Ratings agency S&P downgrades outlook for US government debt

Andre Damon, Barry Grey
19 April 2011

Standard and Poor's (S&P), the debt rating agency, announced a lowering of its outlook for United States debt Monday, in a move aimed at pressuring the US government to set in place harsh austerity measures before the 2012 elections.

S&P changed its outlook on the AAA rating of US debt from stable to negative. In a press release, the rating firm quoted its credit analyst, Nikola G. Swann, as saying: "Our negative outlook on our rating on the US sovereign debt signals that we believe there is at least a one-in-three chance that we could lower our long-term rating on the US within two years. The outlook reflects our view of the increased risk that the political negotiations over when and how to address both the medium- and long-term fiscal challenges will persist until at least after the national elections in 2012."

S&P, along with Moody's one of the two major credit rating firms in the US and internationally, left little doubt that it was intervening in the official political debate over the budget for fiscal year 2012, which begins October 1, 2011, as the representative of Wall Street. In effectively issuing an ultimatum to the Obama administration and Congress to pass legislation imposing unprecedented cuts in social programs with devastating implications for working people, S&P was applying to the US the tactics employed by it and other rating agencies and the international banks to force through brutal austerity measures in Europe.

Over the past two years, strategic credit warnings and downgrades on the sovereign debt of countries such as Greece, Ireland, Portugal and Spain have been used to encourage speculative attacks on those countries' credit and whip the respective governments into line. By fostering an atmosphere of intense crisis, these moves are intended to create more favorable political conditions for overcoming popular opposition to the gutting of social services, jobs and wages.

This is the first time in its 70 years of rating US debt that S&P has lowered its outlook for the US. Over this period, the US has always maintained the highest rating of AAA. Were its debt to be downgraded, the implications for the American and world economy would be far-reaching and convulsive. US Treasury securities have long been considered the safest investments in the world and are held in the trillions of dollars by banks and governments internationally. Their credit-worthiness is bound up inextricably with the role of the US dollar as the leading world reserve and trading currency.

S&P's announcement triggered a fall in stock markets in Europe and a sharp decline on Wall Street. The Dow Jones Industrial Average fell 140 points, or 1.14 percent, for the day. The S&P 500 and Nasdaq indexes also closed more than 1 percent down on Monday.

The warning takes place as the Obama administration and congressional Republicans, after agreeing on $38.5 billion in cuts for fiscal year 2011, are staging a public debate on the 2012 budget, with both sides agreeing in advance on the supposed need to slash trillions of dollars in social spending and impose historic cuts in the government health care programs, Medicare and Medicaid, over the next decade.

The effect of S&P's announcement will be to further shift the framework of the official budget discussion to the right, giving the Republicans an excuse to demand even deeper cuts and Obama and the Democrats an excuse to accommodate them.

The S&P press release quoted Swann as saying in regard to the budget and deficit-reduction: "More than two years after the beginning of the recent crisis, US policymakers have still not agreed on how to reverse recent fiscal deterioration or address longer-term fiscal pressures."

The release described Obama's budget plan announced last week as reducing the federal deficit by $4 trillion over 12 years and the Republican plan approved by the House of Representatives as cutting the deficit by $4.4 trillion over 10 years. It stated no preference between the two plans, instead demanding that the two sides come to a quick agreement.

"We believe there is a significant risk that congressional negotiations could result in no agreement on a medium-term fiscal strategy until after the fall 2012 congressional and presidential elections," the press release stated. This was an implied threat to downgrade US sovereign debt if no austerity program is passed before the elections.

John Authers of the *Financial Times* pointed out the agenda behind S&P's move, noting, "Politicians normally require a full-blown financial crisis to galvanise them into action. S&P's move is a provocative but sensible attempt to get Washington to act, without putting everyone through another financial crisis."

In 1996, Moody's threatened to downgrade the US federal debt, but changed its outlook after Congress raised the US debt ceiling. But in today's announcement, Standard and Poor's did not even mention the debt ceiling as a concern, despite the fact that Congress must raise the current debt ceiling by early July to avert a default on US government debt and Republican congressmen are threatening to block such action if the Obama administration does not agree to deeper budget cuts.

Despite the overtly political motives behind S&P's announcement, the move points to the precarious fiscal and debt position of the United States. The government has been driven ever deeper into debt by a decade of tax cuts for the rich, the ongoing wars in Iraq and Afghanistan and soaring military budgets, a multitrillion-dollar bank bailout, and the impact of the deepest recession since the 1930s on tax revenues.

Between 2000 and 2010, individual income tax revenues fell by 30 percent, while corporate income tax revenues fell by 27 percent, according to an analysis by David Cay Johnston of Tax.com. The figures represent a combination of tax cuts and the disastrous impact of the loss of 7.2 million jobs since the start of the economic downturn in 2007.

In its press release, Standard and Poor's observed: "In 2003-2008, the US's general (total) government deficit fluctuated between 2 percent and 5 percent of GDP. Already noticeably larger than that of most 'AAA' rated sovereigns, it ballooned to more than 11 percent in 2009 and has yet to recover."

The US federal deficit is $1.3 trillion, about 9 percent of yearly output. The total federal debt is $13.5 trillion, or about 90 percent of US gross domestic product.

That Standard & Poor's and Moody's are far from impartial and incorruptible agencies has been amply demonstrated by the Wall Street crash of 2008, which ushered in current crisis. Last week, the Senate Permanent Subcommittee on Investigations issued a report that pointed to the culpability of the two ratings firms in the orgy of speculation and swindling that led to the financial debacle, noting: "It was not in the short-term economic interest of either Moody's or S&P, however, to provide accurate credit ratings for high-risk RMBS (residential mortgage-backed securities) and CDO (collateralized debt obligations) securities, because doing so would have hurt their own revenues."