

A letter on the US debt bubble

28 July 1999

Dear Editor:

There are serious problems with Blecker's analysis in "The Ticking Debt Bomb". The expansion in the absolute levels of foreign holdings of US financial assets relative to US holdings of foreign financial assets reflects the inflation in US asset prices relative to Asian and European asset prices. Blecker explains that his measure of foreign asset holdings is based on projecting historical measures forward using the appreciation in the S&P composite stock market index. (Notes to Figure 3, page 8.) Given that about half of foreign holdings of US corporate securities are bonds, which have not appreciated at the rate of stocks, his figures will tend to vastly overestimate the increase in foreign asset holdings. The data his projections are based on can be found at

<http://www.bea.doc.gov/bea/di/bpatbl-d.htm#int-inv>.

And if the stock market suddenly crashes, the value of foreign-held equities will also crash, eliminating the equity part of the "problem" in the course of an afternoon. Foreign holdings of US Treasury bonds are somewhat more worrisome, but the annual debt service burden is only about \$78 billion (1.3 trillion x 6%, the market yield on the 30-year bond). This is less than 1% of US GDP, which compares very favourably to the external debt service burden of other governments.

The second concerns the measurement of investment. The reported figures are measurements of fixed capital formation. Although investment in software and information technology are included in this category, they are poorly measured. The rapid deflation of prices in the information technology sector creates a downward bias in the measurement of investment. As firms invest more heavily in information technology, the investment figures reported in the national accounts become more and more misleading. The investments of US corporations in information technology are showing up in increasing productivity levels. Changes in the productivity of investment are far more important than

minor fluctuations in the level of investment. Neoclassical analysis would argue that consumption is rising because people believe that current investments will yield high levels of output in the future. (Of course people might turn out to be wrong!)

Thus Blecker's evidence does not support the two key ingredients of his argument: that the US faces an onerous external debt burden, and that US investment is not capable of generating the returns needed to service the level of debt.

This is not to deny that the speculative bubble gripping the US stock market and spreading to the US real estate market may well end badly. The high consumer debt levels suggest that the US economy is unusually vulnerable to a shock to aggregate demand. Nor am I suggesting that information technology has created a new golden age for capital where a financial crisis will not occur. But there are reasons to believe that information technology has (i) increased the productivity of workers (ii) increased capital's share of workers' output. Since the US is the undisputed leader in the application of this technology, it seems to me that even a Marxist analysis supports an appreciation in the value of US capital assets.

All in all, it seems to me that you need to view reports that support your criticisms of financial capitalism with the same critical eye you cast on those that don't.

IM

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