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Date: 8/4/99 2:44 PM
Normal
TO: senator at Collins-DC
Subject:
------------------------------------ Message Contents

Dear Senator Collins:

The Treasury Department is looking into buying back some government securities with the budget "surplus". Good idea, like paying down your highest debt financing, but it needs more scrutiny.

We should first call all callable Federal securities (with higher rates of return) possible, to take advantage of those conditions in our favor. As a bonus, we'll be collecting capital gains taxes. This always happens as market yield go down; value of bonds with above-market yield goes up in inverse relationship. Economics 101 says we should already be doing this.

However, no one is going to surrender a non-callable security unless he is going to at least break even on it, getting a similar yield (after adjustment for taxes and expenses). Turning it in to the government is going to incur a capital gains tax unless you have a situation where you have losses to offset those capital gains. A good example would be an insurance company; many are currently showing a lot of red ink. However, insurance companies like having high levels of investment income , it allows them to keep prices lower. Hopefully the Treasury won't be motivated to make a political gesture to preserve someone's legacy and overspend money foolishly.

We could sell new securities at a below-market yield, and discount the face amount, using the "surplus" to fund this. This would result in lessened payments over the next 10-20 years or so, less pressure on the budget from allocating monies to pay interest costs if we slide into a recession. At the end of the term, the owner would turn them in, collect the face value and pay tax on a long-term capital gain since they bought the security at a discount. There's no benefit for the rich here; no one gets a freebie since the interest rate they are receiving is exactly the market yield on their investment right up until the day they turn the note in.

One of the reasons that the budget deficit accelerated so much in the Reagan years was the increased rate we had to pay on government borrowings, thanks to the Carter Administration. Every additional dollar that had to go to pay interest on a 10 or 12% Treasury note came out of tax revenues or more borrowings. Prior borrowings that had to be rolled over (borrow more to pay off noteholders) were renewed at those higher rates. I'm not saying that that was the whole reason for the deficits brought upon us by a Democratic Congress (remember, this budget is dead on arrival, per the Tipster), but it wasn't chicken feed either. Instead, it was a big lump of double digit interest rates that had to work its way through the system. Most of those notes were passing out of the system in the late 80's and early 90's, to be replaced at much lower rates and paving the way (along with the Democratic tax increases of '90 and '93, and the Republican choice of Alan Greenspan) for the stupendous (PROJECTED) surpluses we see today, before consideration of actually funding Social Security.