



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

SECRETARY OF THE TREASURY

May 13, 2011

The Honorable Michael Bennet
United States Senate
Washington, DC 20510

Dear Senator Bennet:

Thank you for your recent letter requesting an estimate by the Treasury Department of the fiscal and economic consequences of failing to raise the statutory debt limit. I greatly appreciate your leadership on this issue and your strong commitment to protecting the full faith and credit of the United States.

I hope that Congress will act in a timely manner to increase the debt limit and protect the full faith and credit of the U.S. government, but I appreciate the opportunity to respond to you about this matter. As you know, the debt limit does not authorize new spending commitments. It simply allows the government to finance existing legal obligations that Congresses and presidents of both parties have made in the past. Failure to raise the debt limit would force the United States to default on these obligations, such as payments to our servicemembers, citizens, investors, and businesses. This would be an unprecedented event in American history. A default would inflict catastrophic, far-reaching damage on our Nation's economy, significantly reducing growth, and increasing unemployment.

A default would call into question, for the first time, the full faith and credit of the U.S. government. As a result, investors in the United States and around the world would be less likely to lend us money in the future. And those investors who still choose to purchase Treasury securities would demand much higher interest rates, reflecting the increased risk that we might default on our obligations again.

Default would not only increase borrowing costs for the Federal government, but also for families, businesses, and local governments – reducing investment and job creation throughout the economy. Treasury securities set the benchmark interest rate for a wide range of credit products, including mortgages, car loans, student loans, credit cards, business loans, and municipal bonds. Accordingly, an increase in Treasury rates would make it more costly for a family to buy a home, purchase a car, or send a child to college. It would make it more expensive for an entrepreneur to borrow money to start a new business or invest in new products and equipment.

A default would also lead to a sharp decline in household wealth, further harming economic growth. Higher mortgage rates would depress an already fragile housing market, causing home values to fall. Additionally, a default would substantially reduce the value of the investments – including Treasury securities – held in 401(k) accounts and pension funds, which families depend on for their retirement security. This significant reduction in household wealth would threaten the economic security of all Americans and, together with increased interest rates, would contribute to a contraction in household spending and investment.

Default would also have the perverse effect of increasing our government's debt burden, worsening the fiscal challenges that we must address and damaging our capacity for future growth. It would increase rates on Treasury securities, which would significantly increase the cost of paying interest on the national debt. Additionally, the severe economic damage caused by a default would result in weaker growth for an extended period of time – lowering tax revenues and putting increased demands on social safety net programs. As a result, a default would channel a larger share of our national wealth toward paying our creditors rather than reducing our debt or making productive investments in education, innovation, infrastructure, and other areas that will help drive economic expansion and create new jobs.

The unique role of Treasury securities in the global financial system means that the consequences of default would be particularly severe. Treasury securities are a key holding on the balance sheets of virtually every major insurance company, bank, money market fund, and pension fund in the world. They are also widely used as collateral by financial institutions to meet their day-to-day cash flow needs in the short-term financing market.

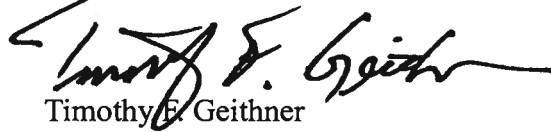
A default on Treasury debt could lead to concerns about the solvency of the investment funds and financial institutions that hold Treasury securities in their portfolios, which could cause a run on money market mutual funds and the broader financial system – similar to what occurred in the wake of the collapse of Lehman Brothers. As the recent financial crisis demonstrated, a severe and sudden blow to confidence in the financial markets can spark a panic that threatens the health of our entire global economy and the jobs of millions of Americans.

Even a short-term default could cause irrevocable damage to the American economy. Treasury securities enjoy their unique role in the global financial system precisely because they are viewed as a risk-free asset. Investors have absolute confidence that the United States will meet its debt obligations on time, every time, and in full. That confidence increases demand for Treasury securities, lowering borrowing costs for the Federal government, consumers, and businesses. Indeed, during the recent crisis, investors flocked to Treasury securities as a safe-haven asset in the midst of a damaging financial panic. A default would call into question the status of Treasury securities as a cornerstone of the financial system, potentially squandering this unique role and the economic benefits that come with it.

Moreover, the fact that the United States would not have enough money to meet all of its obligations would have serious economic consequences. If the United States were forced to stop, limit, or delay payment on obligations to which the Nation has already committed – such as military salaries, Social Security and Medicare, tax refunds, contractual payments to businesses for goods and services, and payments to our investors – there would be a massive and abrupt reduction in federal outlays and aggregate demand. This abrupt contraction would likely push us into a double dip recession.

It is critically important that Congress act as soon as possible to raise the debt limit so that the full faith and credit of the United States is not called into question. Congress has never failed to raise the debt limit when necessary. I fully expect that Congress will once again take responsible action, and look forward to working with you and your colleagues on this issue in the weeks ahead.

Sincerely,

A handwritten signature in black ink, appearing to read "Timothy F. Geithner". The signature is fluid and cursive, with a long horizontal stroke at the end.

Timothy F. Geithner

cc: The Honorable Ben S. Bernanke
The Honorable Jack Lew