

rense.com

# US Budget Deficits Risk Crash - Australian Treasury

By David Uren and Roy Eccleston  
The Australian  
2-25-5

Peter Costello's closest adviser fears the US is heading for a devastating financial crash that could ravage Australia's economic growth.

As the Reserve Bank considers raising interest rates at its board meeting next Tuesday, Treasury Secretary Ken Henry likened the flood of money pouring into the US to support its budget and current account deficits to the stockmarket's dotcom bubble of the late 1990s.

Were it suddenly to stop, there would be shockwaves felt throughout the world's economies.

The financial crash feared by Dr Henry would involve a sharp fall in the US dollar and a bond market sell-off, which would push up US and world interest rates.

This would hit US economic growth and, as a result, cut Chinese exports of manufactured products to the American market. In turn, this would threaten the boom in Australian mineral exports to China.

Fears that the world economy is in grave danger are growing in the major financial capitals.

The International Monetary Fund, which is responsible for stability of the world economy, also warned yesterday of a sudden collapse.

IMF managing director Rodrigo de Rato said urgent combined international action was required to head off the dangers.

The main cause of concern is the fact the US is running a trade deficit of about \$US600billion (\$760billion) and a budget deficit of about \$US430billion for 2005.

US imports are almost 50per cent greater than the country's exports, with the deficit being financed by international central banks and funds managers.

Despite signs that the deficit is getting bigger, money is pouring into the US from Asia and Europe at such a rate that the US has been able to keep its long-term interest rates steady at 4.2 per cent since the middle of last year.

Dr Henry said the flood of money was "worryingly reminiscent of Federal Reserve chairman Alan Greenspan's warning in 1996 of irrational exuberance in US stocks".

He said that, as with the dotcom bubble in the 1990s, one could not tell how long it would keep going, but it would burst eventually.

Dr Henry's comments, made to a meeting of Asian treasurers in Sydney yesterday, reveal that Treasury is much more worried about the health of the world economy than is the Reserve Bank.

Reserve Bank governor Ian Macfarlane said last week that he did not think the US current account deficit was a serious threat.

"I suspect the rest of the world will continue to finance the US current account deficit," he said. But if it did not, all that would happen would be a fall in the US dollar, which would not have serious consequences.

The Reserve Bank expects world economic growth to slow only slightly from last year, when it recorded the fastest growth in almost 30 years.

The different views about the economic risks may be aired at the Reserve Bank meeting on Tuesday. Dr Henry sits on the Reserve Bank board.

The bank does think there are risks of financial collapse in the US, but believes it would be caused by the complexity of new financial products.

The IMF also thinks economic growth will remain firm over the year ahead, but Mr de Rato says there are "serious threats and challenges ahead".

Mr de Rato warned that it was highly unlikely that the US would continue to have access to "easy credit", based on its present economic policies.

Mr de Rato said the fall in the value of the dollar should act as a "timely wake-up" to policy makers around the world to tackle the imbalances in the world economy.

Mr de Rato said these included not only the US's deficits, but also resistance to economic reforms in Europe and Japan, as well as China's fixed exchange rate.

Dr Henry said the problems went beyond the American deficits, which he said were mirrored by excessive surpluses in Asia.

He said Asian countries were not allowing their domestic economies to grow fast enough, and were relying too much on exports. This put them at risk in any world economic downturn.

The boom in investment in American financial markets could be brought to a halt by a number of developments, Dr Henry said.

A slowdown in American growth could lead international private investors to pull out of the country.

Foreign central banks, which have been buying long-term American government bonds, are already facing big losses as a result of the fall in the value of the greenback.

"What if they change their mind?" Dr Henry asked.

He said it was imperative that the Americans take action to reduce their budget deficit, while they should allow the value of the US dollar to fall further.

[Disclaimer](#)

[Email This Article](#)

---

**MainPage**

<http://www.rense.com>

**This Site Served by TheHostPros**