

Senate Committee on Foreign Relations
Senator Richard G. Lugar
Opening Statement for Hearing on
Foreign Policy and the Global Economic Crisis
March 25, 2009

I join Chairman Kerry in welcoming a very distinguished panel which will offer insights into the global financial crisis and recommendations for U.S. policy.

At this stage, no one knows for certain how long or how deep this economic downturn will be. With the Administration's announcement of a plan to manage bad assets on the balance sheets of banks and corporations, we are at a critical moment in the resolution of our banking crisis. A fundamental strengthening of our banking system is a necessary precondition to a return to solid economic growth.

I am hopeful that as this plan is implemented, the U.S. government will be judicious about sinking taxpayer money into banks and corporations that are insolvent. As many experts have suggested, we need a careful triage of financial entities to determine which ones can stand on their own, which could become healthy with a reasonable infusion of additional capital, and which are insolvent beyond repair. Banks that are insolvent should be either liquidated or, in some cases, merged with other banks. Depositors should be protected, but shareholders may have to take their losses. U.S. taxpayer funds should only be used for recapitalization of troubled banks in limited cases, and the terms for government assistance should be uniform and transparent. The goals must be to restore discipline to the banking sector, reestablish investor confidence in healthy banks, and ensure that banks have the capacity to contribute to economic growth.

Actions to address our own economy are vital. But given the linkages between our financial sector and that of other countries, we cannot achieve economic recovery in isolation from the rest of the world. The United States must provide leadership in restoring the health of the international financial system. In particular, the lending capacity of the IMF must be increased. The Obama Administration has proposed increasing this capacity by \$500 billion, of which the U.S. commitment would be \$100 billion. I will be very interested to learn the witnesses' views of this proposal and whether they believe it is appropriately sized for the problem.

As we work with other nations, our government must pay attention to how the global economy and our role in it can be rebalanced. Some level of deficit spending is appropriate at this stage in the crisis, but the U.S. budget deficits that are projected cannot be sustained without extreme risk to both Americans and the international community. We cannot depend indefinitely on China investing heavily in U.S. government debt. Some thought must be given to how we work with China and other nations to establish a more sensible global balance that depends less on demand by American consumers.

We also must be cognizant of the incredible pressures this global financial crisis will place on stability and peace. We have to expect additional political, economic, or even national security shocks. We know from history that societies under severe economic stress often do not make good political choices. In the face of job losses, wealth evaporation, homelessness, hunger and other outcomes, the fabric of many nations will be tested. The crisis is likely to stimulate nationalism that could lead to demagogic policies or governments. Under such conditions, some nations might experience a retreat from democracy. This in turn increases the possibility of violent conflict within and between nations. Consequently, maintaining international cooperation in addressing the economic crisis affects more than our prosperity.

The upcoming G-20 meeting must be a success, not just in the proposals that are adopted, but also in the tone that is established for subsequent cooperation. The meeting should offer a clear message that the major economies will cooperate on financial restructuring and resist protectionism.

The United States must prepare itself for changes in its international role. We should ask ourselves, what will be the basis of U.S. national influence in the future? Why will nations continue to listen to us? What leverage over rivals can we preserve and how can we ensure that we will still be able to rally friends behind vital U.S. objectives? The global crisis has increased the skepticism in emerging economies about American-style capitalism. And it is likely to reduce enthusiasm within the United States and beyond for liberalized trade measures that would greatly benefit our country. I do not believe that we are facing a precipitous collapse of U.S. influence. But we have to be far more deliberate in executing a rational plan that gets the most out of U.S. strengths and compensates for new weaknesses.

I thank the Chairman for calling this hearing and look forward to today's testimony.

###