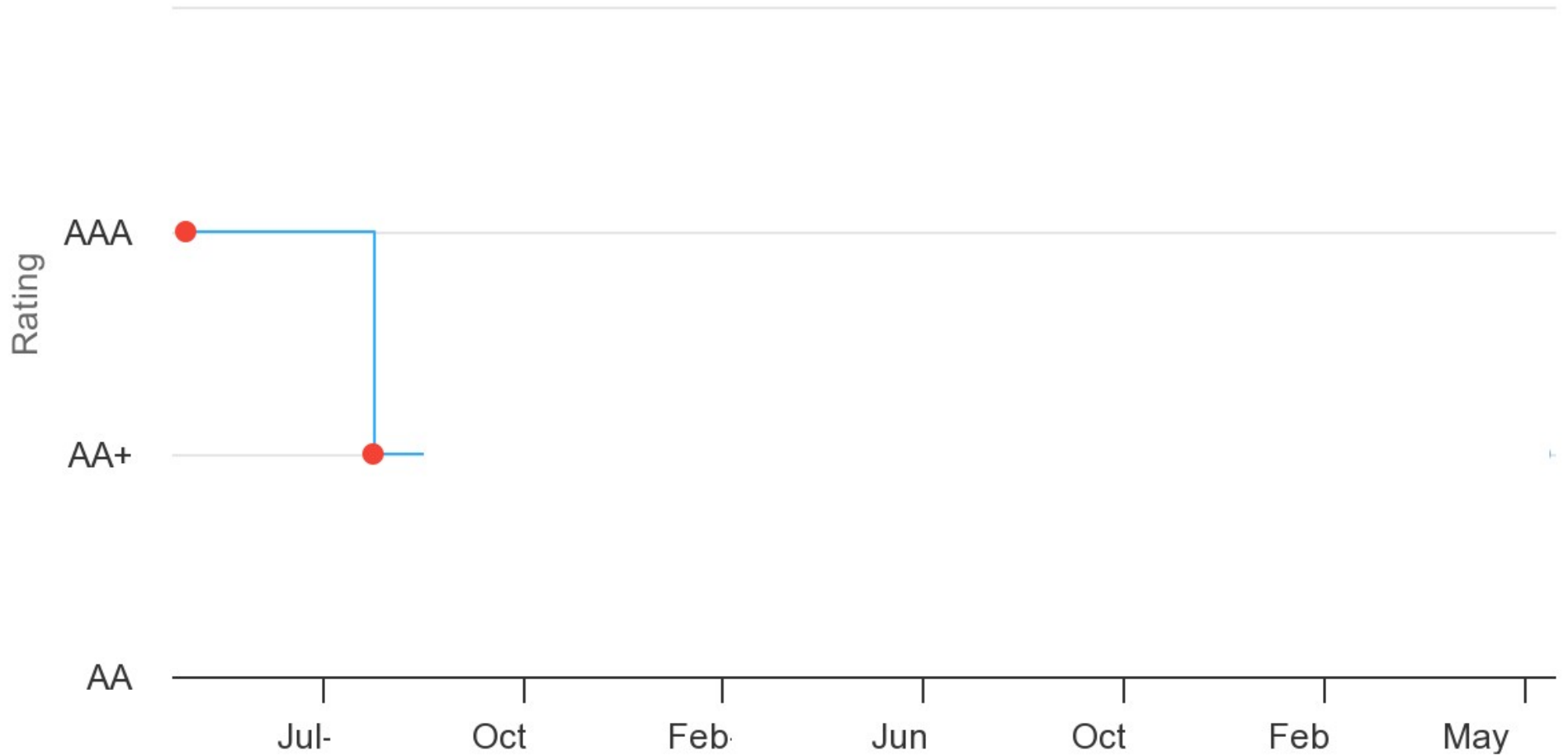
T H E
U W
N O W

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University of Wisconsin*

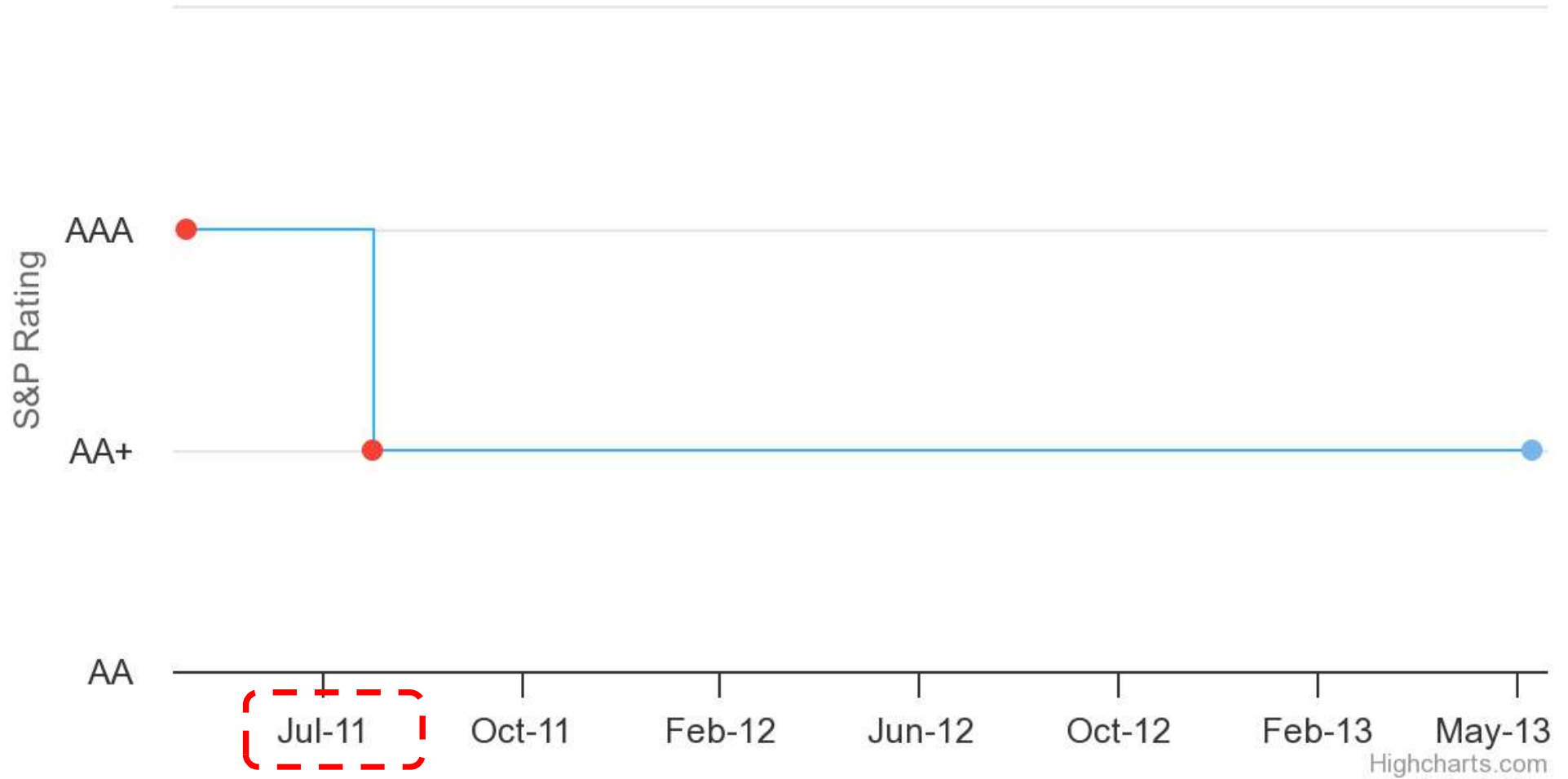
The Downgrade, The Debt Problem, and the Macro Outlook

United States historical ratings



United States historical ratings

S&P Agency



United States historical ratings

Fitch Agency

Fitch Rating

AAA

AA+

AA

May-95

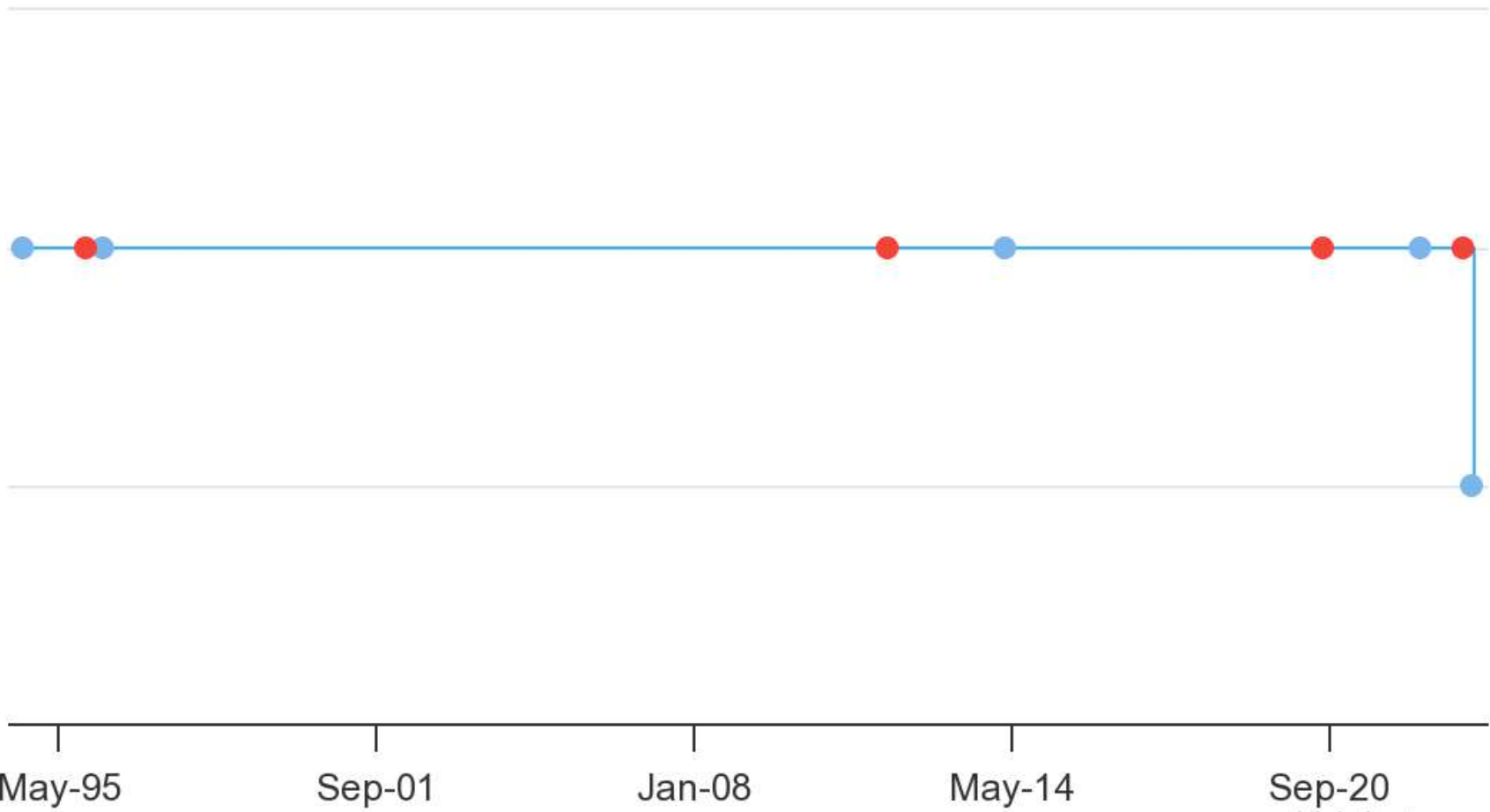
Sep-01

Jan-08

May-14

Sep-20

Highcharts.com



The S&P downgrade took place over a decade ago

- No clear impact then
- No noticeable impact likely now
- Why do we care about ratings?
- For private corporations, historical records can inform ability to pay
- For nation states, credit ratings measure both ability *and willingness to pay*

Fitch's Rationale

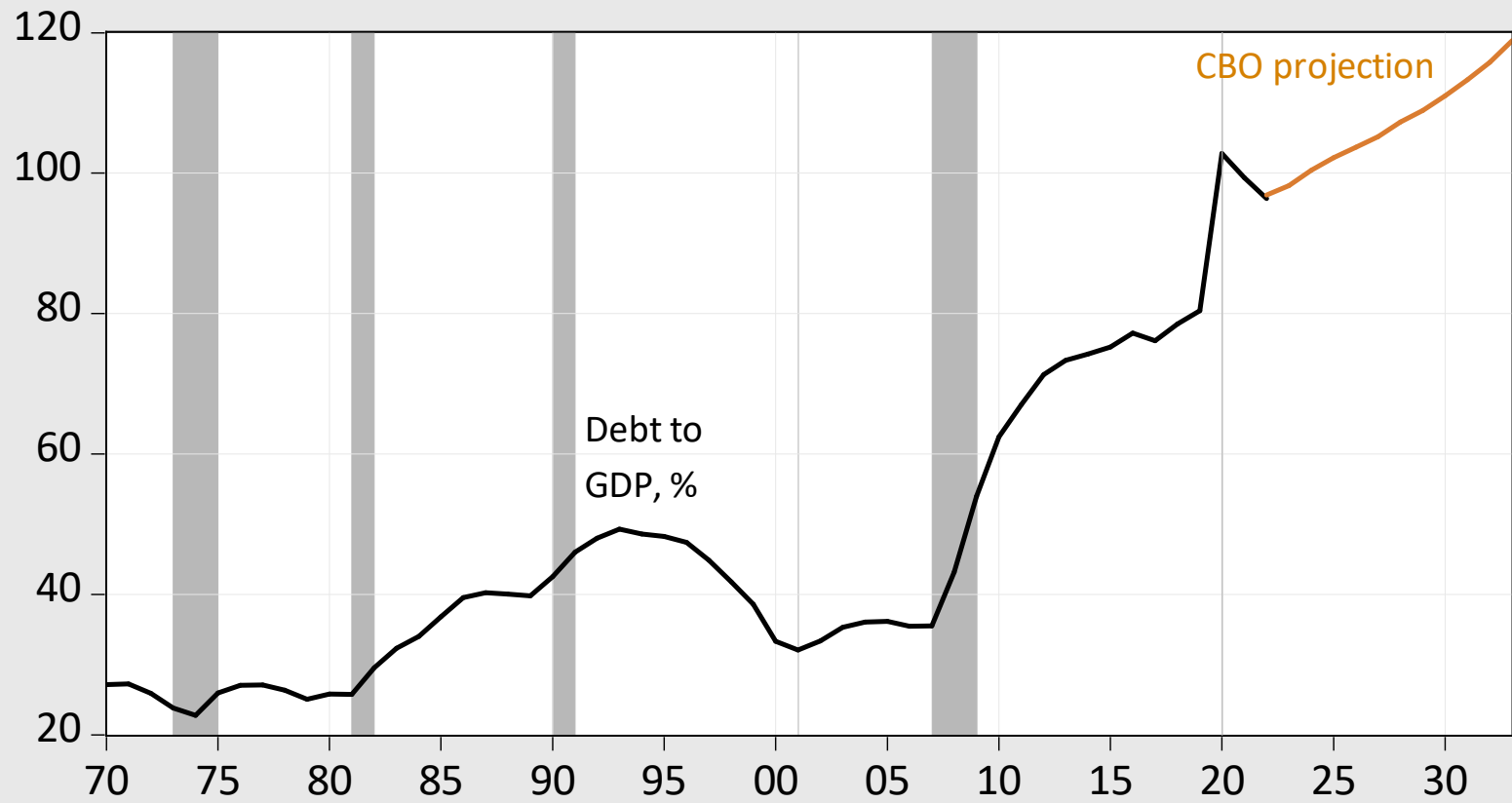
“The rating downgrade of the United States reflects the expected fiscal deterioration over the next three years, a high and growing general government debt burden, and *the erosion of governance* relative to 'AA' and 'AAA' rated peers over the last two decades that has manifested in repeated debt limit standoffs and last-minute resolutions.”

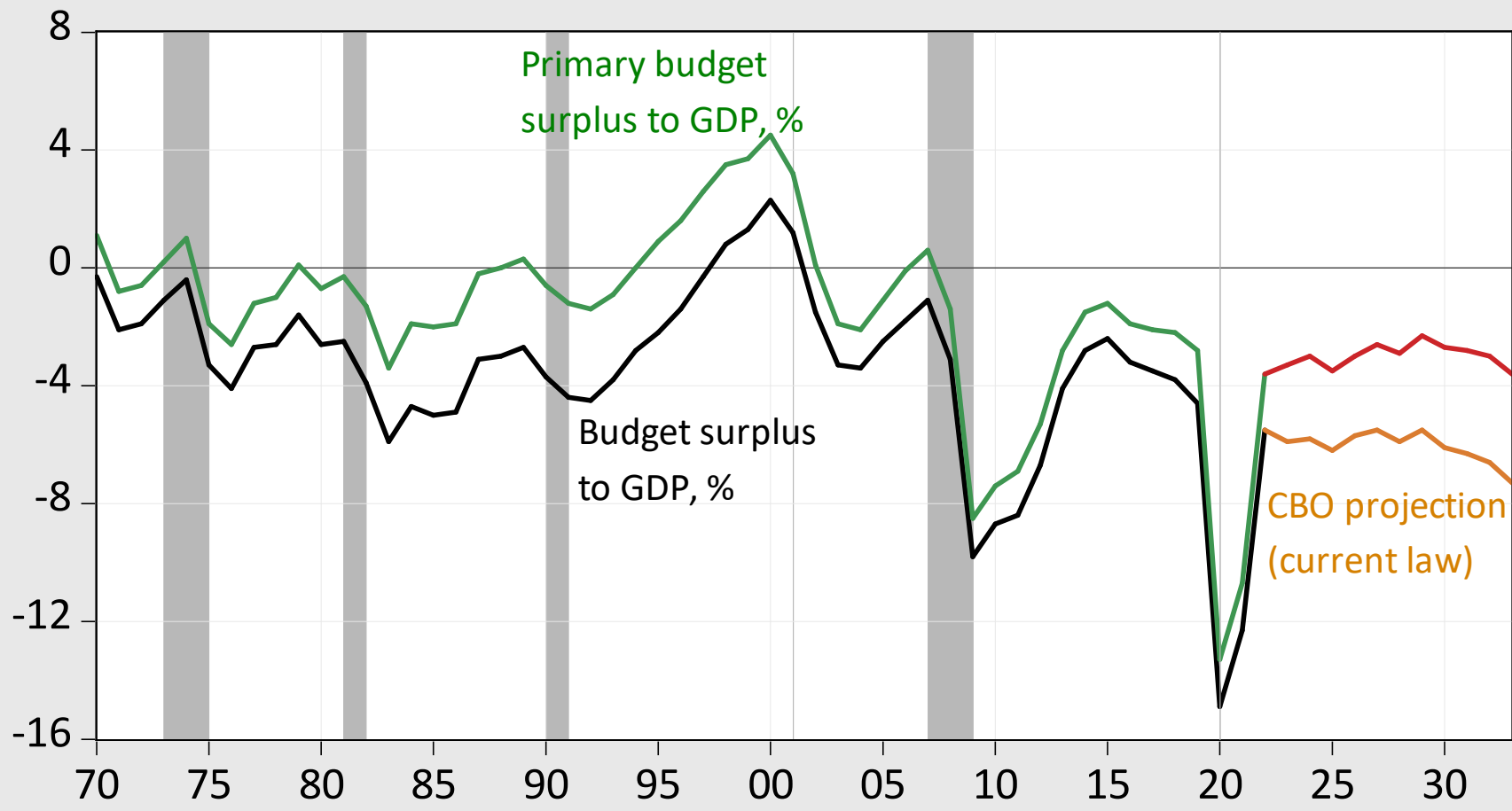
Compare US 2023 to Argentina 2001

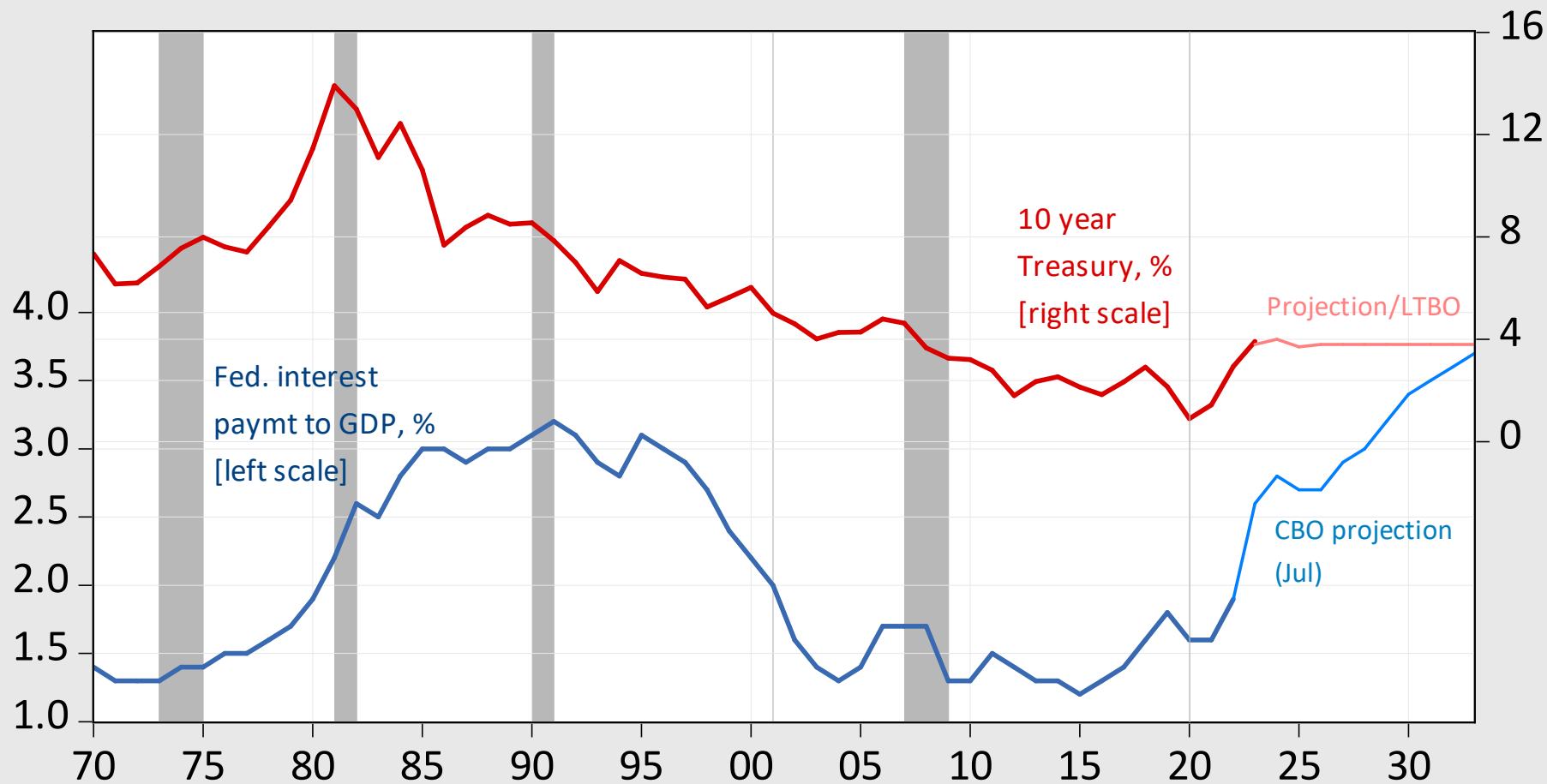
- Argentina had foreign currency debt
- ...Growth slower than the interest rate
- ... And a technical constraint (tax collection system) combined with political inability to cut spending
- The US is growing faster than the real interest rate (for now)
- ... runs its own monetary policy
- ... and US borrows in its own currency

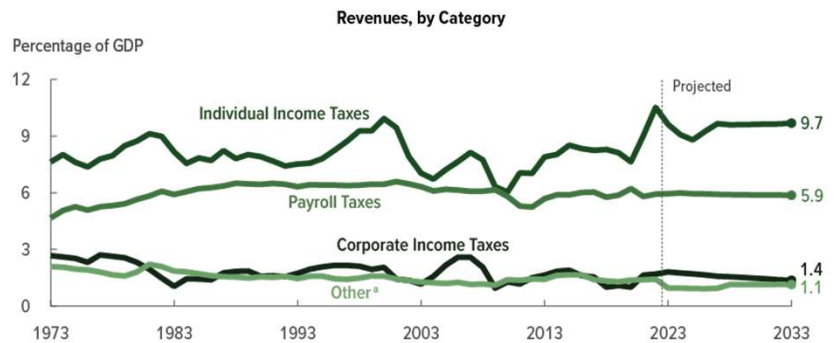
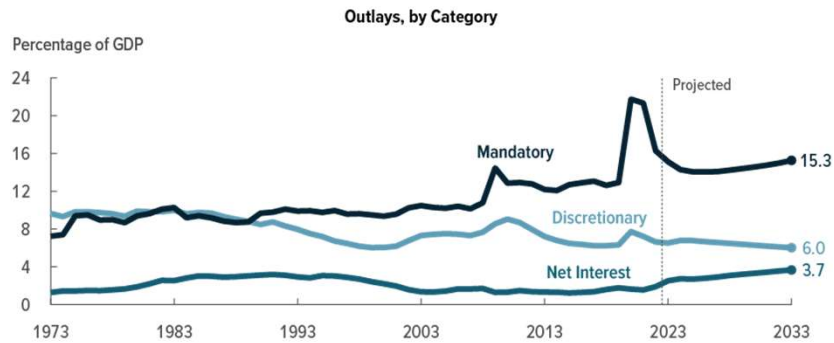
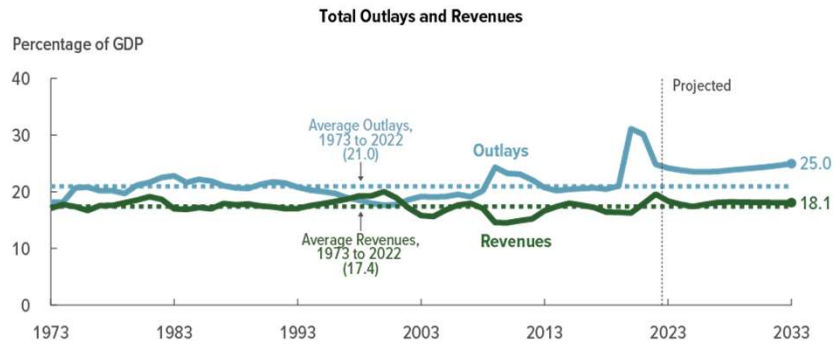
The Real Problem

- The US is running large budget deficits
- Growing entitlement costs will deplete the trust funds
- Entitlements will squeeze out discretionary spending (defense, everything else)
- We have the technical and economic capacity to raise revenues
- Which if combined with do-able modifications to Social Security can slow the growth of debt

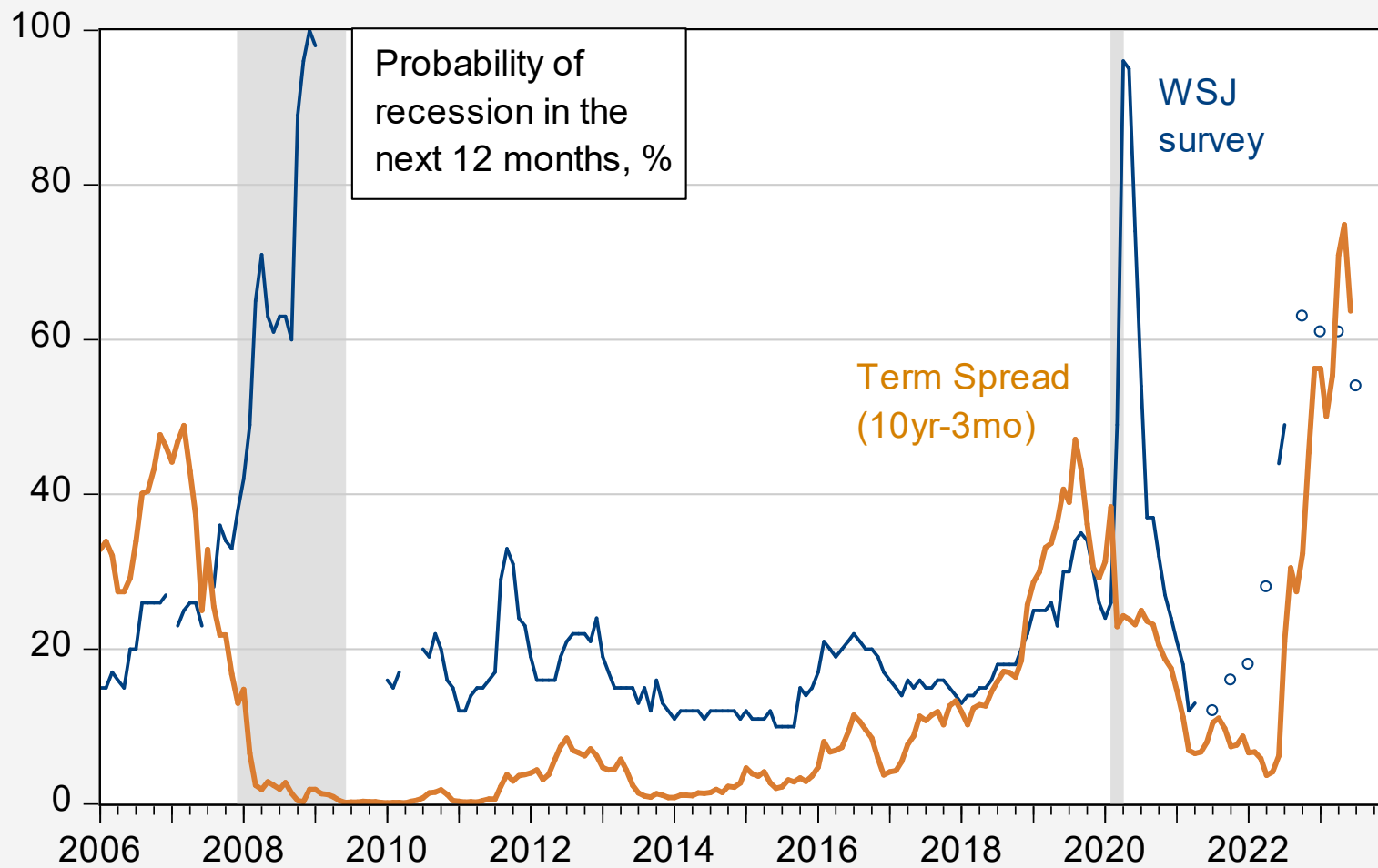


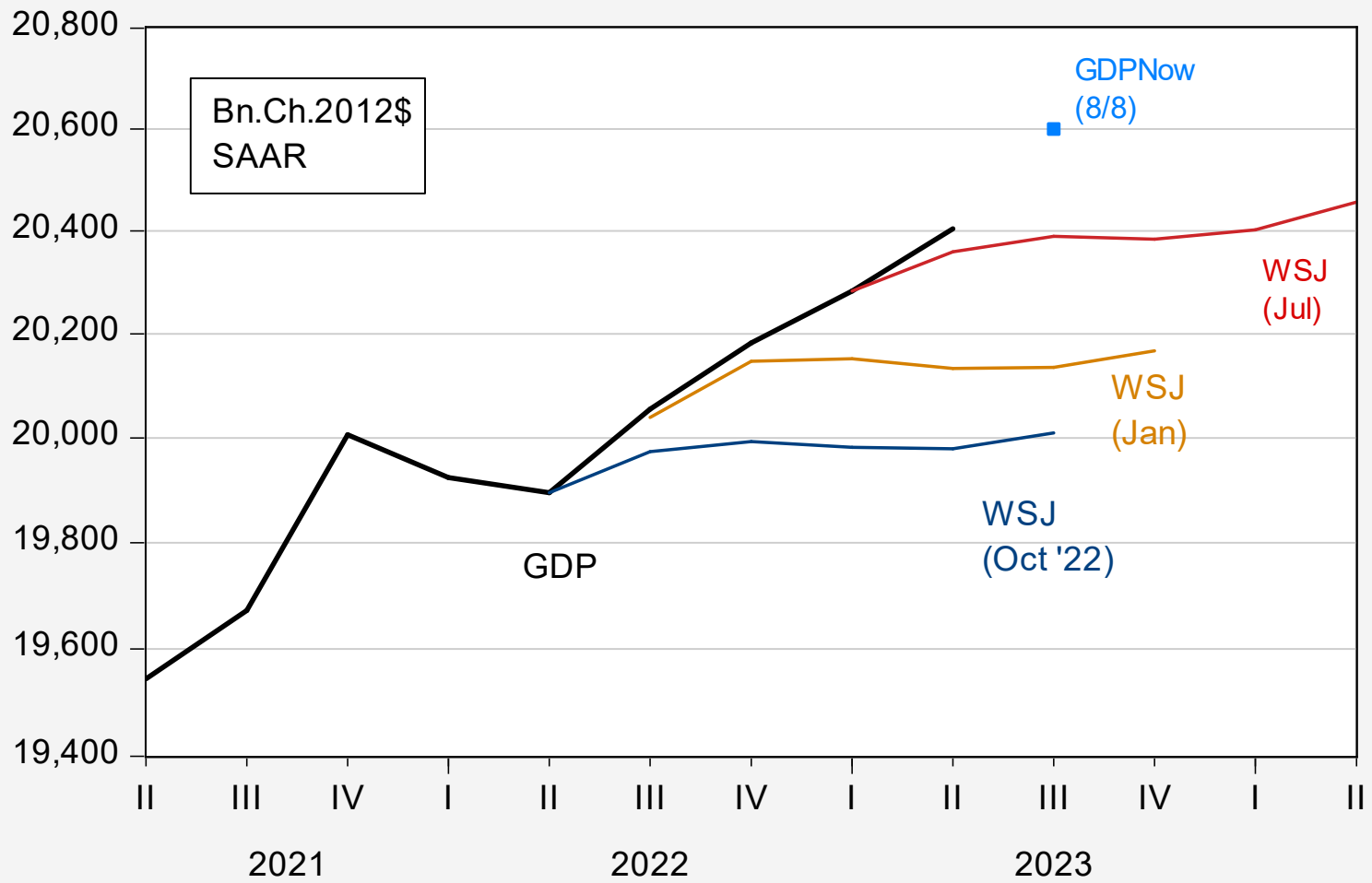


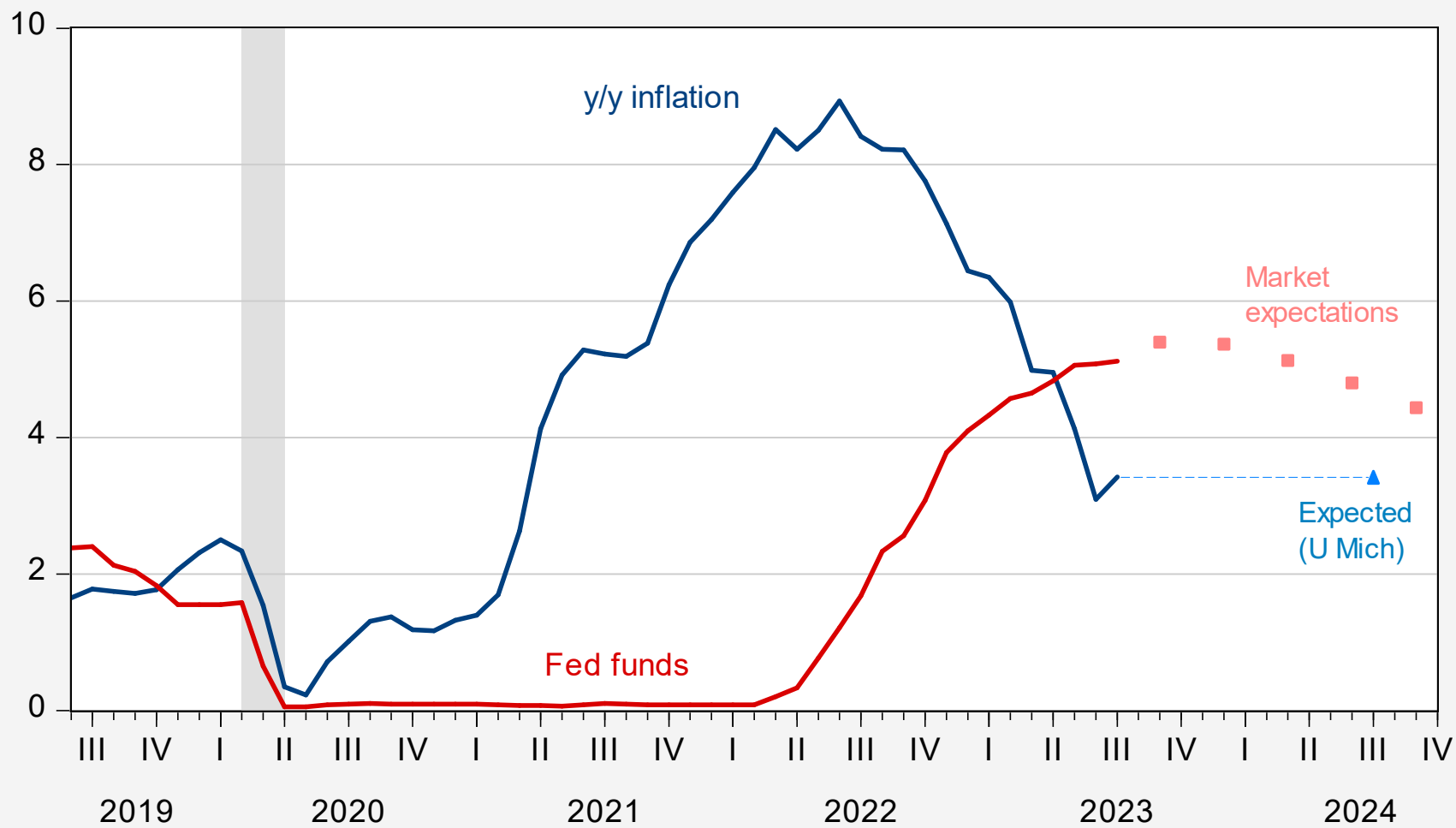




- Revenues are stable
- But outlays – particularly mandatory spending – keeps on rising
- Larger debt combined with rising interest rates squeezes out discretionary spending over time
- *In short term* there's no problem







Keeping Things in Perspective

- US short term outlook is improving
- And is better than the one facing the Euro area, UK, Japan
- But can be knocked off course by energy, geopolitical disruptions or a big China slowdown
- Medium term outlook largely unchanged with respect to fiscal policy and debt
- But they are technically fixable with the proper policies

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