

Former Treasury official: The U.S. should spend like China

Nin-Hai Tseng

Dec 13, 2011

FORTUNE – Why is China’s economy booming while America seems to struggle?

Frank Newman, former deputy secretary of the U.S. Treasury, argues in a new book that America’s government isn’t spending enough, and that’s largely what’s holding its economy back. It’s a bold statement that even Newman acknowledges, as the soaring debts and deficits in the Western world continue to unnerve investors across the globe.

Newman, who recently completed five years as chairman and CEO of China-based Shenzhen Development Bank, says government spending and deficits aren’t anything to fear. He points to China, which in late 2008 embarked on a two-year, \$586 billion spending program to try to stave off a recession and keep the Chinese economy growing. But while China trumped its spend and build motto, President Obama’s latest stimulus plan focused more on tax cuts and aid to states.

Admittedly, Newman’s book, *Six Myths that Hold Back America: And what America can learn from the growth of China’s economy*, might come off as somewhat overly simplistic given the vast differences between the economies of China and the U.S. And while he joins many others urging increased spending on America’s infrastructure, Newman sets himself apart by testing the popular perception that excessive sovereign debt is irresponsible.

We caught up with him recently to talk about his book. Below is an edited transcript of the interview.

Why do you think the U.S. shouldn’t worry so much about deficits?

With 14 million people unemployed, deficits aren’t a bad thing – they’re an essential and critical tool for government to boost the economy. Those who worry about America’s debt simply do not understand the nature of Treasury securities. It’s not debt the way personal debt is or even the way corporate debt is.

There’s no safer place to invest than U.S. Treasuries. Suppose you are a wealthy investor with \$10 million. If you leave it in the bank, you’re probably not going to get any interest. And it’s insured only up to \$250,000. But if you put your money in Treasuries, they have the full faith and credit of the U.S. government.

But if our debt levels get out of control, wouldn’t that worry investors and slow U.S. growth?

You hear that you can't have more than 70% debt to GDP or your economy will run into big trouble. That may be true for Europe, but perhaps not for other countries. The U.S. has been over 100% before; Great Britain has been 150% to 200% and has done fine; Japan is over 200%. Even though Japan had this lost decade, in 2010, before the tsunami struck, Japan had no inflation with only 5% unemployment and over 3% GDP growth. The U.S. and Europe would have died to have such good numbers. And Japanese government bonds sold like crazy.

And it's a myth that America's debt is going to be a great burden to our children and grandchildren who may have to repay it. The truth is it never gets paid back. In over 200 years American history, we've almost always had debt. It keeps going up.

In your book, you suggest the U.S. should spend like China spends on infrastructure to boost its economy. But some say China's economy is growing too fast and could be in for a hard landing. Would you still say China is the right model to follow?

Every year there are skeptics who say China is going to hit a brick wall. But for 20 years in a row, GDP has grown over 7% a year. The contrast recently is particularly striking.

If you look at the third quarter figures that just came out for the U.S., in real terms, GDP in the U.S. is just barely above where it was prior to the crisis during the third quarter of 2007. It's only one half of one percent greater. During that same period, China's GDP is up 40%. It's just staggering. There's got to be something that we in America can learn from how China has been addressing its economic issues because this difference is too striking to ignore.

If the U.S. doesn't work to reduce its debt, couldn't we end up like debt-troubled Europe?

No. The problem is that Europe has a central bank for the entire 17-nation eurozone. Suppose a Greek bond matures in Greece. Investors get paid in euros. They don't have to put that money back in Greece. They can put it in Germany or the other countries in the eurozone. In the U.S., that's not possible. It has to go back into the U.S. financial system. In the U.K., pounds have to go back into the U.K. financial system. And in China they have to go back into the Chinese system. Europe is a totally different situation, and it's a fundamental issue that a lot of smart people in Europe haven't grasped yet.

So U.S. debt can grow and grow and it shouldn't be a problem. That's a bold statement, isn't it?

It's a bold statement but it's true – logically.

<http://fortune.com/2011/12/13/former-treasury-official-the-u-s-should-spend-like-china/>