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REACHING THE LIMIT:
ENDING THE CYCLE OF DEBT CEILING SHOWDOWNS

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P R O C E E D I N G S

MR. HASKINS: (in progress) -- thanks to everybody that we ought to do something about the debt. And as you can see, we've been extremely successful in getting the Federal debt way down. So we are --

MR. HOLTZ-EAKIN: If the deficit is going the right way?

MR. HASKINS: The deficit, yes, but --

MR. HOLTZ-EAKIN: They've got to take credit for something.

MR. HASKINS: I know, but it's still higher than it's almost ever been except for the last couple years, but -- So, we should have called this event. Here we are again, the debt ceiling has been increased something like 100 times, actually more than 100, and 18 times just during the Reagan Administration. And in recent years it has been the cause of great sound and fury, including playing a major role in the 17-day Government Shutdown in 2013. So for the two people out there who understand less about the debt ceiling than I do, let me just summarize our current situation.

The basic idea is that Treasury needs to borrow money on a continuing basis, because what a shock, we have less revenue than we do spending. So, to pay the bills you have to borrow money, but Congress, wanting two bites of the apple, they originally voted on all the spending, CBO told them what impact it was going to have, and yet they control the debt limit. They tell Treasury, go and borrow up to a certain amount, and as I say, we've had to increase that amount, many, many times; over 100 times.

So our current situation is a little bit unique, because the last time around, in February of last year, the Congress voted to suspend the debt limit, not to increase it. I supposed there might have been political motivation there; that they could tell their constituents that they did not vote for a debt increase, they suspended the debt.

So we really, at this moment, have no debt limit at all, but in that original legislation, the debt limit comes back into force on March 15th, and the debt will be on March 15th, however much we owe to ourselves, to the government agencies, and to the public. And CBO says, that's about $18 trillion, so that will be the limit on March 15th. Then on March 16th, which is next Monday, we will be over the debt limit, unless we actually raise the debt limit, which there is no prospect we are going to do.

So, that means that we have to resort to this Treasury Extraordinary Measures, or whatever they call it, and they will have to do a bunch of tricky things. CBO says that can last until probably September, October, no one is certain of the date, and then they really would run out of ways to cover the debt, and then they would not be able to pay all the bills, so that would be -- that would certainly be a crisis. Some people think it's a crisis to be in the situation we are in now.

So, one last thing, the politics of this, Mitch McConnell said earlier this week, two important things. One, the Republicans were not going to allow the government to close because of the debt ceiling; and secondly, that it would -- I think he actually used the term months -- so there is no immediate prospect that there's going to be action on The Hill, or at least, that there may be someone on the Panel knows about it, and they'll tell us that there really is going to be.

So now the question is, what happens? And what happens now? What happens Monday? What happens over the next several months? And we could not have a better group of Panelists to talk about.

First, it's going Maya MacGuineas, who is the President of the Committee for a Responsible Federal Budget. Steve Bell, many years on The Hill, was often for a long period of time, twice I think, for multiple years, was a Staff Director to Senate Budget Committee. He is now the Principal in Steve Bell LLC. David Wessel, who, for many years was Economic Editor of *The Walls Street* Journal, and now directs the Hutchins Center on Fiscal and Monetary Policy. And then finally, Doug Holtz-Eakin, a Former Head of the CBO, and now the President of American Action Forum.

Here are our rules. They each are going to talk for 10 minutes, then I will ask them a couple softball questions, and then it will be your turn, and you can ask them really tough -- you can play, stump the Panel if you like. And then after that's over, we'll all go home and feeling like we really know all about the debt ceiling. So, we begin with Maya.

MS. MACGUINEAS: Great. Thank you, Ron. Good morning, everybody. I want to join Ron in welcoming everybody to the event. I'm also going to put on just a quick disclaimer on my own comments, which may not be very articulate, because I just spent my first night in a new house, and this is how my morning went. It was not a good morning where, I showered and flooded the bathroom and realized I had no towels, I had packed the towels, no towels.

SPEAKER: (Inaudible) around quickly.

MS. MACGUINEAS: Yeah. Right -- Well, and I had to figure out what to do with the flood, so that was like, all the clothes. Then I locked myself out of the house because I went to get the newspapers, and then remember; oh, I forgot to get the newspapers changed, so there weren't any, and I was locked out. And all I could find for breakfast, I kid you not, this morning was a bologna sandwich. So, I just feel like I've not started my day well, so luckily we have a phenomenal panel of people.

MR. HOLTZ-EAKIN: It's Friday the 13^{th}, and we are talking about (inaudible) -- what did you expect?

MS. MACGUINEAS: Right. Yeah.

MR. WESSEL: Is this also supposed to be a metaphor for Congress, Maya?

MS. MACGUINEAS: You may be right. So maybe that's appropriate.

MR. HASKINS: We don't know yet, but the audience supposedly, are not going to be serving bologna (inaudible), as I can probably assure you.

MS. MACGUINEAS: Yeah. Bologna sandwich and tea; so anyhow luckily we have a really good Panel, and we just thought it would be a great chance to sort of talk about the debt ceiling, because clearly it's played different roles, and more recently become a big issue. So, I'm just going to just tee off.

We have a new paper that just came out, that I assume is somewhere here, available for people, Improving The Debt Limit, and I'll go over a little bit about what's in that paper as my comments to kick off our discussion. But obviously, the debt ceiling has led to tremendous damaging brinkmanship in the past recent years. But before that we shouldn't forget that it also has been used really productively, to help us at various times to move forward as we've had to face and think about fiscal issues in the country.

And so just to think about a couple of those, it was increased and used as part of Gramm-Rudman-Hollings, twice. Twice, I believe? In 1997 it was part of the line-item veto, it was in 2010, part of increase of -- putting back statutory PAYGO, and creating an Executive Commission for what was the Simpson-Bowles Commission; and then most recently it was part of the BCA. And it was also an increase, as part of all the major budget deals in 1990, '93 and '97.

So, while recently our experience with it has obviously been, and it's led to turmoil and threats, it's also been part of pushing us in positive directions in the past. That said, it's obvious that that debt ceiling, in its current form, is fraught with problems, and it's not just the brinksmanship. There are a couple of things, that when you think about the debt ceiling, don't make a lot of sense.

Clearly it's not linked to any spending or tax decisions, and it's not linked to any objectives, any fiscal goals. At the same time that it's not connected to them, it doesn't do anything to restrict them. So there's nothing about the debt ceiling, while it limits your debt, it doesn't limit how you tax, how you spend, or whether you've achieved a fiscal goal or not. So it's really inconsistent with what one would think you wanted to do.

It focuses on the past, it focuses on the decisions that you've made, instead of the decisions that you are about to make. It's not as economically meaningful as it can be, could be, because of how we've constructed it. And finally, as we've seen, it creates these moments of brinksmanship, which have gone too far and at real economic cost in recent years.

So we need to reform the debt ceiling, is the conclusion that we've come up with. I think there are a numbers of ways to do that, and think about that, so the principles that we tried to do, as we came out with a bunch of options are; that you want to really have a balance between the fact that is still one of the only speed bumps, one of the only things that's out there, that helps focus on fiscal responsibility. So you'll want to keep something that does that, while you are also minimizing the risks of brinksmanship and, clearly, default.

You want to use the debt ceiling, or some kind of restriction, to actually encourage the changes that would be good for the fiscal health of the country. You want to create a more orderly process than what we currently have. You'll want to link it to decision-making, and you'll want to think about the future liabilities. You'll want to control where we are headed.

So, let me just talk about four of the recommendations and there are -- sort of, different variations of each one of them that we put out. The first one is thinking about the McConnell Rule which, what this allowed to do, is it gave the President more power to lift the debt ceiling on his own. He can now do it with only one-third of the Senate plus one. And we have a couple of variations that we might think about that.

So, we talk about whether the President could lift the debt ceiling if the debt met certain fiscal targets. So, if the debt is on track, as you'd want it to be, then you would have the President authority to go ahead and lift it. Another option, this is modeled off of something we've seen in New Zealand, would be that the President could lift the debt ceiling while in conjunction, putting forward a plan to get control of the debt.

I think that's the kind of thing you'll want to think about, so how you automatically link increasing the debt ceiling with talking about changes, putting changes in place that would get the debt back on pace of where you want it to go.

Then you could also do it, and it wouldn't have to just be the President, there's another option where you could have the debt ceiling increase automatically, if you were meeting certain fiscal targets. So, if you are on track, the debt ceiling increases automatically. If not, you have to go back either to the President or Congress to get the authority to do so.

The second option is different variations of the Gephardt Rule. The Gephardt Rule had the debt ceiling increased as part of the budget process, since this is when you are actually making the decisions that affect the debt. So the different ways to do this; you could, as part of the Budget Resolution, have a separate vote on the debt ceiling. This would like the debt ceiling to what you are putting in place with the budget, and it would sort of -- it would create, I think, the incentive to have a more responsible Budget Resolution.

The accountability for those people who have supported the Budget Resolution, of showing what it does to the debt ceiling, and stability, because you would know when you are passing the budget that the debt ceiling was also being increased. Other options are to make it more common, that you use reconciliation as the process that actually requires the debt to be increased by the same amount as what your budget resolution is doing.

Oh. And then there's a third option; which would be not necessarily as part of the Budget Resolution, but anytime that there is legislation that has significant costs, that you'd also have a separate debt ceiling vote that was part of it. So, basically this says; when you are making the decisions that are going to increase the debt, that’s when you have to approve the debt ceiling, not when you actually hit the debt ceiling. It does a lot more to link accountability.

Third, making the debt ceiling more economically meaningful, it is odd that the debt ceiling is capping gross debt. Generally, from an economic perspective, debt held by the public are the debt that we borrow in the open market that’s considered to be more economically meaningful, so you might want to switch to that. Even more so, one that I think makes a lot of sense, is having the debt ceiling be on, debt as a share of the economy. This is really the most important, kind of meaningful fiscal metric that there is, what the debt is as a share of the economy.

So we should be limiting that, because what can happen right now is that your nominal debt could be increasing, whereas going down as a share -- it's going down as a share of the economy at the same time, so you are on track from and economic perspective, and you are still hitting up against the debt ceiling. That’s not as helpful for making sure that it's actually a useful metric. So changing what it's limiting is one possibility.

And then finally, do we want to use the debt ceiling to limit unfunded liabilities or the promises in the future? There are a lot of benefits of this, there's some things troubling, which is the calculations of unfunded liabilities are very challenging to do, they are very whimsical based on the assumptions that you are using, but if you can find the best ways to limit the promises that you are making in the future.

One of the things that this would do, is it would mean that, if you made some of the long-term term changes; take entitlement changes, for instance, right now there are not a lot of parts of the budget process where you get credit for doing that, where you make changes that the savings show up in the future, but if you had a debt ceiling that were limiting those kinds of promises that you put out there, there would actually be more incentives for policymakers to make some of the long-term changes that are important.

So, I'll just close there, saying, the clearest, most obvious goal here is, we can't have a country that even talks about defaulting. It's been incredibly dangerous that we've used the brinksmanship and gone as far as we have. It's always been used by all parties, it's always been the majority who falls for it -- with the responsibility of lifting the debt ceiling.

There have been lots of heartfelt speeches around lifting it, about how responsible we should be, and we are not being by the same people who are taking the votes that were increasing the debt in the first place. We can't let it go as far as it's gone. And it's kind of, the genie is out of the bottle, it's very hard to go back to where we knew we would lift it, but we would still, hopefully, attach some smart things and allow these speeches and focus on the debt for a minute. We have to really take precautions against letting what's happened in the past happen going forward.

But I would advise against the notion of walking away completely from one of the only restrictions that we have on pushing us towards more fiscally-responsible decisions without replacing it with something else. So hopefully this list of options is something for policymakers to think about, and for us to discuss and start off the discussion with a bunch of different ideas.

Thanks.

MR. HASKINS: Steve?

MR. BELL: First, thanks to Maya; and to Ron, for putting this on. Also thanks to Sur Irving and her group at the GAO for all the work they've done over the last three years on the economic impact of these impasses.

I'm going to be a little bit boring, instead of a lot boring, which is how I normally am. Because I'm going to be -- I have kind of -- more of a market, point of view, than perhaps others do. We have lowered deficits but our statutory debt limit is going up. Compare the interest rate forecast that CBO put together, back in 2010, debt service costs have declined by $3.2 trillion from those forecasts. And we all know why; QE1, QE2, QE3, and now the demand from overseas nations because of the strong dollar, to own our debt, and to get paid in dollars, not in local currencies.

This not a criticism of CBO, they assumed that we would go back on the 10-year note from very low numbers, as most of you know, we've been somewhere between 22 and 15 the last 18 months. The average since World War II, is about 5. CBO made the rational assumption that we would have 3.9 in 2011, and 4.9 in FY '14; and my recommendation to all of you, is if we do get to 4.9 on a 10-year, please buy it.

Two people that I know a little bit; I used to work for Warren Buffett, who used to say that, the best way to go bankrupt was to try to predict interest rates. Mr. Buffett, two years ago, attempted to predict interest rates, and he has written n his recent letter that his notion of a strong dollar -- of a weakening dollar was probably a little off-base.

And Bill Gross who lost his job at PIMCO because he said, at the beginning of January last year; whatever you do, don't buy the 10-year. The 10-year went up about 40 percent in value, while he said that. And so he's now at a different place. Health care cost declined, and we don't know whether they'll continue to decline, but they certainly are less than what we had forecast they would be five or six years ago.

Lower interest cost, lower health care cost compared to what we thought. Why are we then on our way towards -- I'm going to use the statutory debt limit because I'm a creature of the Senate, and that's what my boss used to have to vote on. Why are we on our way to $20 trillion in the statutory debt limit three years earlier than CBO had forecast just five or six years ago? What is happening inside of this budget?

11,000 people -- its 11,000 people a day we know signed up for Medicare, and in a little while it's going to be 12,000 people day. And then all of a sudden we are going to have a real nice time, and it's going to be 15,000 people a day. I don't have any solution for that problem, and I can tell you that we at Bipartisan Policy Center don't either.

Could you do this; could you do this if you were any other country in the world? The answer is no. We have the reserve currency, there's a book out called *Extraordinary Privilege*, by [inaudible), which I recommend that you read. That phrase comes from a French Foreign Minister, who, very, very angrily, after Bretton Woods, and the dollar became the -- essentially the reserve currency of the world; who said, that really is bad. That is an extraordinary privilege.

And so it's turned out to be. Most transactions now are in dollars. That means that we can just keep printing. We don't have to do what Sweden did in the 1990s, which is an act of, I think, tremendous courage what they did. But at the same time, I will describe to you what I -- the way I kind of look at the situation, it's a balance sheet situation. If I describe to you a company whose indebtedness was increasing more rapidly than its productivity, whose basic production -- let me call that CAP EX, capital and expenditures just for the sake, it's a kind of a crude approximation; who was declining, and had been declining for the last decade, and which had substantially underfunded health and pension benefits. You would not buy that company.

For example, we used to joke about GM. GM is a company, we said -- before the great recession -- that provides health and pension benefits to a large number of people, and administer to that, and every so often, makes a car. That was not as much of joke when the great recession hit, as it was before then. But that really is where the United States is right now, if you were looking at it on a cash flow basis, and whether you wanted to buy it as a stock.

Our CAP EX is down substantially. Whether it's health research, education research, the basic things we think about like infrastructure. Those things are declining. At the same time, future benefits, in the form of pensions and health care costs, are increasing. And despite the good news on higher revenues than we anticipated, lower interest rates than we anticipated, health care cost slower -- it's more slowly increasing than we anticipated, we still are increasing, inexorably, the debt we owe.

That is a difficult situation because it's fundamental. Again, we are very lucky we had the reserve currency. In my lifetime China will probably not have the reserve currency, although they are attempting have a couple of deals with Brazil and others, where they can bypass dollar exchange.

Great Britain in 1914, the pound, was the reserve currency of the world, and you had a bunch of old guys sitting around at Whites, which is a club in London; talking about how the Raj had collapsed and things were going to hell in a hand basket, and people made fun of him.

Thirty-five years later the pound sterling was no long the reserve currency of the world. There is no commitment from Lords, that the United States forever will be able to be either the reserve currency, or that we will be able to avoid, at some point, the results of a fiscal fallacy -- pardon me -- fiscal folly.

And I want to conclude by saying, because I -- because they want me to, it's my job; we have this really, really typical BPC thing, that we are putting out this morning because we've got to compete with you, but this is a debt limit analysis. There are no recommendations in it, it just repeats what people in this room know, and almost nobody in Des Moines and Iowa knows.

So, if you go to our website, we've got lots of numbers in it of course, and lots of the kind of analysis I just gave you; but I want to conclude by saying, I'm pretty pessimistic about getting the kind of agreement that we all, here, have pushed for over the last five or six years; whether it was Simpson-Bowles, whether it was Domenici-Rivlin, whether it must be agreements trying to be reached on The Hill by others.

And frankly, I think the fact that the Republicans control both the Senate and the House, and I am a Republican, makes things harder, but certainly doesn't make things easier. Because the splits within that party will be highlighted now, I think, more dramatically than ever, as we try to get a budget reconciliation package -- budget and reconciliation package out that leads to a balance in 10 years.

I will just say, we tried it; my friend, Bill Hoagland, and I who have been together since '81; have tried to put together without new revenues, a balanced budget in 10 years. We would have to do what Sweden did, that is to cut present beneficiaries' money. So if you've got $1,000 a month, sorry you are down to 900. Something in me, after 11 Federal campaigns that they have been, tells me that's not going to happen.

So on that up upbeat note, I'll stop. I will not try tell you -- sell you the stock, and only can close by saying there are three companies in America that are Triple AAA-rated, under Standard & Poor's, the United States Government is AA-plus.

MR. HASKINS: Dave Wessel, (inaudible); with us.

MR. WESSEL: I'm depressed that we are having a Panel on the debt ceiling. I think it's a distraction from real issues, it's a shame that people at the Bipartisan Policy Center are running spreadsheets to figure out whether we'll run out of cash in the third quarter or the fourth quarter. And it's a shame that people in Maya's shop are trying to tweak something which has become a symptom of dysfunction in Washington.

You know, it's worth to remember a little bit of history. The debt ceiling was -- and originally there wasn't a debt ceiling, Congress approved every debt issue. It was during World War I when that got to be a bit of hassle that Congress, in order to make life easier for itself and give the Treasury more flexibility, said we won't make you come to us with every debt issue, we'll have just an overall cap.

And over time this gave -- the Treasury got more and more leeway, it evolved from a limit on debt issuance to a limit on the total bonds in the 1930s and it was kind of raised without controversy periodically although if you go on YouTube there's this absolutely fantastic, Everett Dirk's on TV Spot, where he talks about raising the debt limit, and how -- and this was not a politician made for TV, so it's definitely worth watching.

But it was Dwight Eisenhower, in 1953, who first ran into trouble, he was doing a lot of borrowing to fund the Interstate Highway System, and a Republican Congress refused to raise the debt ceiling. And then he ran into Harry Byrd, the Democrat from Virginia, who thought we had too much debt, and he tried to use the debt ceiling as a lever to cut spending. It went on for about a year. Eisenhower won, although he didn’t get as much of a debt ceiling at the time as he had sought.

And he said when signed the new debt limit, "An essential part of this preparedness for national security --" that was an excuse for the highway system, "-- is a debt limit high enough to permit the Treasury, if necessary, to borrow the funds required to carry out the government's obligations under the constitutions and the laws of Congress." It seems like a kind of reasonable position. Half the people in Congress would probably vote no, if that was a joint resolution.

The reason I say it's a symptom of dysfunction in Washington, is that there are a lot of things in the fiscal process that have broken down. For a number of years there hasn’t been a budget resolution, appropriation bills, the 13 appropriation bills, the so-called regular order are -- it's the exception when they do all those, confirmation of presidential appointees from the Senate are backing up.

So, I think that it's part of a bigger piece. Maya is absolutely, I mean it's nuts. Congress has already approved the taxes and spending that lead to the debt. It's like you buy all the stuff on your credit card, and then the bill comes and you say, well, I don’t want to pay for it. It's completely irrational.

And now, it's true that, as Maya points out, that in the past the fact that you had this must-pass piece of legislation, sometimes led to other legislation being attached to it, for better or worse, and that long list of things she said were attached to it, I think you'd get a good argument about whether they accomplished anything.

You've got -- in order to get the debt limit passed; you've got an Executive Committee on the deficit that doesn't do anything. You've got the Budget Control Act, and we've got the Sequester, so whether those were the net plus, I think is open question, but I think what's happened is, that attaching things to must-pass legislation made a lot of sense when Congress would pass must-pass legislation.

And what's changed now is, people seem to take -- it's an open question whether we really have to pass this, and this leads to an incredible amount of wasted time, as we figure out; so, if we hit the debt ceiling will the Treasure pay the bonds first? Is that legal? All of which have nothing to do with making America a better country.

We have to raise the debt ceiling as long as we have a deficit. And as Maya pointed out at the Senate the other day, if Congress wanted to reduce the deficit to zero over 10 years, which some of them say, that's $5.5 trillion in savings, eight times the size of the fiscal cliff deal, and they are not going to do that. I mean, the latest reports from David Rogers are, they are not even going to try and balance the budget in the next 10 years, which may be reasonable, but it's not reasonable to take that position, and not lift the debt ceiling.

This business of not passing it has real cost. As Susan Irving's group, and the GAO has calculated that 2011, 2012 fiascos consume 5,750 hours of work, as they try to figure out what they would do in the administration if we hit the debt ceiling, and she estimated that they -- or their team estimated that the perturbations in the bond market cost the government somewhere between 1 billion and $1.7 billion, just because of the debt ceiling fiasco.

Now, that's real money although in Washington it's not very much. I think that the other thing that this is as -- it's about the cause and -- it's a cause for further problem in Washington, which is simply the erosion of public trust in the government which is really important because if people don't trust the government they are never going to do the things that most of us think will have to be done to put the debt on a sustainable course.

At the time of Watergate, half the people in America said they trusted the government to do the right thing, most or all the time. That was Watergate. Today it's one in five if you've used the Gallup Poll; one of four if you use the Pew Poll. If you ask people, do you have trust in Congress? And they give these scales. You know, do you have some or a great deal of trust in Congress?

The Military people say they have -- 74 percent of the people say they have trust in the Military, 45 percent say they have trust in churches, 26 percent say they have trust in banks, 22 percent say they have trust in newspapers; Congress, 7 percent of the people, right. I always love these polls because it makes reporters feel better like, as bad as things are for the press, Congress is always worse.

So, I think the thing that I wish we could talk about, and we will, and Steve took us down that path is, if you are worried about the debt, what should you be thinking about? And what you should be thinking about is, as Maya said, the ratio of the national debt, that held by the public to the gross domestic product. And we should be talking about, what can we do to reduce the numerator, the debt, and increase the GDP?

And nothing that comes up in the debt ceiling conversations does any of that. The Federal debt remains on an unsustainable course, even though spending on everything outside the Social Security and health programs is on track to reach the smallest share of GDP since the 1940s, according to CBO. That is social security and health programs are such a big part of the budget now; that they are crowding out other things.

Larry Summers observed, and I thought he was exaggerating, so I checked the numbers, and unfortunately for me I didn't get to do a gotcha with Larry Summers, he was right. That net Federal investment; that is Federal investment spending minus depreciation, or wear and tear on what they are buying is approximately zero, as a share of GDP.

You can think of lots of things that might increase the GDP a little bit, growth, you can pick them. It could be tax reform, it could be investment and infrastructure, it could be changing Obama Care, it could be changing Dodd-Frank, but the debt ceiling debate diverts attention from the things that would really make America better, and that's just really a tragedy.

MR. HASKINS: Doug Holtz-Eakin.

MR. WESSEL: So you are the optimist, Doug.

MR. HOLTZ-EAKIN: Okay. Well, clearly from first principles point of view, the debt is the problem, not the debt ceiling. And I won't repeat the key facts about the trajectory which is bad, the fact that the composition of the spending which is driving the large debt is crowding out the future at the expense of these legacy entitlement programs.

You know, the key fact is that in most of the projections, the deficit is interest for all practical purposes, that we are borrowing to pay interest on previous borrowing, and that's a completely dangerous position to be in, and we survive in these circumstances, only by the virtue that we are the best-looking horse in this glue factory, the rest of the world is worse. That's it.

And that's how we maintain the status of reserve currency, that the interesting economic consequence of these debt ceiling battles is it endangers that rope which has been given to us by the whole financial system, because if you impair the liquidity of treasuries, by failing to meet obligations to pay in a timely fashion, the use of the dollar as reserve currency, is no longer very attractive, and I think -- you have to be able to transact in these things.

And so that's the economic, real economic consequence of tiptoeing up to these fights all the time. So, you know, put aside the economics for now, and just think about the politics of this. You know, everyone has a different recollection, but one of the things that I guess I'd emphasize is, it is more than norm, than the exception, that debt ceiling increases are accompanied by some requirement to do something. Whether it's a commission or genuinely some legislation that changes spending or raises taxes or, you know, it deals with the underlying budget as well as raises the debt limit.

So the nothing that somehow it's brinksmanship to do this in recent times, I think is not correct. That is pretty much what happens, they are embarrassed that they have to raise the debt limit, they attach something that says; honest, we are going to deal with this, and that's the thing that typically, it goes through.

What I think is different in the current environment is that the inside baseball playbook for getting the debt limit increased has changed. It used to be that the House had this thing called the Gephardt Rule, if they passed the Budget Resolution, it was deemed to have automatically raised the debt limit, so they never actually took a vote to raise the debt limit. No fingerprints at all over in the House.

Over in the Senate, the Gentleman's Club had an agreement, if you were up for reelection you voted no, if weren't up, you voted, yes. It went to the President, everyone hold their noses, they signed, done. And there was a roadmap, that roadmap is gone. The House decided when the Republicans took over in 2010 they were going to vote on every fiscal thing, they weren't going to use the Gephardt Rule. So now, you've got a House or Representatives that's going to vote on this, and so there are going to be fingerprints, it makes it way, way harder.

On top of that, if you count, which is a good thing to do on Friday the 13th, go to the Republicans in the House, and count the number who have made a pledge in their election to their constituency that they will never raise the debt limit. And you will find out that you cannot get to 218 votes with Republicans alone. There is no way John Boehner can put together anything, a debt limit increase plus, you know, close every agency in the Federal Government, that won't pass with Republican votes. So it's always going to be an extremely messy situation in the house, no matter what.

If you go over to the Senate, that the Gentleman's Club is gone, right, and the Senate is increasingly looking like the house, and they don't know how to get there either. So I think the fact that this is a tough political vote, has not changed, it's always been a bad vote to raise the debt ceiling, no one likes it, what has changed is the mechanics of getting it through and getting it to the President for signature; and that really does complicate things tremendously.

If you look at the list of things that -- and I haven't read your paper, I don't know why, and I wasn't even locked out of my house, but at least, I haven't tried to go home yet, but anyway, but most of the things that you hear in those recommendations, it's let's try to insulate raising the debt limit from the politics, and I think that just won't work, right. In the end, this is a democracy, and if people don't like what's going on, they are going to demand a say in it. So I am a little bit skeptical of that route going forward.

The other thing, you know, dealing with debt relative to GDP, has a difficult politics at the other end. The American public cares a lot about simple measures of fiscal health, and if you look around the globe, fiscal rules, you know, hard balanced budget requirements, things like that have been effective, and Maya's group has done some great work on this.

But they have to be simple and understandable to the public. And in this environment the key thing to remember is, if you poll on budget issues, the number one thing people care about, is that it balances, and if you can say, my budget balances, people like it, it doesn't matter what's inside of it, and if it doesn't they don't like it.

And that's the appeal of these 10-year balance things, it's all -- it's the ability to go back to the public. And so the public is not going to understand the debt to GDP ratio, they are not, they are going to think that you are gaming the GDP forecast, because, you know, if I was the Chief Economist, I would. And, you know, that leads to a real difficulty in going to those kinds of more subtle measures.

Now, let me close with the optimism. And I am genuinely optimistic about this. We are about to see the whole dynamic change, right, because the debt debate is going to be different going forward than going back. If you are running for President in 2016, and nearly everyone is, I mean when you are running, I mean, you know, your advisors are going to be able to look at the CBO forecast, and say, you know, this is what it looks like and, by the way, if you want to be governing in 2024 when, you know, we really get to the point where the interest is practically the whole deficit. So if you are running in '16, you want to govern in 2024, and on your watch, it's all going to fall apart.

That's not a very appealing thing. Now, one thing to do is get elected, and then surprise plan to completely change the social safety net, that's not going to be very popular. You cannot surprise people with a huge change in everything at the Federal entitlements. So we are going to have to see candidates acknowledging the problem. I don't expect big, dramatic, you know, precise plans in 2016, but the presidentials are going to have to say things like, hmm-hmm, we've got a problem, you know, we've got to sit down as a group and sort of work on this.

It will be more visible in 2020, but it will -- you can start seeing the arithmetic in 2016 adding up. What that says is we are going to start to have some presidential air cover for doing things in this area. We haven't had any presidential air cover for a long time, and the Congress can't do without the White House's help, but it then gets some air cover from the White House, I think the dynamics of doing some stuff together will be very, very different.

It's also going to start from the bottom up, right? As everyone has pointed out, the defense discretionary and non-defense discretionary accounts are getting crushed by the spending and the rest. We are already seeing the cry of this million payment, particularly out of the Defense Department this year who have talked -- you know, all four of the leaders of the Service Branches have said, America's safety is at risk with these numbers, we need more money, and so that's a bottom-up pressure to get entitlement reforms.

We finally are going to have some people who are favor of the entitlement reforms. Historically, the only people in favor are the geeks, right. Would say, oh, you ought to do that. And everyone goes, no, are you nuts.

Now we are going to have people saying, we need to do this, there's also going to be the non-defense discretionary folks, there is actually in this town, the coalition, the non-defense discretionary coalition, the single worse named coalition in Washington, I've spoken to them. And they are actively putting together a campaign to lobby for entitlement reform.

That's the heart of this problem. And so from the bottom, the retail politics are going to be different. They are going to be votes for. And from the top I think you are going to start to see increasing air cover, and so we'll see a difference in the politics of this going forward than we had in the past. It's not going to change overnight, but the pressures are there, and with the pressures come new politics.

And, you know, since something has to change, we can't continue along this trajectory, the question has always been, what will give? And I think the politics are about to realign for that reason. That's the optimism.

MR. HASKINS: Well, thank you. A lot to think about, so let's think about a couple of things; first what I want to do is something very quickly. McConnell says, no matter what, Republicans are not going to allow the government to close. Is that correct? Are you completely confident that the government will not close as a result of this fiasco?

MR. HOLTZ-EAKIN: Yes.

MR. HASKINS: You are?

MR. HOLTZ-EAKIN: I am.

MR. HASKINS: Does anybody disagree with that?

MR. WESSEL: So does McConnell speak for the House?

MR. HOLTZ-EAKIN: No. But you just heard what --

MR. WESSEL: The Immigration Bill, is that --

MR. HOLTZ-EAKIN: But it's in close.

MR. WESSEL: Right. Exactly. That's your argument, that in the end they won't get to --

MR. HOLTZ-EAKIN: In the end -- in the end it will be --

MR. WESSEL: It will rely on the Democrats to win the vote?

MR. HOLTZ-EAKIN: Yeah. He doesn't have to '18.

MR. WESSEL: Right.

MR. HOLTZ-EAKIN: He's relying on the Democrats every -- you know, no matter what, on this issue. And so, you know, the only question is when they rip the band-aid off this, and we then take the vote.

MR. HASKINS: Okay. So question --

MS. MACGUINEAS: I just want to add one point.

MR. HASKINS: Oh, yeah. Go ahead.

MS. MACGUINEAS: I don't think it is going to close, but I want to clarify one thing, because last time when we had a debt ceiling and almost a government shutdown, a lot of people started thinking those were the same thing. And so a government shutdown comes from whether we fund the government, and a default comes from not lifting the debt ceiling. And I mean, I think Doug made this really good point, that simple rules were the only things that the public understands, and one of the challenges we have in all this, is that it's not always the public not understand this, how could they? It is so convoluted and so complicated, but just so that we don't continue that complication --

MR. HASKINS: Yeah, it sounds like it could have (inaudible).

MS. MACGUINEAS: -- default and government shutdown are different.

MR. HASKINS: Yeah. That was good. So Doug --

MR. BELL: I would add --

MR. HASKINS: Oh, go ahead.

MR. BELL: Let me just add one thing.

MR. HASKINS: Yeah.

MR. BELL: Fidelity has already admitted publicly how much money it cost them to prepare for the possible shutdown, I think since --

MR. WESSEL: Default, for the possible default, you mean, default?

MR. BELL: Yeah; the default because of the -- well, yeah, yeah. Citicorp probably spent more, they'll show it in their earnings now that they've passed the stress test, but probably more than a billion dollars was spent in the private sector preparing for a potential default on

American sovereign debt. Nobody sees that in the public record, but that's about what was spent on this.

And one last thing, in all the years that I've been watching markets, I have never seen what happened in July two years ago. And that is that, a major firm said that it would not accept, as collateral, any August-dated American sovereign debt as collateral; wouldn't accept it. That's extraordinary. And that I say it about Poland, no offense to Poland, but you would -- I've heard it said about the United States that I won't accept your collateral, United States sovereign debt because it's dated in August, and I don't know what the heck is going to happen in August. So this has really had in the past, damaged.

MR. HASKINS: Okay. So let's follow up a little bit on Doug's optimism. I notice that you did not mention revenue and taxes. I've been in this town a long time, and I don't see how you can get a big deal without tax increases as well, but I also don't see how a Republican -- I mean, the Republicans are talking about cutting taxes more. How can we get a deal without tax increases? And will a Republican House ever support a tax increase?

MR. HOLTZ-EAKIN: They may have to. I mean, let's face it, this is not about -- again, the foundation observation is, the current combination of policy and politics is unsustainable. So you cannot make the argument, that everything is going to be the same in the future (inaudible). It can't be.

So the question is, what gives and when? And I'm not smart enough to know when, I just don't, but we know what has to give. There has been a -- you know, a Mexican standoff for decades, where the Republicans say to the Democrats, we are not raising any taxes unless you guys get these entitlement programs under control. And the Democrats say to the Republicans, we are not touching our favorite entitlement programs until you raise taxes, especially on rich people. And you know, since basically, you know, 1990 they have stared at each other.

MR. HASKINS: Okay. But how do you respond if someone says to you --

MR. HOLTZ-EAKIN: And so that -- now that gave a little bit, right. The taxes went up on the fiscal cliff deal, with that -- with no entitlement reforms whatsoever.

MR. HASKINS: Yeah. Yeah.

MR. HOLTZ-EAKIN: And so if they are going to get more tax increases, there's going to have to be some entitlement reforms, and we know that's what we need, as communicated.

MR. HASKINS: But don't you think that your characterization of the Republican as saying, we are not going to increase taxes unless you reform entitlements, and vice versa for Democrats? That that's morphed into; we are not increasing taxes, period, they --

MR. HOLTZ-EAKIN: For some, for some, I know.

MR. HASKINS: You just talked about the number of folks in the House, who say they will never support a debt increase. And even more than that, signed a No-New-Taxes Pledge.

MR. HOLTZ-EAKIN: But we also have seen taxes go up, and we've seen the debt limit raised, and that means that some people are disappointed, that's how democracy works. There are going to be people say, no, I don't want to do that, and they are going to vote no, but that doesn't mean we'll never get a deal, and we are going to have to get one.

MR. HASKINS: So I have to pass it with lots of Democrats support, and violate their --

MR. HOLTZ-EAKIN: Or maybe two, who knows. I mean, this is not a 2015 or '16 vote we are taking.

MR. HASKINS: Right.

MR. HOLTZ-EAKIN: What will the world look like in 2018, more likely '22 when this has --

MR. HASKINS: So you are thinking another four, six, eight years?

MR. HOLTZ-EAKIN: You have to -- I mean this is not now, you know, if you want to look at what's going to happen now, write down the shortlist of things they have to do, and they are likely to do them, and rename some post offices, and (inaudible). (Laughter)

MR. HASKINS: Steve, you said -- Staying with this topic a minute. You said that it makes it more difficult to make progress on the debt ceiling and our underlying problem of debt, because Republicans control the House and the Senate. Will you say what you mean by that? And I'd like to hear the other Panelists reflect on it for a minute.

MR. BELL: The fault lines in the party, compared to when I first started in 1970 in the Republican -- a little Republican race in New Mexico, the fault lines now are clearer, and the distance between the two parties, if you want to call it, inside of one party, the distance of these factions is much greater.

I cannot tell you, and I think Alice and I have talked about this. When Alice was CBO Director, and I staggered into becoming the Staff Director of the Budget Committee, the one thing we never heard anybody say was; you know, we could default for a day or two, that's just a temporary default. If we had said that, she's much more respected than I am, so she'll probably keep her job. I would have been fired immediately.

We are now hearing people say that. We are hearing serious people, people who went to places like Harvard.

MS. MACGUINEAS: (Laughter) Just to name one of them, yeah.

MR. BELL: Just to name one, yeah; and who are Rhodes Scholars.

MR. HASKINS: Are we sure it's a serious place?

MR. BELL: Who are saying, oh, it doesn't make any difference. It's only a temporary default. They had actually no idea how financial markets work. Most of them don't know what a repo is, let alone anything else. So I believe you are going to have -- and let me use some names, because at my age I have no future anyway.

You are going to have Mike Lee and Ted Cruz, and people like that over here. And you are going to have a guy like Portman who understands these things very well, and Thune and people like that saying, you know, this cost benefit analysis is stupid. And you are going to have the Democrats saying; you know, you didn't give us a lot of help over the years, so why are you asking us to help you pass something you are scared to pass?

And that's a logical position. In the House, John Boehner, if he could get together with Steny Hoyer, would probably be able to have, as long as the President averted his eyes, a point that Doug made very well, is that presidential leadership when this happens, you could probably put together what's called Centaurus Coalition, I don't know what that looks like but -- I used to know what it looks like, I don't know what it looks like now.

But John Boehner is going to have to make deal after deal after deal with the majority of Democrats in the House. There's no way around it. And maybe at some point, we'll realize, as Republicans, that Jim DeMint was wrong. That it is not better to have 30 pure Republicans in the Senate in a minority, than having 51 Republicans in the Senate, some of whom, you know, may be Catholic instead of Methodist, or some other religion.

So I really believe the big story is going to be, can they get a budget resolution? Yeah, you can put a -- you can put a blueprint together by doing all sorts of games. I've been accused of that. Can you pass reconciliation instructions that make that blueprint a reality? And if you pass them, and you tell the Finance Committee to save $800 billion, without taxes, in programs under their control; do you think the majority of Republicans with 26 of them up, in 2016; that you could get even in private caucus majority?

If you do, talk to some senior Budget Committee staffers, and they'll tell you; in a private caucus, in the Senate, Republicans would not vote for the Ryan Plan of the first two years. That's why I think the split is going to become really the highlight. It's not Congress versus the President. It's not Republicans versus the President. It's Republicans against Republicans. In my opinion, that's an opinion.

MR. HASKINS: So Doug says -- We recognize that; so Doug says, something has got to happen. If Steve is right, it is hard to think of what it could be?

MR. HOLTZ-EAKIN: But it's not now.

MR. HASKINS: I'd like to hear --

MR. HOLTZ-EAKIN: It is not now.

MR. HASKINS: Okay. I understand that.

MR. HOLTZ-EAKIN: I mean there's no way --

MR. HASKINS: But I'd like to hear from the rest of the Panel, too. What do they think is going to happen in the long run that will extricate us from the situation?

MR. HOLTZ-EAKIN: So this is, I mean you know -- First of all, I don’t want to agree, I think that the over-hyping of what Republicans through the entire Congress has been a big problem. I mean, you know, I think I have people who can bear witness to the fact that I told my staff, like the day after the elections, the number one thing to do is to lower expectations, that’s just -- there is the notion that somehow the house and the senate are this well oiled, monolithic machine that was going to go do -- no way.

And the kinds of things that were even being in the senate were all wrong. Mitch McConnell was saying, we are going to send Bill after Bill to the President's desk, and he can either veto or sign them. And we are going to return to regular order. Those are completely contradictory, because regular order means you don’t get anything done.

And so, you know, from the beginning it's been destined to disappoint people, I think, because there was just too much -- too much hype on this stuff. And there are these fault lines, and there's no doubt about it, and they are comparably true on the democratic side, so it's a much more complicated situation than that.

We used to have the White House, Harry Reid, and Republicans in the House. Now we have the White House, Harry Reid and divisions in the Republicans in the House and the Senate. It's a very complicated landscape. It's a recipe to not do big things now, and so I don’t expect the budget resolutions to even attempt to do those big things, because they are -- people know that’s unrealistic.

I do think there's some potentially valuable learning that can go on. For example, we need more defense discretionary spending, pick a number, $50 billion. The political price for that, from the White House will be, we want 50 in non-discretionary spending; fine. Get reconciliation instructions to save $100 billion over 10 years in the mandatory programs.

That does exactly what we need to do to get the composition right. It's tiny but it gets the composition right. It uses reconciliation to send to the President a Bill that he needs and wants to sign. Off we go. That's tiny, and it will be painful, but we'll have to do it again next year. It will be tiny, it will be painful, but after you go through two painful years, and you get the new crowd in, in 2017, then you sort of say; okay, we are sick of this year-by-year pain, let's fix something. And that's the dynamic, I think, that has to play out.

MR. HASKINS: David?

MR. WESSEL: So, the longstanding question is, what will change things on this front. So I think that there are a couple of possibilities, one is the crisis. Could be a financial one, it could be a political one. Some Ross Perot-like figure rises up and shames the presidential candidates into saying something, or doing something.

And a second is leadership, which has been lacking. But I think that there's an underlying fundamental problem and this is one that Bill Galston, a Political Scientist here a Brookings, was talking about in a meeting we had yesterday, is that the institutional mechanisms for dealing with polarization are not working. That is that the distance -- the gap in Congress between left and right, and in the public between left and right, has grown.

And there was a Political Scientist from the University of Denver here yesterday, Peter Hanson, who has this nice little chart, it's a little hard to describe without a slide, but it basically shows the ideological difference in the Senate between the 51^{st} vote for something, and the 60^{th} vote that you need to get past the filibuster. And it was like this in '70s, and it's like this today.

And so, Galston says, there are really only two options he sees for resolving this. One is, gridlock, persistent until some crisis comes, and the other is some kind of change in the rules which allows more of the majority in the Senate to do things without the 60 votes needed.

So I share Steve's pessimism about anything happening in the near term. And frankly, in the near term there's not anything to force them to do anything. The deficit has come down. We are able to borrow at very low interest rates. The chances that Europe is going to get its act together and become the reserve currency of the world in the next 36 months, is less than zero, like interest rates in Europe are less than zero. (Laughter)

So there's no pressure on them to do it, and it's very difficult for them to do things that will -- that the benefits only get paid in the future. And the thing that makes you optimistic is that, every time we get to this point, something happens and they do something. I mean, Bill Clinton did not do the middle-class tax cut, he reduced the deficit when he became President. George W. Bush said he would never raise taxes, he did. He lost the election, but we were on a more sustainable fiscal course for a while.

So I share Steve's pessimism about the near term, and Doug's faith that if something has to give, something will give, it's just hard to know what and when.

MR. HASKINS: Maya? Just a (inaudible) forecast in several -- just being a transparent about your forecast.

MS. MACGUINEAS: Yeah. I think the framing and the structure that everybody has said is right. One, I think it's interesting when you think about markets that nobody in Washington understands markets. And then the opposite is also true, that markets don't understand Washington at all. The disconnect between those two is really pretty frightening.

But I think that this model is right, that it's either going to come from leadership or crisis, and the fact is, something is going to change, like Doug said, because it has to change. So, when I think about it, and we think a lot about, sort of, the strategy of how you help push along change. A couple of years ago, there was a real opportunity, based around Simpson-Bowles and Domenici Rivlin, there was a real chance that there was going to be a grand bargain.

And a grand bargain was desirable because it meant everything was done at once, everybody had to be a part of the solution, it won. It's really hard to go through these hard things, like the Sequester is fixed every year, you do something so hard, and then it turns out you actually haven't really fix the problem. So, one of the benefits of a grand bargaining in addition to that everybody is a part of it, is that you actually have the upside of having fixed something.

To go through these tough votes when you haven't fixed it is not appealing. So it made a lot of sense that it could have worked --

MR. HASKINS: That's why it's one in two, by the way, they need to learn that.

MS. MACGUINEAS: If they want -- you want them to go through with the hard thing, and wake up to headlines that you still face?

MR. HASKINS: Yeah.

MS. MACGUINEAS: And by the way, what you are saying is a sequester fix, as I understood it, is you are doing 10 years offsets for every one year of fix, right? So it's not --

MR. HOLTZ-EAKIN: It's the only way to get it (inaudible).

MS. MACGUINEAS: Maybe it is the only way, but it's not even very hard.

MR. HOLTZ-EAKIN: I know.

MS. MACGUINEAS: They still don't even understand what the real cost of something is, because it's so much easier. But it's now clear, that only is the grand bargaining not going to happen on the debt. The debt, I think is one of the hardest challenges we have policy-wise, and realistically, if you look at what's happened in the past years, we can't get anything done. We can't get anything done in Washington. And I think that has become the biggest symbol for a broken government.

But so the question is, what steps do you take along the way that bring us to being more ready to make the changes when the timing starts to push us again, or the structure does. And it's why I think I disagree with Dave a little, about some of the things that have been attached to the debt ceiling in the past weren't helpful. I think they were, because I think the moments -- I think having these big commissions was incredible helpful. I think PAYGO was helpful. I think the various processes which didn't fix the problem, but it focused on the issue, have been steps in the whole process.

And now I think, again, to agree with Doug, the next important step, hopefully, happens during this presidential election. The only way that the next step is going to happen, is when there is, the bully pulpit is used to educate the country about the situation.

And, again, the point I made a minute ago, is it's really complicated to talk about this, but if you can simplify it enough that people understand there's two real truths out there -- well there's lots of real truths on budget -- but one is, we do have to make changes. It's not going fix itself, we do need to grow the economy, that's really important, but we are still not going to grow our way out of it. Policy changes will have to be made.

And the second one which, Ron, you go to in your question is, there's just no way, realistically, to fix this problem without revenues being a component of it. And that's because the spending cuts that will be required without revenues are so steep and hit so many people you don't want to hit, that that's not going to happen.

So the question is, and this is the question we really grapple with. We are doing a big project with the Concord Coalition called First Budget, which is going to focus on Iowa and New Hampshire, and how you get these presidential candidates to talk about this issue. So you have to think about what you are going to ask of them.

The big question is, how do you get people to be as specific as possible in politics about what they would do to fix the problem, and those specifics can't just be, oh, I would cap spending, because that's a really easy answer, and that's why have a sequester, because you don't get specific about the programs within that are. You need to get people to talk about how you would actually meet whatever the fiscal target is. Let's say it's getting the debt to 60 percent of GDP within 10 years.

And you have Republican candidates talking about it, Democratic candidates talking about it. We see what's really involved. We can look at the tradeoffs and we can compare them. You come up with a reasonable solution that way. But the risk of course, is that whoever talks about it honestly, it's like the President's dilemma, they get kicked out of there so quickly there's no way that the other guy comes up and meets him with an equally honest but different budget.

So I think the next step of this discussion is, how do you make transparent what the various choices are in policy? I think we need to fix a fiscal metric of something we are trying to do, balancing the budget is the easiest because the simplest thing to understand is what works in other countries, but I don't think it's realistic in a normal amount of times, so it's hard to figure out how you do that. And then we need to have kind of a fair set of rules where everybody is required to put out, in the same level of detail, how they would get there.

So I always like it when Rudi Penner says, you know, the problem -- the process isn't the problem, the problem is the problem, and the policy is the problem. We need policy, not just process, but like the conversation we are having here today about the debt ceiling, I think there are processes that we can think through and put in place that would help make transparent what the policy choices are, and that will move us yet another step closer to getting to this deal that doesn't have to happen in the next couple of years, but will have to, in all likelihood, happen in the next presidential watch.

MR. HASKINS: Okay. The audience. Let's have questions, and not long statements, please. Right here on the right? Wait one second, you'll get a microphone. Tell us who you are, and ask your question? Right -- I'm sorry, left. I'm so used to saying right.

MR. WALLACH: I'm Phil Wallach, from Brookings. I have two quick -- two quick remarks. The first is, it's hard for me to understand why 2016 should be better than 2012. We were having much closer to a trillion dollar deficits in 2012, and the Romney Campaign, ran right away from that issue as fast is it could get. And now we are going into 2016, we are having sort of -- by GDP -- a deficit to GDP standards, that's a pretty low deficit right now.

It's hard to see why, even though the long-term math is just a compelling as you've said, it's hard to see why the candidates are going to force themselves to look down that road and run those issues in 2016. I think that’s very unfortunately and short-sighted, I just -- it's hard for me to see why that would change.

The second comment is, a lot of the discussion jumbles together the budget questions, and we are not even talking about the debt ceiling specifically. There's some idea that having the debt ceiling kicking around the mixture must help, but I'm with David, I just -- I don’t understand why the debt ceiling doesn’t just become a distraction. You get the President who says, oh, I'm not going to play this brinksmanship, it just becomes a way of looking away from the actual spending and revenue questions that matter, and creating some third thing, that just totally districts from the process.

I know that that’s the debt ceiling increases have been attached to some of these big budget deals in the past, but that’s kind of just a necessity. It has to get raised at some point and gets attached to these things. It doesn’t actually force -- if you want to cut spending, cut spending in the budget process. I guess I would be interested to hear Maya and Doug talk more about why exactly they think having the debt ceiling in the mixture actually improves the discussion.

MR. HOLTZ-EAKIN: On the latter I didn’t say that, and I don't think it does. I mean -- but I think we'll get it done. It's not an economic entity. It's not something, if you wrote it down as first principles, you wouldn’t have a debt limit, right. You'd take care of the spending and the revenue decisions, and that they would determine the amount of debt you have and you are done, it's a political entity. It was put there, first, to give the Treasury more flexibility and retain to make sure that Congress could weigh in, right? And there are many instances where we have things that just force the Executive and the Congress to weigh in on things.

And that’s what the debt limit is. It hasn’t proven to be particularly successful, and in my view, but it’s there. On my optimism for '16, just let me be real clear what I'm saying. If you look at the CBO forecast for 2024, so you know, the end of the second terms, we have not just the big deficits, the deficits that are having a composition where a trillion-dollar deficit is $800 billion in interest borrowing.

And so the nature of that deficit is important. The composition is, we are just paying off previous borrowing, a very dangerous place to be. And it's getting worse, right, the trajectory is up. I don't think any president wants to be in that situation, and the risk that it runs for a genuine crisis, right. And they are not going to want to deal with this. No one will want to deal with this; we've proven that, right?

But, their smart advisors are going to tell them this is a risk, and unless something changes, we are going to have to deal with that risk, and that will force them to first, internally, and then perhaps publicly, acknowledge this problem. They are not going to have plans in 2015, I want to be real clear about that. They are not going to say, here is the plan. They are not.

But they are going to, for the first time, probably acknowledge, you know, we can't keep Medicare as we know it, right? And stop playing the granny card, granny is going off the cliff one more time. She always comes back from the next election; I don't know why we are worried about her. But it's going to build; and so, the '16, that the early onset, because it's the political map that matters, and it will be much more visible in the years after that.

MR. HASKINS: Maya?

MS. MACGUINEAS: Yeah. So those were two really good points. The first one about the deficit; I mean, one of the ironies of the fact that it was trillion-dollar deficits that woke up the country up to the problem, and that's when all this attention was focused on it. But it led us to focus on the wrong fixes. Because it wasn't making the trillion-dollar deficit go away, in the short term; that was the goal.

It was; hey, we've got 10 and 20 and 30-year debt problems, and how do we use the fact that people are turning out fiscal issues, to fix those things. And frankly, we did it completely the wrong way. We did the fiscal cliff deal and the sequester, and those things raise tax rates instead of reforming the tax code, and put spending caps on the absolute wrong part of the budget.

And importantly, forced cuts and increases in the immediate term when the economy was still recovering and did very, very little to improve on the long term. What's been improved in the long term the health care stuff wasn't part of those deals. So let's hope the health care improvements really stick, because that's going to be a key part of it.

But adding to that problem, of course, is now everybody is kind of pointing to the shrinking deficit saying, look, we've done it. You know, we've to the President out there repeatedly saying, we've cut the deficit by two-thirds. But the point is that that wasn't the goal. First off, that came after a huge, almost 800 percent increase in the deficit. But that was not the goal. The goal was to get the debt more controlled over 10 years, that didn't work.

So while you are right, that people aren't as aware of it, because the deficits come down, part of that reason is, politicians are claiming victory, look, the deficit has come down and there hasn't been a victory. But Doug is right that anybody who wants to be presiding over -- you know, running this country when these things hit, needs to start doing their own -- laying the groundwork for why we are going to make these reforms. Otherwise, they are going to have a nightmare of a time being a President when all those things happen.

And just on the debt ceiling, the bottom line is, the debt ceiling is not a smart way to do what we do. What my point would be is, we need action-forcing moments. Congress does not take action on fiscal policy unless there are action-forcing moments. And we have a number of stupid policies in place right now, I'll just point to SGR. SGR, right, the doc fix, never happens, it's a stupid way to fix health care.

But the truth is that over 90 percent of the fixes in times you've addressed this, it's led to health care reforms which actually were smarter reforms. So if you don't have those moments to push the change, then it's very unlikely anything will happen.

MR. WESSEL: I think that there's a chance, Phil, that the next President will do what Doug says, but it will be framed in very different terms. I don't think there's much evidence that getting up there and saying, I'm going to reduce the debt to GDP ratio, is going to make your life better.

But I can imagine some alternatives. I can imagine the President saying, you know, we are going to make Social Security sound, and all the fiscal economists here will see revenues going up and spending projections going doing, but it will be sold as making -- Social Security sound so that young people can count on it.

I can imagine, I mean, at some point they are going to do something on the infrastructure, and it may involved some revenues that will not be called a tax. I can imagine the colossus that's the Affordable Care Act, having changed the trajectory, but then forcing some changes in Medicare that are described as making Medicare compatible with whatever the post-Supreme Court Obama Care thing looks like.

And the people here at Brookings will be adding these up and saying, you know, these three things, an infrastructure thing, a Medicare reform plan, and safe Social Security, add up to a pretty coherent fiscal solution, but the President may never describe it that way. So, there are ways to get to go without holding -- I don't think -- I don't think the Simpson-Bowles, Domenici Rivlin Model is very attractive to politicians, as attractive as it is to us, because we like to see everything added up.

MR. HASKINS: That's exactly right. I think that's important.

MR. BELL: Let me just comment very briefly --

MR. HASKINS: To the right, you are -- Oh. Go ahead, Steve.

MR. BELL: -- on my question. Why do we get balanced budgets? We get balanced budgets because the person in the White House was willing to risk a tremendous amount of political capital. He was willing to piss off the people in the Senate who came to him as individual senators, and absolutely disagreed with him, both on welfare reform and on a balanced budget.

And because he had market people, like Bob Rubin, or like Larry Summers, advising him, saying; you need to be conscious of how markets are going to operate, and he was willing, and kicking and screaming, he dragged or drug, whichever is the right word, his party towards the center. If you don't have that kind of President who is willing to actually stand up and say, this is what we should do, then I think most of the time we are going to solve this by crisis.

And I have no idea what that crisis will be, but it's going to come out of the White House, and that's why maybe we'll talk about it in the '16 election. Or maybe it will turn out that Putin decided he wanted to go to Lithuania; and I'll tell you, that will make a difference in the discussion.

MR. WESSEL: Let me make two footnotes to that, Steve. First of all there was enormous stroke of good luck. It's good to be President when you've got this boom going, so Clinton got some tailwinds from that. The recent presidents had the opposite. And the second thing is that, I don't think any of us in Washington at the time, would have said that in 2015 Newt Gingrich would look like a reasonable guy, but compared -- the kind of negotiations that went on between Clinton and Gingrich that produced something are not something that we've been able to see in the current -- with the current collection of leadership; Obama, Boehner, McConnell.

MR. HASKINS: Let me violate my moderator's role, and add something to that I think is crucial. And that is that we also had a House that was, maybe not under Gingrich's control, but he had dramatic influence. Remember the Republicans said, one House for the first time in 40 years, and I can remember Republicans closed the government twice. Gingrich went up to the White House and sat down with the President, and they negotiated a deal. He took it back to the House, and he called everybody into the Cannon Room, that big glorious room in the Cannon Office Building, and he said -- he explained the deal, virtually without notes, it was an amazing performance.

And he said, this is not the best deal, this is the best deal we can get, and if you don't support it, you can find yourselves another speaker. If Boehner said that, it would be, bye-bye, John. So we don't have the kind leadership now, and an influence in the leadership, that we had there.

And the next question; back here on your right. Yeah, good.

MS. IRVING: I'm Susan Irving. Thank you, Steve, for recognizing. We've done a whole bunch of reports, and have another one coming out on the debt limit interaction. And I'd just like to say that I think one of the problems with the examples Maya cites on the -- she's read it previous; it's all of them still pretend that in doing that, you are going to -- it means you don't have to raise the debt limit again. And you will always have to raise the debt limit again, especially as constructive -- imagine the Social Security surplus returning, right.

And so I think what happens is, raising the debt limit is, as Doug said, a very hard vote, but what we need to do, is stop separating it, as Maya said, from the freebie vote of voting for spending, increases tax cuts, disaster relieve without offsets. And think about what Congress did in HEMP, and TARP, where they raise spending and raise the debt limit.

So I think what we -- first of all, let's not -- we all gravitate to a discussion now about the long-term problem because we all agree, that's the real problem, but this year, the problem is, are we going to scare the blink out of the markets again? Until 2011, the markets viewed Congress the way Congress viewed the markets; oh, a bunch of people jabbering but they'll do the right thing.

In 2011 they were scared -- you know, a word I can't use speaking for GAO. And then in 2013, you'll see other requests, so my question is, how do we begin to get people to understand that the debt limit is in fact the credit card? It's where do you pay your credit card bills, and it's got nothing to do with your future spending. And that's my problem, if you tie it to a deal, are you willing to default if we are not on track. I know you are not, but that's the problem with -- we are going to have to finesse some of these ideas.

MR. HASKINS: Well, Doug, what's your experience in talking to Members of the House, about the debt ceiling, when you go out there and talk to Republican members?

MR. HOLTZ-EAKIN: I decline to answer because this is a nice environment.

(Laughter)

MS. IRVING: Is that a point, that you can't convince them to (inaudible) because you are not --

MR. HASKINS: It's all on your shoulders, Doug.

MR. BELL: Especially now that you have absolutely no power.

MS. IRVING: Especially now that the left wing -- you know, you can't be crossed off as a left wing (inaudible) --

MR. HOLTZ-EAKIN: Then that part we can agree on. The not part is (inaudible) -- (laughter).

MR. HASKINS: It's just which one is going to get there first.

MR. HOLTZ-EAKIN: You know, here is the reality of discussions with "Republicans" number one they are not all alike. It's important to recognize there is a range of views, and it's a continuous range. It's not, just say no, and then reasonable people. There's a variety of different arrays of information, sophistication, and some people who have a deep interest in policy, and some of them, flatly just fundamentally and politically driven.

And so, you've got some who have pledged never to vote to increase the debt ceiling, it's a political position, and they are not going to mess with that. So, you know, I see no reason to try to convince them. I mean, you have to have good policy, be good politics, they've decided that that's their politics and that's not good policy.

So, when you talk to the rest, you get exactly the kind of conversation we've had today, which is many of them going, well, this is a very bad thing, and it will be bad for the country, and there's just no way we can let it happen, and my vote is in. That's all there is to it. And then you get in the middle, wow, is it really going to be that bad? Yes, I assure you it's going to be that bad, you have to do this.

All right, but it's a terrible vote. And I'm not sure I can do it. And so they are just -- they are doing exactly what this room is doing, which is they are weighing the politics and the policy, and with great reluctance, voting, yes, sometimes, and some just absolutely having decided in advance to vote, no.

MR. HASKINS: The next question? Yes, right here. Wait till you get the microphone.

MR LORENZEN: Ed Lorenzen, with the Committee for Responsible Federal Budget, and I worked on the paper. I just wanted to sort of take a little bit of issue with what Doug said, and contrasting with what Sue said, and that the paper -- the options paper weren't necessarily trying to insulate members from raising the debt limit entirely, it was insulating them from the debt limit if they were doing fiscally responsible actions, at least that's what many of their opposers were doing.

At the same time the point that Sue made is also true, that if those conditions aren't met or the process doesn't work, that there is still the risk of default, and the problems we have now, but that is, at least, no worse than we are today with the process.

And so it's in trying that balance between using it as a tool and eliminate the debt, but using it as an incentive, but forward leaning, of telling policymakers, if you are taking actions to keep -- meet these targets we are doing as a part of a budget, we are making these fiscal responsible choices that you can then avoid the politically tough one, and the risk of default, but you'll have to be taking those actions.

And so this would, you know, one, of people's thoughts as to where that -- whether that balance made sense of taking that risk away and taking the politically tough option away, but only if we are doing responsible things.

MR. HOLTZ-EAKIN: Here is my point. I mean, I understand the framework. It makes perfect sense, and I'll look at it more carefully, but my instinct was, you run the following political risk, right, which is, people will say, gee, the debt limit is going up, I mean we are just -- this thing just keeps going up and up, and it's an unpopular thing. Why aren't -- how did that happen?

Oh, well, they have this -- they've created this secret cabal that says if you have debt relative to their measure of projected GDP going in the right path, they don't have to vote on it, it just happens. Wow, like that a bit. Who are these people? Do we believe these forecasts? This is an utterly inside job, they are screwing us, and the mechanism doesn't survive it politically.

That’s my concern.

MR. HASKINS: One more question.

SPEAKER: Have any of you ever had a course in macroeconomics? Isn't it obvious that we need more revenue? I mean, the trade deficit -- the trade deficit -- Let me finish.

MR. HASKINS: Didn’t everybody say that?

SPEAKER: Well, they didn’t go into specifics. The trade deficit with China alone is about $850 billion a year. You put an economic multiplier of 3 on that, that’s $2.5 trillion worth -- worth of GDP; 20 percent of that will be $500 billion more of revenue for the Federal Government, and that’s just with China alone. Nobody wants to mention that, and now we want to talk about the TPP, and they export even more jobs overseas.

We have 46 million people getting food stamps. So do you want to have 100 million, and then you cut the food stamp budget, because it's an entitlement? Have you gone mad?

MR. BELL: Let me answer that.

MS. MACGUINEAS: The have you gone mad part?

MR. HASKINS: Well, Steve, you are our hero. Thank you.

MR. BELL: Clearly, clearly many people in this room in 1981 thought it would be invented reconciliation that that I had gone mad, but then we proved it by passing Gramm-Rudman-Hollings, before I left, so that kind of, yeah, I'm mad. I don't think it makes of a difference in the present situation, market situation, in the foreign exchange markets, whether China has 800 -- 1.1 trillion, or 1.5.

In fact, and this will be hearsay, I suspect our interest rates will stay lower -- there I go again, I'm going to get bankrupt, lower than people expect, because of flight to dominated assets. So contrary to what the general opinion is; that this June or this September, the Fed is going to do something which, it's only been forecast now for about three years, and therefore it's not in the market, doesn’t persuade me.

What persuades me is this, people who own our debt have -- would like very much not to lose too much on it. I don't know about the trade, I'm not a trade person at all, you know, it's not my thing. But I can tell you what markets will do if they look at China buying -- which they have -- $300 billion of our debt through British banks. If you take a look at the Treasury statement you'll see Great Britain had this much two years ago. Why in the hell do they have 350 now? Well, because the Chinese are buying it through Britain.

I love it that they have our debt, because it means they are constrained from a fire sale. And that's the only -- the redeeming factor, I think, is that they don't want to lose. Let's see, 1.2 trillion, take 10 percent away, and it's 120 billion, it's not a rounding error. So, in one sense, having foreign nations own our debt does not imprison us, it imprisons as a practical matter, them.

I'm not recommending that as what we do in the future, but I've got to tell you that we have a slow economy, it should surprise nobody. There have only been books written about it since 2009. Our friends at the University of Maryland and elsewhere have written about it. Europe is in trouble, GS, no surprise. You try to put Portugal together with France -- with Germany, thought that was going to work.

As Doug said, we are the nicest-looking horse in the glue factory, but at some point I have this question for people, how low can interest rates go in other nations, trying to drive export economies, when only America is buying things? I don't know that answer, but I do know that we tried it once before about 80 years ago. We didn't know that you were trying it then.

But I'm deeply concerned about what market reactions are going to be, not because of the traders -- of trade, and not really because of who holds our debt, I'm concerned because of what I said earlier, and I hate to filibuster. People who get paid literally tens of millions of dollars a year, and have 5, 6, 7,000 employees throughout the globe, looking at every commodity, at every foreign exchange.

People who know more about it than all of us put together, are watching carefully, and if some bond trader in Japan for Nomura, who is 26 years old, because that's about what they are, and he doesn't know. He remembered the last time, you know, these crazy fellows almost --

well it's a debt, and as my friend who is running a hedge fund that's focused on bond said, don't worry, Steve, if there is a panic, I will be the first out the door. And that's what I get worried about.

MR. HASKINS: Anyone on the Member's Panel, would like to make a concluding statement of any kind? Maya?

MS. MACGUINEAS: I'll make a point that, you know, so Monday we start extraordinary measures, and I go back to the first time we started using this, where you are kind of taking money from one trust fund, and switching it with another, because they don't all -- the debt limit doesn't apply to all them. And they were -- they were threatening to impeach the Secretary of the Treasury who was doing this for the first time.

And now, it's such commonplace. We go through it every time, and the problem of course is, we are going to wait until the very last minute again, with something this serious. And I think the most frustrating thing beyond the fact that we can't just go forward and work on the fiscal policies that need to be addressed in this country, is that there isn't a single negotiation that happens in advance of when it needs to. We always till the very last deadline.

And it's because, I think both sides feel like they can't give anything until they absolutely have to. But when it's something as serious as potentially defaulting, and we've had real threats of it before, that last-minute activity has real cost. And so it's one of the reasons I think figuring out ways to reform the debt ceiling so that there are still things that push us to address this. But don't get down to that last minute, is very desirable.

MR. HASKINS: Thank you. And thank you to the -- Do you want to say --

MR. WESSEL: No. Amen.

MR. HASKINS: Okay. All right, amen. Okay. Amen. Thank you to the audience. Good day. (Applause)

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