Too Big to Fail
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The United States is too big to fail. The largest economy in the world is too strong and too influential to fail. The United States economy leads all other economies as it has for the last 100 years; it has extensive ties to the global economic community. What's good for the US is good for the world. And what's good for the US government is good for its citizens.

These are the arguments we hear as the US debt issue approaches a full-blown debt crisis, similar to the near bankruptcy in Greece that continues to plague the EMU. Today Italy and Spain appear to have caught the Greece contagion.

Could the US actually default on its obligations? Would default be catastrophic? Is the United States, in fact, too big to fail?

There is no doubt that the United States is coming very close to actual default, just as Greece did earlier this month. The US Treasury must pay interest on outstanding national debt by August 2, 2011. It pays interest from monthly federal income (taxes, fees and interest earned) and from borrowing. The Federal government borrows 40 cents of every dollar it spends. And there's the rub. Federal borrowing is limited by law, and Congress has already spent up to (and a bit beyond) the legal debt limit of $14.3 Trillion. So if Congress does not raise the debt limit by $2.5 Trillion by August 2nd, the Treasury will be forced to pay debt interest and not pay out some domestic obligations. If it defaults on its debt payments, the credit rating of its sovereign debt will be downgraded, and the Dollar will decline. Secretary Geithner called the potential result "catastrophic."

Unlike Greece, the US has no higher collective available with bail-out funds at the ready. Neither the ECB nor the IMF can help the US. Not even the Bank of China could rescue the US today. It already owns over a $1Trillion is US Treasurys.

The current Keynesian solution is to raise taxes by $1Trillion or more over the next ten years, and maintain the current growth rate for federal spending. Maintaining the growth rate of federal spending implies cuts in federal programs because national demographics portend rapid cost growth in entitlement programs such as Medicare and Social Security. The tax hikes, now called "revenue increases" would come in the form of "closing tax loopholes" on corporations and setting higher tax rates for "millionaires and billionaires." Taxing the rich, it is thought, will help close future budget deficits and therefore reduce the federal debt. Budget cuts would maintain the current spending growth rate (rather than reverse the slope of the spending curve), and be limited to discretionary programs, including defense, but would not include Medicare and Social Security.

Those opposed to raising taxes cite the nation's anemic GDP growth rate, which has slowed to just 1.8%, and persistent high unemployment, which ticked up to 9.2% in June. Raising taxes, the opponents claim, might push the economy into a double-dip recession, or worse.

The president agrees that raising taxes in a recession is a bad idea. That's why he said in his press conference on Sunday that no new taxes will take effect until 2013. The president has stated this position before. In August 2009, on a visit to Elkhart, Indiana to tout his stimulus plan, Obama sat down for an interview with NBC's Chuck Todd, who passed on a question from Elkhart resident Scott Ferguson: "Explain how raising taxes on anyone during a deep recession is going to help with the economy." The president responded, "First of all, he's right. Normally, you don't raise taxes in a recession, which is why we haven't and why we've instead cut taxes. So I guess what I'd say to Scott is – his economics are right. You don't raise taxes in a recession. We haven't raised taxes in a recession."

But delaying tax hikes to 2013 will not change the need to pay debt obligations on August 2, 2011. And not fixing Medicare and Social Security is no solution to the controlling the largest consumers of the federal budget.

Opponents say it is time to re-prioritize the federal budget, and slash programs that are not essential to operating the federal government, while lowering taxes across the board. In Greece, the parliament agreed to deep cuts and a wide-ranging austerity program, required by its bail-out creditors.

The bail-out creditors in our case are the US citizens and businesses that pay federal taxes, purchase goods and services with US Dollars. Without substantial budget cuts and entitlement reform, taxpayers will pay more for spiraling federal costs directly by taxes, or indirectly through the inflation that follows the creation of money (and US Treasurys) out of thin air.

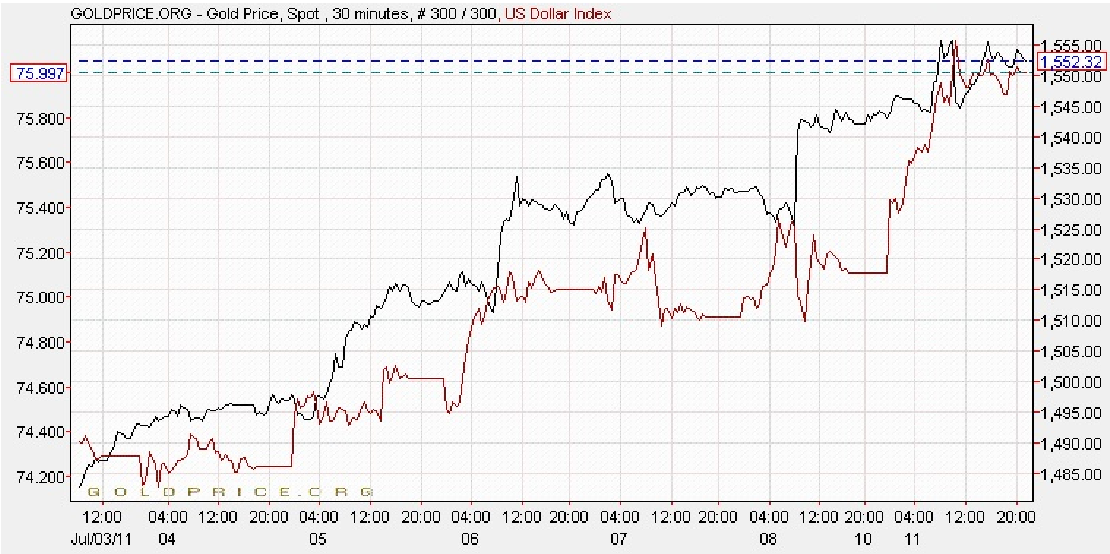
So it is the US taxpayer that will bear the brunt of a decision that does not cut federal spending by 3 times or more than the debt ceiling credit raise.

The US debt negotiations are being held in secret, away from the well of the Congress, away from debate, and away from the American people. The people are left with one-way press conference quips and few facts on which to judge, much less to act. And the story keeps changing. It's a wonder that the rating agencies have not come down with a verdict already. But the day ain't over yet.

The markets are reacting. Monday, the Dow dropped 150 points. The NASDAQ shed 2%. The sell-off may have come in part from new fears of debt crisis contagion in Italy and Spain. But there is no good news coming out of the secret US debt crisis negotiations. To the contrary, the US Treasury Secretary took to the Sunday talk shows with a message of impending doom.

Gold is reacting also. Gold continues to move up in price as investors seek the safe-haven trade. Gold open interest has swelled by 12,000 overnight contracts. Large Speculators have increased their long positions substantially, according to the CFTC.

What is more significant is the fact that since the negotiations began, Gold and the Dollar are moving in positive rather than traditional negative correlation.



It's time to start thinking about real solutions to our spending problems. As usual, Europe is light years ahead of the United States. The EMU addressed the debt crisis in Greece by enforcing strict austerity by the Greek parliament. We should learn from this example before, by accident or by treachery, the US debt negotiation catapults into a full-fledged debt crisis.

Part of the solution should be a return to sound money-- Bretton Woods II, with some refinements based on experience. One cannot build a sound monetary system based on money backed by thin air. Gold-backed US currency would bring fiscal discipline to the government and help grow the economy.

With a gold standard, commerce would flourish and citizens would prosper. The Federal government would be smaller and maybe more efficient. The United States economy would grow and become once again, a shining example for the world to see, a tower of financial and economic strength-- too strong to fail.

Investors from around the world benefit from timely market analysis on gold and silver and portfolio recommendations contained in *The Gold Speculator* investment newsletter, which is based on the principles of free markets, private property, sound money and Austrian School economics.

The question for you to consider is how are you going to protect yourself from the vagaries of the fiat money and growing inflation? We publish *The Gold Speculator to* help people make better decisions about their money. Our Model Conservative Portfolio gained 66.7% in 2010, and 55% for 1Q2011. Subscribe at our web site www.thegoldspeculatorllc.com with credit card or PayPal ($300/yr) or by sending your check for $290 ($10 cash discount) The Gold Speculator, 614 Nashua St. #142 Milford, NH 03055