EUROPE'S SOVEREIGN DEBT CRISIS: CAUSES, CONSEQUENCES FOR THE UNITED STATES AND LESSONS LEARNED

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EUROPE'S SOVEREIGN DEBT CRISIS: CAUSES, CONSEQUENCES FOR THE UNITED STATES AND LESSONS LEARNED

Wednesday, March 21, 2012,

HOUSE OF REPRESENTATIVES,
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM,
Washington, D.C.

The committee met, pursuant to call, at 9:30 a.m. in room 2154, Rayburn House Office Building, Hon. Darrell E. Issa [chairman of the Committee] presiding.

Present: Representatives Issa, Burton, Turner, McHenry, Jordan, Lankford, DesJarlais, Gowdy, Farenthold, Kelly, Cummings, Maloney, Norton, Kucinich, Connolly, Quigley and Welch.

Staff Present: Kurt Bardella, Majority Senior Policy Advisor; Brian Blase, Majority Professional Staff Member; Robert Borden, Majority General Counsel; Molly Boyl, Majority Parliamentarian; Lawrence J. Brady, Majority Staff Director; John Cuaderes, Majority Deputy Staff Director; Gwen D'Luzansky, Majority Assistant Clerk; Linda Good, Majority Chief Clerk; Tyler Grimm, Majority Professional Staff Member; Peter Haller, Majority Senior Counsel; Ryan M. Hambleton, Majority Professional Staff Member; Christopher Hixon, Majority Deputy Chief Counsel; Mark D. Marin, Majority Director of Oversight; Rafael Maryahin, Majority Counsel; Kristin L. Nelson, Majority Professional Staff Member; Laura L. Rush, Majority Deputy Chief Clerk; Jeff Solsby, Majority Senior Communications Advisor; Noelle Turbitt, Majority Staff Assistant; Rebecca Watkins, Majority Press Secretary; Jaron Bourke, Minority Director of Administration; Kevin Corbin, Minority Deputy Clerk; Carla Hultberg, Minority Chief Clerk; Adam Koshkin, Minority Staff Assistant; Lucinda Lessley, Minority Policy Director; Leah Perry, Minority Chief Oversight Counsel; Jason Powell, Minority Senior Counsel; Steven Rangel, Minority Senior Counsel; Dave Rapallo, Minority Staff Director; and Mark Stephenson, Minority Director of Legislation.

The CHAIRMAN. The Committee will come to order.

The Oversight Committee mission statement is that we exist to secure two fundamental principles. First, Americans have the right to know the money Washington takes from them is well spent. Second, Americans deserve an efficient, effective government that works for them. Our duty on the Oversight and Government Reform Committee is to protect these rights. Our solemn responsibility is to hold Government, I repeat, Government, accountable to taxpayers because they have a right to know what they get from their Government. Our job is to work tirelessly in partnership with citizen watchdogs to deliver the facts to the American people and genuine reform to the Federal bureaucracy.

Today's hearing is most important because, in fact, since 2009 Europe has been struggling to emerge from a severe sovereign debt crisis brought about by massive government spending and a weak economy. America could say the same: that we, in fact, have been struggling since 2009 to emerge from a severe sovereign debt crisis brought about by massive Government debt and, in fact, a weak economy.

But that is not the issue today. The issue is not America's economy or sovereign debt; the issue is if the European Union in international monetary funds spends hundreds of billions of Euros to aid Greek, Ireland, Portugal, the E.U. and, with IMF assistance, if, in fact, America will be drawn into this problem. Can America afford one sovereign debt crisis such as Greece?

I believe, after over a year of watching the Greece on-again, off-again crisis, there is a certain assumption that eventually it will be solved, a certain assumption that we know what we are doing, a certain assumption that, in fact, it will, in time, be solved.

Clearly, this hearing, which builds on the good work of Chairman Patrick McHenry, is, in fact, to ask a greater question. The greater question is: what if we could go beyond Greece. Assumptions are that, between hedging and, in fact, other means, that the problem is manageable. Our obligation is to say what if it is not.

Our witnesses today are the two most important individuals at the center of this. Our Federal chairman certainly has a good understanding of our economy, what the Federal's capabilities are, and ultimately what he can do if, in fact, things go wrong.

Secretary Geithner, who has been a loyal servant of the American people both at the Federal Reserve in New York and now in his current position, also has been intimately involved in both the U.S. crisis and in matters of Europe.

So today our primary question will be, in fact, on what U.S. exposure truly is, what the impact to taxpayers could be. We will try not to look to the past; we will try to look to the future. But let us understand that, while we have a budget deficit of more than a trillion dollars, while our debt in the United States is 100 percent of GDP, while, in fact, we are still remembering the good and the very bad of TARP, we are still remembering both of the individuals before us today came and were involved in saying what TARP would be spent for, none of which came to pass. Ultimately, as Secretary Geithner has recently said, he does not plan on needing a bailout. He does not anticipate it.

Our obligation on this Committee is to anticipate and to plan; therefore, the questions today for our two esteemed witnesses will be: what is plan B? I repeat, what is plan B if what you are managing is not manageable?

With that I would like to recognize the Ranking Member for his opening statement.

Mr. CUMMINGS. Thank you very much, Mr. Chairman, for calling this hearing.

I want to say to you, Secretary Geithner and Chairman Bernanke, I thank you for your service to our Country, and I thank you on behalf of a grateful Congress and a grateful Nation.

Mr. Chairman, this is a very important issue, addressing the financial crisis in Europe and the lessons that can be learned here at home from it.

Since the last hearing we held on this topic in December, the European officials have taken decisive action to reestablish financial stability in the Eurozone. American officials have helped diplomatically through consultation, through our participation in the IMF, and through the Central Bank support. No one is declaring mission accomplished, but the signs of improvement are impossible to miss.

Unfortunately, it appears that some in the majority see the Euro crisis as a justification for imposing extreme austerity measures here at home. Yesterday the House Republicans released a budget proposal to cut $5.3 trillion over the next ten years to end Medicare as we know it and shift costs to seniors and give further tax rates to corporations.

Today the majority will seek to draw parallels between Greece's financial troubles and those of the United States. In our last meeting, a majority witness called Greece a "wake-up call", arguing that the United States should shred our Nation's safety net and cut taxes to avoid Greece's fate.

Don't believe it. While strong medicine is needed, it is the banks that caused the financial crisis who should be taking the hit.

What we have learned from Greece is that austerity measures imposed during an economic downturn have very real negative consequences for working people, hard-working people, while they leave economic elite unscathed. Nevertheless, some Republicans believe we should implement similar extreme austerity measures here at home in the form of deep across-the-board spending cuts.

Secretary Geithner, on past occasions you warned against such actions. For example, you said this, "We need to stay intensely focused on straightening our economy in the short term. We can't cut our way to growth. Severe austerity now would be very damaging."

But how Republicans have ignored this key point. Different problems require different solutions. In the case of the United States, economists largely agree that the housing bubble and risky investment products created by Wall Street were the key causes of our economic collapse. As Mark Zandi, chief economist of the Moody's Analytics Link, stated: Housing is ground zero for the economy's problems, high unemployment, and lost jobs.

Although the recent $25 billion settlement with five of these banks is commendable, the sad truth is that millions of borrowers will not receive the relief they so desperately need because one important entity refuses to cooperate. The Federal Housing Finance Agency, the FHFA, Fannie Mae's and Freddie Mac's regulator, will not allow them to participate in the settlement, reportedly because much of the relief would be in the form of principal reduction.

If we want to ensure that our economy at home is strong enough to weather the Euro crisis, turbulence from slowdowns in other foreign economies, we must end the housing crisis here at home. We must have principal reduction as one tool for borrowers who are underwater and who owe more than their homes are worth—in many cases through no fault of their own, by the way. FHFA's own data shows that principal reduction would save taxpayers billions of dollars. But Edward DeMarco, the agency's acting director, maintains what happens to be an ideological opposition. It is my hope, as we examine the Euro crisis, we keep in mind what should be our ultimate goal: rebuilding and protecting a strong economy for the millions of middle class Americans here in the United States.

Mr. Chairman, with that I ask unanimous consent to enter the March 20th Washington Post article entitled: The Man Blocking America's Recovery into the record.

The CHAIRMAN. How is this germane to today's hearing?

Mr. CUMMINGS. It addresses this issue.

The CHAIRMAN. We can include it as extraneous material, but it was really germane to the hearing we had in New York and would also suggest it be placed in the record for that hearing.

Mr. CUMMINGS Thank you very much.

The CHAIRMAN. You are welcome.

We now go to the chairman of the Subcommittee, Mr. Patrick McHenry, for his opening statement.

Mr. MCHENRY. Thank you, Mr. Chairman, and thank you for calling this hearing today.

Nearly four years ago Americans witnessed domestic and global markets deteriorate, resulting in millions of job losses and unprecedented measures by Government and central banks to prop up financial institutions. As the United States economy remains vulnerable in the midst of a very shaky recovery, just across the Atlantic our European friends fight to fend off a second wave of economic and financial turmoil. Their lesson is one for the world, as well as the United States.

In December my Subcommittee invited officials from the Federal Reserve and the United States Treasury to explain the economic unrest facing Europe and what actions they would consider in reaction to it and what measures remain at their disposal as events change day by day.

At the time the Federal Reserve had just authorized foreign currency liquidity swap lines with five central banks to bide time for a political solution in Europe and for recapitalization purposes, as well. Daily headlines read of liquidity injections to the tune of billions and trillions of Euros swaying stock markets wildly.

In December the ECB had a second auction known as a long-term refinancing operation to provide European banks with over 500 million Euros in cheap loans and a credit event was declared in Greece. The credit event in Greece is one of particular concern to markets around the world.

As we look ahead, the European story is far from over. European leaders continue to strengthen the weak framework of the E.U. to substantiate their rescue efforts, and financial markets become more dependent on the continued willingness of the central banks to use their balance sheets to rescue the global economy.

My understanding is that the economic storm facing Europe influences U.S. markets. I commend Chairman Issa for inviting Chairman Bernanke and Treasury Secretary Geithner here to Congress to address this critical issue.

I am interested to hear how our Nation's foremost economic experts and authorities view the Euro's own crisis, the impact it can have on the United States' economy, and our pension funds and market participants, as well.

With that, I would like to yield the balance of my time to the former Chair, Mr. Burton.

Mr. BURTON. I thank the gentleman for yielding.

The Chairman said in his opening remarks that he wanted to find out if the United States possibly could be drawn into the Euro crisis. I have been to Europe. I have been all over the place over there, including Brussels. I am convinced that we are already drawn in. So I would like to find out today how deeply we are drawn in and how severe the problem could be, especially if the Euro is devalued. And I want to find out if we are underwriting or bailing out the Europeans, and to what extent.

When I was in Brussels I found out that the invitation to us printing money with QE1 and QE2, the European central banks are doing that over there, as well, so they are inflating their money supply.

Let me first say, according to the Congressional Research Office, our exposure to Greece, Ireland, Italy, Portugal, Spain, and France and Germany is $641 billion for those, and for France and Germany it is $1.2 trillion, so there is that exposure already.

Regarding the currency swaps with the European central banks, including Canada, Switzerland, Japan, and the United Kingdom, we have as of February 15 $109 billion is outstanding on those lines. As I said before, if there is a devaluation of the Euro, what does that do to our exposure and how much is that going to cost the United States?

In addition to that, Treasury Secretary Geithner has dismissed reports that we might participate in a special IMF European aid fund, and I would like to know if that is accurate and if that is going to be true in the future. And the Obama Administration increased our contribution to the IMF, which is currently 17 percent of the IMF's overall budget, and the IMF has indicated it is going to need another $500 billion.

So what I want to find out is: how much exposure are we facing right now? And how much exposure are we likely to have added on to us? And are we going to be underwriting the European financial crisis, and what impact that is going to have on the United States of America?

Thanks, Mr. Chairman.

The CHAIRMAN. I thank the gentleman. I thank both the Subcommittee chairman on TARP and Financial Services and our former full Committee chairman.

With that, we go to the Ranking Member of the Financial Services and TARP Subcommittee, Mr. Quigley, for five minutes.

Mr. QUIGLEY. Thank you, Mr. Chairman.

Today's hearing, as we know, builds on the two previous hearings we held before the TARP Subcommittee, of which I am honored to be the Ranking Member.

As in December, today's hearing will examine the European debt crisis and what it means to U.S. taxpayers in our economy.

As Mr. Douglas Elliott of the Brookings Institute testified in December, in 2010 our exports to the E.U. totaled $400 billion. We have over $1 trillion of foreign direct investments in the E.U. The global market is not what it was ten years ago, or, for that matter, five years ago. The complexity of the market is such that there can be no question a healthy European economy is in the best interest of the United States and the American taxpayer.

The plain truth is: when the earthquake of a financial crisis hits, every nation feels its aftershocks, including here at home. That is why I am encouraged by the work Secretary Geithner and Chairman Bernanke have done to engage the E.U. I am also cautiously optimistic by the steps taken by Europe's political and financial leaders since our Subcommittee hearing in an effort to add stability to the European financial system. European leaders created a fiscal compact under which 25 nation states agreed to new rules aimed at controlling deficits. And Greece recently restructured its debt. The European Central Bank has also worked to contain a crisis by purchasing bonds and providing loans.

These recent actions have lessened the pressure on our financial market here at home; however, it is important to recognize that the Eurozone has a long and challenging road ahead. Countries like Greece, Italy, and others need to implement a balanced approach to their short-term and long-term financial challenges.

Some have likened our economy to Greece's, but I believe that the U.S., unlike Greece, controls its own destiny. We need a balanced approach to get our own fiscal house in order. We have to put everything on the table, but we also have to ensure that in reducing the deficit we don't torpedo our recovery.

The truth is that the mission of government matters, but reckless decisions have made it harder to fulfill that mission. We cannot allow politics to get in the way of what is right. We need to take a balanced approach both in spending and revenue-generating measures.

Reality is that now is not the time to pull the rug from those who need the help most, but a long-term deficit reduction plan is not incompatible with economic growth.

We also must not forget politics, not economics, nearly saw the U.S. Government default on its debt in early August. We cannot allow politics to stand in the way of addressing the home foreclosure crisis, ensuring our Nation's seniors have health care, and low-income children have food to eat.

As Ranking Member Cummings addressed in his statement, strengthening our economy must be our number one priority, but we cannot forget about the essential links between our economic and Europe's.

I look forward to hearing the testimony of the Secretary and the Chairman on this important issue.

Thank you. I yield back.

The CHAIRMAN. I thank the gentleman.

Before I introduce the witnesses, I want to caution the Committee. It is our policy when we invite guests, I joked with them both beforehand, to tell them what the Committee hearing is about, to expect that they will have answers for our questions, not just answers irrelevant of our questions. But, at the same time, we have an expectation that today's hearing is primarily and technically exclusively about the European debt crisis and how it might affect America.

So although by definition there is a ripple effect and you may want to ask broader questions, if you ask questions that are not germane to the subject for which we have invited our guests, it will be their option whether to say they were prepared or not prepared to answer them. We want our witnesses to be fully prepared. We only asked them here under that fairly narrow set of circumstances.

Now, Mr. Secretary and Mr. Chairman, you are very good beyond that, so I won't be surprised if you may choose to answer questions, but I am cautioning all of our people that you are our guests. We do not intend to have you asked questions and expected to answer them if they are well outside the scope of today's hearing.

With that, pursuant to our Committee rules, all witnesses must be sworn. Would you please rise and take the oath.

Please raise your right hands. Do you solemnly swear or affirm that the testimony you are about to give will be the truth, the whole truth, and nothing but the truth.

Secretary GEITHNER. I do.

Mr. BERNANKE. I do.

The CHAIRMAN. Let the record reflect all witnesses answered in the affirmative.

Please take your seats.

A little bit like yesterday, with Secretary Chu, we would like you to stay as close to five minutes as possible. We would like you to know that your opening statements, of course, are placed in the record in their entirety, along with extraneous material you may choose to enter after the hearing.

With that, I am not sure we did a coin toss, but I will go from left to right.

Mr. Secretary, you are recognized for five minutes.

WITNESSES STATEMENTS

STATEMENT OF TIMOTHY F. GEITHNER

Secretary GEITHNER. Thank you, Mr. Chairman and Ranking Member Cummings and members of the Committee. Thanks for giving me a chance to come talk to you today about the crisis in Europe and its risks and implications for the United States. This has been going on for more than two years, of course, and we welcome the attention you are bringing to this important question.

Europe is a key strategic and economic partner of this Country, and we have an enormous stake in the success of Europe's efforts to avert a catastrophic financial crisis.

Our economy is gradually getting stronger, but, of course, we still face a lot of tough challenges here in the United States. Among those challenges, of course, unemployment is still very high, the housing market is still very weak. We still have a long way to go to repair the damage caused by our crisis, but we also face a challenging and uncertain global economic environment with the risks around Iran adding to the pressure on oil prices and Europe facing a long and difficult crisis.

Europe accounts for about 18 percent of global GDP. It is the major source of financing for many emerging economies and accounts for about 15 percent of U.S. exports of goods and services, with a larger portion of the exports of many of our trading partners. When growth slows in Europe, it affects growth around the world. And when the fears of a broader European crisis have been most acute, as they were in the summer and fall of 2011, and earlier in the spring and summer of 2010, then financial markets fell around the world, damaging confidence and slowing the momentum of recovery here in the United States and around the world.

Now, over the past few months, with our active encouragement and support, Europe's leaders have put in place a more comprehensive strategy to address the crisis. This strategy has the following key elements:

First, it involves economic reforms, very tough reforms in the member states to restore fiscal sustainability to restructure recapitalized banking systems to improve the competitiveness and growth prospects of their economies.

Second, it includes broader reforms to the institutions of Europe, including the Fiscal Compact that establishes stronger disciplines on the fiscal policies of the member states to limit future deficits and debt as a share of GDP. It involves a coordinated strategy to recapitalize, as I said, the European financial system with government backstop for funding. And it involves a firewall, a financial firewall of funds to provide financial support to governments that are undertaking reforms so they can help retain access to financing on sustainable terms.

These reforms have been aided by a number of actions by the European Central Bank, and together these efforts have helped calm financial tensions somewhat, but Europe is still at the initial stages of what will be a long and difficult path of reforms. And for these reforms to work, policy makers in the Euro area are going to have to carefully calibrate the mix of financial support and the pace of consolidation, fiscal consolidation, ahead.

These reforms, these tough economic reforms, are not going to work without financial support that enables governments to borrow at affordable rates. And if every time economic growth comes in a little weaker than expected governments are forced to cut spending or raise taxes to compensate for the impact on deficits, this would risk a self-reinforcing negative spiral of growth-killing austerity.

The most important unfinished business of this broader financial strategy in Europe is to build a stronger financial firewall. European leaders are now reviewing options for how to expand the combined financial capacity of their two funds so they can make it clear to markets that they have the resources available on a scale that is commensurate with the needs they might face were the crisis to intensify in the future.

As you know, the IMF has played an important role in Europe. IMF has provided advice on the design and reforms, a framework for public monitoring of progress, and financial support for programs in Greece, Ireland, and Portugal. The financial support has come alongside a much larger amount of financial support from the European nations, themselves, as is appropriate.

It is in the interest of the United States that the IMF continue its efforts in Europe, but the IMF resources cannot substitute for a strong and credible European firewall. The IMF has played a major role in every major post-war financial crisis, while consistently returning to the United States any resources with interest that it has temporarily drawn upon. Our premise for the IMF are backed by very strong financial safeguards, and in more than 60 years of experience dealing with financial crises we have never lost a penny.

Over the past 18 months the crisis in Europe has taken some of the wind out of our recovery. We are encouraged by the progress that our European colleagues have been making. We hope they are able to build on these efforts in the coming weeks to put in place a more durable foundation for economic growth and a stronger financial firewall. We do not want to see Europe weakened by a protracted crisis, so we are going to continue to work very closely with them and with the IMF to encourage further progress.

Thank you.

[Prepared statement of Secretary Geithner follows:]

Written Testimony of Secretary Tim Geithner
Before the House Committee on Oversight and Government Reform
March 21, 2012

Chairman Issa, Ranking Member Cummings, and members of the Committee, thank you for the opportunity to testify today on developments in Europe. Europe is a key strategic and economic partner of the United States, and we have an enormous stake in the success of European efforts to restore financial stability and secure growth. The U.S. recovery is getting stronger, but the strength of our recovery will depend in part on events beyond our shores, as we saw last year when U.S. growth was buffeted by headwinds from Europe.

Since that time, European leaders have taken a series of steps to address the crisis and we are encouraged by the progress to date. We hope Europe will build on that progress with additional actions to calm the financial tensions that have been so damaging to global economic growth and put in place a stronger framework of policies and institutions to make the European Monetary Union viable over the longer term and help the member countries to strengthen economic growth.

The European Policy Response

With our encouragement and the support of the IMF, Europe's leaders have put in place a comprehensive strategy to address the crisis. This strategy has the following key elements:

- Economic reforms in the member states to restore fiscal sustainability, restructure the banking systems, and improve competitiveness and growth prospects;

- Institutional reforms, including the "Fiscal Compact," that establish stronger disciplines on the fiscal policies of the member states to limit future deficits and debt as a share of GDP;

- A coordinated strategy to recapitalize the European financial system, with government guarantees of funding; and

- A "firewall" of funds to provide financial support to governments that are undertaking reforms to help assure access to financing on sustainable terms.

These efforts by governments have been reinforced by a substantial amount of support from the European Central Bank.

The European economies at the center of the crisis have made very significant progress.

The causes of the crisis were years in the making and were very different across the continent.

After the establishment of monetary union in 2000, interest rates across the union fell significantly, with rates converging toward Germany's. This was accompanied by a substantial rise in borrowing. In Greece, government spending and borrowing rose dramatically. In Portugal, Spain, and Ireland, private debt expanded. And in all these countries, as well as Italy, the competiveness of the private sector eroded significantly, relative to Germany.

With the exception of Greece, fiscal profligacy was not the primary cause of the crisis.

In Ireland and Spain, the governments actually ran fiscal surpluses, while the private sector borrowed too heavily, inflating a housing bubble. Italy's large public debt is a legacy of a different era. By the early 1990s, the country embarked on serious fiscal consolidation, maintaining primary surpluses (i.e., the government's total revenues exceeded total expenditures, excluding interest payments on debt) between 1992 and 2008.

As the crisis intensified, however, public deficits expanded everywhere, and fears of cascading defaults by government, the collapse of the financial system, or the unraveling of the euro itself caused a broader financial panic across much of the continent, with the governments of many countries losing the ability to borrow at sustainable interest rates without support.

Over the course of the last eighteen months, the countries in crisis have put in place very tough and far-reaching reforms to address the underlying causes of the crisis.

Greece has reduced its structural budget deficit, which measures the underlying deficit adjusted for the effects of recession on revenues and expenditures, by nearly 12 percentage points of GDP since 2009, according to the IMF. Ireland, Portugal, and Spain have reduced their structural deficits by between 4.5 and 5 percentage points over the same period. In Italy, where the structural deficit expanded by much less, the government has shaved off 1¼ percentage points of GDP. Each of these governments has further plans in place to move closer to a sustainable fiscal position over the medium term.

These fiscal reforms are only part of the solution. The harder challenge is to address the erosion in competitiveness and restore reasonable rates of economic growth, a challenge made more difficult by the fact that in a monetary union, the member states do not have their own monetary policies or currencies that can adjust, and in Europe today, there is no mechanism for fiscal transfers to help cushion economic shocks.

The five countries at the center of the crisis are also putting in place measures to restore competitiveness. The Italian government has begun to implement reforms to improve the business environment, and developed plans to reform the country's labor laws. Spain has introduced reforms to increase the dynamism of its private sector. Greece, Portugal, and Ireland have also introduced a range of competitiveness-enhancing reforms, including plans for privatization, and labor market reforms and pension reductions.

And these countries are also acting to restructure and repair their banking systems. Spain is restructuring its financial sector, reducing the number of savings banks from 45 to 15. In Ireland, bank recapitalization of €70 billion is now complete and the deleveraging of the system

– which aims to reduce banks' loan-to-deposit ratios by almost 20 percent over three years – is proceeding as planned.

For these economic reforms to work, policymakers in the Euro Area will have to be careful to calibrate the mix of financial support and the pace of fiscal consolidation. The reforms will take time and they will not work without financial support that enables governments to borrow at affordable rates and keeps the overall rates of interest across the economy at levels that won't kill growth.

Economic growth is likely to be weak for some time. The path of fiscal consolidation should be gradual with a multiyear phase-in of reforms. If every time economic growth disappoints governments are forced to cut spending or raise taxes immediately to make up for the impact of weaker growth on deficits, this would risk a self-reinforcing negative spiral of growth-killing austerity.

These economic reforms have been aided by actions by the ECB, which has lowered interest rates, undertaken purchases of sovereign debt in secondary markets, and provided critical funding and liquidity support for the European banking system. Last December, the ECB introduced the three-year Long-Term Refinancing Operation (LTRO) and broadened eligible collateral. Through its two lending operations in December and February, the LTRO has allotted over €1.0 trillion to hundreds of banks.

In addition, the European Banking Authority (EBA) has conducted a series of stress tests with new disclosure requirements for the banking systems of the entire Euro Area and required banks to raise capital and take other steps to build stronger financial cushions against the economic downturn and to reflect the higher risks of the assets they hold. European banks have raised more capital, but they have also been selling assets and cutting bank lending to help meet the new capital requirements, which is adding to the financial headwinds now slowing growth.

European leaders have worked with private bondholders and the IMF to restructure and reduce Greece's government debt. Fears of a disorderly Greek default played a significant role in fueling the fires of the crisis across Europe over the past two years, and Europe's leaders have, as a result, worked to contain the risk of contagion from Greece and to insulate the rest of Europe from the impact of the solutions necessary in Greece.

This mix of economic reform and financial measures has helped calm financial tensions. The cost of borrowing has fallen sharply for Italy and Spain. Concerns about bank funding problems have eased. But Europe is still only at the initial stages of what will be a long and difficult path of reform.

The most important unfinished piece of the broader financial strategy is to build a stronger European firewall to provide a backstop for the governments undertaking reforms. The existing €440 billion European Financial Stability Facility (EFSF) has made commitments totaling €192 billion. Europe's leaders have decided to establish another fund called the European Stabilization Mechanism (ESM) to succeed the EFSF starting in July 2012. They are in the process of reviewing options for expanding the combined financial capacity of these funds so that they can make clear to financial markets that they have the financial resources available on a scale that is commensurate with future needs in the event the crisis were to intensify.

The European financial crisis has already caused significant damage to economic growth in the United States and around the world, and we have a strong interest in a successful resolution of the crisis.

The Euro Area accounts for about 18 percent of global GDP. It is a major source of financing for many emerging economies. It accounts for about 15 percent of U.S. exports of goods and services, but a larger portion of exports of many or our trading partners. When growth slows in Europe, it affects growth around the world. And when the fears of a broader European crisis have been most acute, as they were in the summer and fall of 2011 and during the spring and summer of 2010, financial markets fell around the world, damaging confidence and slowing the momentum of the global recovery.

Our financial system has relatively little exposure to the five European economies at the heart of the crisis, but we have significant financial and economic ties to Germany and France and the continent as a whole.

We have worked very closely with Europe's leaders over the past two years, and with the members of the IMF, to help support a stronger European response to the crisis.

The Federal Reserve's dollar swap lines with the ECB, the Bank of Canada, the Bank of England, the Bank of Japan, and the Swiss National Bank have played a critical role alongside the ECB's direct efforts. European banks borrowed heavily in dollars before the crisis, and many lost the ability to borrow in dollars as the crisis intensified. The Fed's swaps made it possible for Europe's banks to borrow dollars from their central banks, which has helped avoid a more rapid deleveraging, reducing the impact on financial conditions in many countries where European banks had lent heavily.

The IMF has also played an important role in Europe. The IMF has provided advice on the design of reforms, a framework for public monitoring of progress, and support for programs in Greece, Ireland, and Portugal in partnership with Europe, which has assumed the majority of the burden. These actions have helped limit the damage from the crisis to the United States and to economies around the world.

It is in the interest of the United States that the IMF is able to continue to play a constructive role in Europe. IMF resources cannot substitute for a strong and credible European firewall and response, but they can help supplement the resources Europe mobilized on its own.

The IMF has substantial financial resources available today, and it has the ability, as it has demonstrated in the past, to mobilize temporary resources if that were necessary to help contain the damage from a further intensification of the crisis in Europe. For these reasons, we have no intention to seek additional U.S. resources for the IMF. The IMF has played a critical role in every major post-war financial crisis, while consistently returning to the United States and other IMF members any resources – with interest – that it has temporarily drawn upon.

Conclusion

We are encouraged by the progress that our European colleagues have made over the last few months. We hope they are able to build on these efforts in the coming weeks and months to put in place a more durable foundation for financial stability and economic growth. We do not want to see Europe weakened by a protracted crisis. We will continue to work closely with them, and with the IMF, to facilitate further progress.

The CHAIRMAN. Thank you, Mr. Secretary.
Chairman Bernanke?

STATEMENT OF BEN S. BERNANKE

Mr. BERNANKE. Thank you, Chairman Issa and Ranking Member Cummings, for inviting me. As you know, for about two years developments in Europe have had an important influence on global financial markets and the global economy. High debt, large deficits, and poor growth prospects have led to big increases in sovereign borrowing costs, concerns about fiscal sustainability, first for Greece but subsequently for other countries, as well.

Pessimism about countries' fiscal and economic situations has, in turn, undermined confidence in the strength of European financial institutions.

This has had an impact on the U.S. economic. The European Union accounts for about one-fifth of U.S. exports of goods and services, and we have seen those exports under-perform. Of course, Europe also affects the rest of the world.

Financial strains have been evident. During times when financial conditions in Europe were the most turbulent, we saw a global retreat from riskier assets. In the United States those pullbacks from risks decreased stock prices, increased the cost of issuing corporate debt, and affected consumer business confidence. We have also seen our own financial institutions thought to have substantial exposures to Europe see their stock prices fall and their credit spreads widen.

We have seen some improvement. Financial stresses in Europe have lessened in recent months, which has helped improve the tone of financial markets around the world, including the United States. Several actions by European policy makers have contributed.

First, the actions by the European Central Bank to undertake two longer-term refinancing operations that have helped European banks lock in their funding. The European banks, in turn, have increased their holdings of sovereign debt, which has lowered borrowing costs for some countries.

Secondly, Euro area leaders, including the Greek government and private sector holders of Greek debt, have been taking steps to put Greece on a more sustainable fiscal path. With its sovereign debt significantly reduced, the Greek authorities are intensifying their efforts to implement fiscal and structural reforms and the E.U. and IMF have pledged a considerable amount of new funds as part of a second assistance package. However, the Greek economy remains in a deep recession.

The third positive step has been the approval of a new fiscal compact treaty among the members of the E.U. This treaty is an important step toward resolving the fundamental tension inherent in having a monetary union without a fiscal union, and that should help bolster the viability of the Euro area economy in the longer run.

Although progress has been made, more needs to be done. Secretary Geithner discussed some of these issues: further strengthening of the European banking system, an expansion of financial backstops or firewalls to guard against contagion in sovereign debt markets, and critically we need to continue efforts to increase economic growth and competitiveness and to reduce external imbalances in troubled European countries.

The Federal Reserve has been following these developments closely. We have been in frequent contact with key European policy makers. Our focus, of course, is to protect U.S. financial institutions, businesses, and consumers from any adverse developments occurring in Europe.

To help calm dollar funding markets and to support the flow of credit to U.S. households and businesses, the Federal Reserve acted in concert with major foreign central banks to enhance the U.S. dollar swap facilities, as has been testified to before this Committee. Use of our reestablished lines was limited until late last year; however, in late November we agreed with the ECB and the Central Banks of Canada, Japan, Switzerland, and the U.K. to extend the swap lines to February 2013 and to reduce their pricing.

The lower cost to the ECB and other foreign central banks has, in turn, allowed them to reduce the cost of short-term dollar loans they provide to financial institutions in their jurisdictions. As was noted, the swap line increased considerably and peaked at $109 billion in mid-February. This has had a very beneficial effect on easing dollar funding pressures in European and other foreign banks, which has, in turn, lowered tension in U.S. money markets, alleviated pressures on foreign banks to reduce their lending in the United States, and has boosted confidence at a time of considerable strain in international financial markets.

As market conditions have improved notably, usage of the swap lines has fallen back to currently about $65 billion.

I would add that the swaps are very safe from the perspective of the Federal Reserve and the U.S. taxpayer. They present no exchange rate or interest rate risk. Each drawing has a short maturity and must be approved individually by the Federal Reserve. They are collateralized by the foreign currencies for which the dollars are swapped and our counterparties are the foreign central banks, not the commercial banks who are receiving the dollar loans.

Fed has also worked with the FSOC and other agencies who monitor our financial institutions. Notably, U.S. financial institutions have very limited direct credit exposure to the most vulnerable Euro area countries, and U.S. money market funds have almost no exposure to those countries.

There are some exposures arising from the sale of credit default swaps and sovereign debt, but our assessment is that those are broadly edged with the CDS in the other direction, and that the counterparties to those CDS are broadly dispersed and are strong banks in Europe.

Although U.S. banks have limited exposure to peripheral European countries, their exposures to European banks and to the larger core countries is much more material. Moreover, European holdings represent 35 percent of the assets of prime U.S. money market funds in February, and those funds remain structurally vulnerable despite some constructive steps taken since the recent financial crisis.

So the risk of contagion does remain a concern for both those institutions and their supervisors and regulators. In particular, were the situation in Europe to take a severe turn for the worse, the U.S. financial sector likely would have to contend not only with problems stemming from its direct European exposures, but also with an array of broader market movements, including declines in global equity prices, increased credit costs, and reduced availability of funding.

Most recently, the Fed released on March 13th the results from our Comprehensive Capital Analysis and Review, or CCAR, which is essentially a stress test of the largest banks or bank holding companies. We imposed a hypothetical stress scenario on the banks that involved a deep recession in the United States, with unemployment reaching 13 percent, a decline in activity abroad, combined with sharp decreases in both domestic and global asset prices.

This exercise was designed to capture both direct and indirect exposures and vulnerabilities of U.S. financial institutions to the economic and financial stresses that might arise from a severe crisis in Europe. The results show that a significant majority of the largest U.S. banks would continue to meet supervisory expectations for capital adequacy, despite large projected losses in an extremely adverse hypothetical scenario.

So, in conclusion, the recent reduction in financial stress in Europe is welcome, given our important trade and financial linkages. The situation, however, remains difficult and it is critical that European leaders follow through on their policy commitments to ensure a lasting stabilization.

I believe that our European counterparts understand the challenges and risks they face, and they are committed to take the necessary steps to address those issues.

For our part, the Fed will continue to monitor the situation, work with our financial institutions and foreign counterparts to strengthen our financial system, and be ready to use the tools at our disposal to help stabilize U.S. markets should the situation require such action.

Thank you.

[Prepared statement of Mr. Bernanke follows:]

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Statement by

Ben S. Bernanke

Chairman

Board of Governors of the Federal Reserve System

before the

Committee on Oversight and Government Reform

U.S. House of Representatives

March 21, 2012

Thank you, Chairman Issa, Ranking Member Cummings, and other members of the Committee for inviting me to testify about the economic and financial situation in Europe and the actions taken by the Federal Reserve in response.

Developments in Europe and Their Effects on the U.S. Economy

For almost two years, developments in Europe have had an important influence on the tenor of global financial markets and on the global economy more generally. The combination of high debts, large deficits, and poor growth prospects in several countries using the euro has raised concerns about fiscal sustainability and, consequently, led to sharply higher sovereign borrowing costs--initially for Greece, but subsequently for other euro-area countries as well. Pessimism about these countries' fiscal and economic situations, in turn, has undermined confidence in the strength of European financial institutions, increasing the cost and difficulty those institutions have faced in obtaining funding and reducing their willingness to supply credit.

The difficulties in the euro area have affected the U.S. economy. The European Union accounts for roughly one-fifth of U.S. exports of goods and services. Not surprisingly, U.S. exports to Europe over the past two years have underperformed our exports to the rest of the world. In addition, weaker demand from Europe has slowed growth in other economies, which has also lowered foreign demand for our products.

Financial strains in Europe have also shown through to our financial markets. During times when financial conditions in Europe were at their most turbulent, investors around the world retreated from riskier assets. In the United States, these pullbacks decreased stock prices, increased the costs of issuing corporate debt, and reduced consumer and business confidence. In addition, U.S. financial institutions that were thought to have substantial exposures to Europe saw their stock prices fall and their credit spreads widen.

In the past few months, financial stresses in Europe have lessened, which has contributed to an improved tone of financial markets around the world, including in the United States. The improvement reflects, in part, a number of actions taken by European policymakers. First, measures taken by the European Central Bank (ECB), including implementing two longer-term refinancing operations and easing collateral rules and reserve requirements, have allowed European banks to lock in funding for up to three years, thereby alleviating concerns about their near-term prospects. With the benefit of this support, European banks in turn have increased their holdings of sovereign debt, contributing to lower borrowing costs for some countries.

Second, euro-area leaders, the Greek government, and private-sector holders of Greek debt are taking steps to put Greece on a more sustainable fiscal path. Its sovereign debt has been significantly reduced, the Greek authorities are intensifying their efforts to implement fiscal and structural reforms, and the European Union and International Monetary Fund have pledged a considerable amount of new funds as part of a second assistance package. The Greek economy remains in a deep recession, however.

Third and finally, leaders of most of the members of the European Union have approved a new fiscal compact treaty that strengthens fiscal rules and their enforcement. This treaty represents a positive step toward resolving the fundamental tension inherent in having a monetary union without a fiscal union, and thus should help bolster the viability of the euro-area economy in the longer term.

Although progress has been made, more needs to be done. Full resolution of the crisis will require a further strengthening of the European banking system; a significant expansion of financial backstops, or "firewalls," to guard against contagion in sovereign debt markets; and, critically, continued efforts to increase economic growth and competitiveness and to reduce external imbalances in the troubled countries.

Actions Taken by the Federal Reserve

The Federal Reserve has followed developments in Europe closely, and we are in frequent contact with key European policymakers. We are particularly focused on protecting U.S. financial institutions, businesses, and consumers from adverse financial and economic developments in Europe.

To help calm dollar funding markets and support the flow of credit to U.S. households and businesses, the Federal Reserve acted in concert with major foreign central banks to enhance the U.S. dollar swap facilities that were originally put in place during the global financial crisis and reestablished in May 2010. Use of the reestablished lines was limited until late last year. However, in late November, the Federal Reserve agreed with the ECB and the central banks of Canada, Japan, Switzerland, and the United Kingdom to extend the swap lines through February 2013 and to reduce their pricing, from a spread of 100 basis points over the overnight index swap rate to 50 basis points.[1]

The lower cost to the ECB and other foreign central banks enabled them, in turn, to reduce the cost of the short-term dollar loans they provide to financial institutions in their jurisdictions. As a result, usage of the swap line increased considerably, peaking at $109 billion in mid-February. The expanded use of the swap lines has helped to ease funding pressures on European and other foreign banks, lower tensions in U.S. money markets (in which foreign banks are major participants), alleviate pressures on foreign banks to reduce their lending in the

[1] See Board of Governors of the Federal Reserve System (2011), "Coordinated Central Bank Action to Address Pressures in Global Money Markets," press release, November 30, www.federalreserve.gov/newsevents/press/monetary/20111130a.htm. Similar announcements appeared on the websites of the other participating central banks.

United States, and boost confidence at a time of considerable strain in international financial markets. In recent weeks, as market conditions have improved, usage of the swap lines has fallen back to about $65 billion.

I would add that the swaps are very safe from the perspective of the Federal Reserve and the U.S. taxpayer. They present no exchange rate or interest rate risk; each drawing has a short maturity and must be approved by the Federal Reserve; they are collateralized by the foreign currencies for which dollars are swapped; and our counterparties are the foreign central banks, not the foreign commercial banks that receive the dollar loans.[2]

In addition to its actions to reduce pressures in global markets for dollar funding, the Federal Reserve has collaborated with other agencies--both bilaterally and through the Financial Stability Oversight Council--to monitor the potential vulnerabilities of U.S. financial institutions and to work to enhance their resilience in the face of possible shocks to the global economy. Notably, U.S. financial institutions have very limited direct net credit exposures to the most vulnerable euro-area countries, and U.S. money market funds also have almost no exposure to those countries.

U.S. financial institutions do have some gross exposure to potential losses arising from sales of credit default swap (CDS) protection referencing European sovereign debt. However, for the large U.S. dealer banks, these sales have been more than offset by purchases of protection, which would imply that in the event of a sovereign default, U.S. financial institutions would be net recipients of CDS payouts. These positions still carry some risk in that some U.S.

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[2] For the outstanding amount of dollar funding through the swap lines as it appears each week in the Federal Reserve balance sheet, see www.federalreserve.gov/releases/h41. For other relevant information and materials on the Federal Reserve's website, see www.federalreserve.gov/monetarypolicy/bst_liquidityswaps.htm. For weekly information on the Federal Reserve's swap transactions with other central banks, see www.newyorkfed.org/markets/fxswap/fxswap.cfm. Finally, for copies of the agreements between the Federal Reserve and other central banks, as well as other information, see www.newyorkfed.org/markets/liquidity_swap.html.

banks' counterparties might conceivably fail to make good on their obligations, but such risk is mitigated by the fact that the counterparties to large U.S. dealer banks for sovereign CDS trades are dispersed, primarily across large financial institutions. And in the vast majority of cases, these institutions post collateral to each other to help minimize possible losses.

Although U.S. banks have limited exposure to peripheral European countries, their exposures to European banks and to the larger, "core" countries of Europe are more material. Moreover, European holdings represented 35 percent of the assets of prime U.S. money market funds in February, and these funds remain structurally vulnerable despite some constructive steps, such as improved liquidity requirements, taken since the recent financial crisis. U.S. financial firms and money market funds have had time to adjust their exposures and hedge their risks to some degree as the European situation has evolved, but the risks of contagion remain a concern for both these institutions and their supervisors and regulators. In particular, were the situation in Europe to take a severe turn for the worse, the U.S. financial sector likely would have to contend not only with problems stemming from its direct European exposures, but also with an array of broader market movements, including declines in global equity prices, increased credit costs, and reduced availability of funding.

To address these broader risks, we have been working closely with large U.S. financial institutions. Most recently, on March 13, we released results from our Comprehensive Capital Analysis and Review (CCAR)--a supervisory assessment by the Federal Reserve of the capital planning processes and capital adequacy of large, complex bank holding companies.[3] As part of this exercise, bank capital positions were evaluated under a hypothetical stress scenario that involved a deep recession in the United States (with unemployment reaching 13 percent) and a

[3] See Board of Governors of the Federal Reserve System (2012), "Federal Reserve Announces Summary Results of Latest Round of Bank Stress Tests," press release, March 13. www.federalreserve.gov/newsevents/press/bcreg/20120313a htm.

notable decline in activity abroad, combined with sharp decreases in both domestic and global asset prices. This exercise was designed to capture both the direct and indirect exposures and vulnerabilities of U.S. financial institutions to the economic and financial stresses that might arise from a severe crisis in Europe. The results show that a significant majority of the largest U.S. banks would continue to meet supervisory expectations for capital adequacy despite large projected losses in an extremely adverse hypothetical scenario.

Conclusion

The recent reduction in financial stresses in Europe is a welcome development for the United States, given the important trade and financial linkages connecting our economies. However, Europe's financial and economic situation remains difficult, and it is critical that the European leaders follow through on their policy commitments to ensure a lasting stabilization. I believe that our European counterparts understand the challenges and risks they face and are committed to take the necessary steps to address those issues.

For our part, the Federal Reserve will continue to monitor the situation closely, work with our financial institutions and foreign counterparts to enhance the resilience of our financial system, and be ready to use our tools to help stabilize U.S. markets should the situation require such action.

Thank you. I would be pleased to respond to your questions.

The CHAIRMAN. Thank you.

I will now recognize myself for five minutes.

Chairman Bernanke, in that stress test you, I presume, assume that the Fed systems, including the credit default swaps that are back nation to nation, would work; is that correct? You weren't assuming a collapse of all of the $1.4 trillion exposure?

Mr. BERNANKE. We didn't assume they would work. We checked to make sure we were comfortable with the counterparties.

The CHAIRMAN. But that means you graded yourself as that part working, correct?

Mr. BERNANKE. I am not quite sure what you are asking. We looked at the CDS positions of the banks and we verified first that they are largely hedged against sovereign default in Europe first. And then secondly we looked at the counterparties of those credit default swaps and assured ourselves that they are widely dispersed and represent the strongest financial institutions.

The CHAIRMAN. Like AIG did a couple years ago?

Mr. BERNANKE. AIG is an example of what we don't see now. AIG was not appropriately regulated. It was not appropriately hedged. It didn't have sufficient capital behind those CDS. We know there is nothing like that——

The CHAIRMAN. So you are comfortable today that there are no AIGs hiding in the woods, no FP sitting in some small company in London that essentially is at the bank without us knowing it?

Mr. BERNANKE. Well, our stress test has covered all the largest bankholding companies in the U.S. We have looked also at other large banks, with a somewhat less stressful but somewhat different approach, but within that whole range of U.S. bank institutions we don't see any similar problems.

The CHAIRMAN. Thank you. One of the most important parts of today is to ask the questions that weren't asked in earlier times before what couldn't happened occurred.

The Eurozone has an economy we will call nominally our size. It has a depth, if I am roughly right in the Euro conversion, of about $14 trillion of sovereign debt. Some countries actually have positive, but we will just look at their sovereign debt across the board.

So it is fair for the American people, not being talented economists, but for the American people to say same size entity, similar debt to ours, not exact but similar. If that is the case, why is it that they are not being treated, and this is a question for the American taxpayer, if you will, being treated much more like we treat our States? California doesn't look to Greece or Germany for a bailout. They could look to the United States Federal Government. In other words, we are internal.

What is the justification for the American people to understand of a zone similar size to ours, similar wealth to ours, similar debt to ours, looking around at the rest of the world and saying, what part will the United States put into a European Union member such as Greece's problem?

Mr. BERNANKE. Your question highlights the difference between Europe and the United States which is we have a fiscal union as well as a monetary union, and, as you point out correctly, the reason that we don't see the same kind of stresses at the State level is because implicitly there is support from the Federal Government for the rest of the Country.

The CHAIRMAN. But for the taxpayer, and I want to get to Secretary Geithner, too, for the taxpayer, if they are very similar to us in the positive side, human beings move freely within the Eurozone. Money moves freely. Most of the Eurozone is a single currency and, in fact, they basically act, from a winning standpoint, as a protective trade partner. They treat each other in a way they do not treat us. Period. We simply do not enjoy the advantages of selling into the Eurozone, that the Eurozone enjoys throughout the European Union.

So the question is, for the American people, and by the way, this is not a question of why are we doing it in our own self-interest. I understand we are doing it in our own self-interest, too. But the question is, why is it that the Eurozone isn't being asked by our Government to step up much more and take more responsibility? Why is it that it comes to the American people at all?

Not why is it in our best interest, but why does it come to the American people when, in fact, they have the same wherewithal, and when they are trading with each other they trade like States, but when they have a problem with a rogue nation or two or three or four they turn to the IMF and other external forces in which we participate?

Mr. BERNANKE. It is a good question. Our position, and perhaps the Secretary can speak to this from the Administration's point of view, the position of the United States has generally been that Europe needs to really step up and do a lot more. We have been encouraging them to strengthen their firewalls, strengthen their fiscal compacts, and essentially to move in the same direction as the United States is currently structured.

The CHAIRMAN. And Mr. Secretary, as I go to you I want to say this because, as you said in your statement, we have never lost a penny to the IMF. We have been fully repaid. Some might say that the interest has not always been what we would hope it to be, but, in fact, it has been a good bet overall for the world economy. But the American people are wondering what I asked, and I hope you can give it to us in a way.

The follow-up question I will give you in advance, which is, doesn't it strengthen Europe's hand when we make it clear that the American people are essentially saying no, and you are going to have to convince us if you need large amounts of money. You are going to have to convince us to go against what is, in fact, a populist feeling within Mr. Cummings' community and mine, as well.

Secretary GEITHNER. We have a very similar view to the view you expressed. Europe is a very rich continent. Absolutely has the means to solve this on their own. And you are right to point out that because they are a monetary union without a fiscal union they don't have the mechanisms we have in the United States, not just the discipline, the borrowing behavior of our States which we have, but we have a set of fiscal transfers that are very powerful in the United States to soften the downturns that individual States might face.

The IMF is an institution where its members have a right to request assistance, and if they are prepared to meet the conditions that the IMF establishes, then they have the right to request that assistance. And our judgment has been that it has been in the interest of the United States, and fully consistent with its institution, and certainly better for us as a Country for the IMF to play a modest supplemental role alongside the much more dominant financial role of the European authorities going forward, and where they have asked us the IMF to take more of the burden we have said no, we don't think that is appropriate.

So we are taking very much, I think, the course you would take and most Americans would say which is they are a rich country, and, in fact, nations around the world are taking a similar view, which is let's make sure people understand for their strategy to work the world needs to see Europe, that very rich continent of Europe, demonstrate that they are prepared to do what it takes to make this work. And we can help with advice and some support in the margin. We are not going to do that in a way that puts the American taxpayer at risk, and we are not going to do it in a way that shifts the burden of solving their crisis to the American taxpayer.

The CHAIRMAN. Thank you.

Mr. Cummings?

Mr. CUMMINGS. Thank you very much, Mr. Chairman.

Secretary Geithner, Europe has a housing crisis, does it not?

Secretary GEITHNER. Parts of Europe do.

Mr. CUMMINGS. And so to restore our economy you would agree that housing has to be addressed. Do you believe that, the foreclosure situation that we are going through right now?

Secretary GEITHNER. I do think that obviously our economy, as I said, is still suffering from a lot of damage, collateral damage fallout from our crisis. You see that in housing, not just in high unemployment. And our judgment is that we should do everything we can to help repair that damage, and that would make the economy stronger over time. That is what we are trying to do.

Mr. CUMMINGS. Now, the House Republicans released a budget proposal this week that would lay a course that would cut more than $5 trillion in Medicare as we know it, shift the cost of health care to seniors, slash education, research, and infrastructure funding. Chairman Bernanke, you and I have talked about this a number of times. You gave a speech back in 2008 in which you said principal reductions that restore some equity for the homeowner may be a relatively more effective means of avoiding delinquency and foreclosure; is that right?

Mr. BERNANKE. Our research shows that sometimes it can be effective. Yes.

Mr. CUMMINGS. And Secretary Geithner, you also agree that principal reduction can be a critical tool if it is well designed; is that right?

Secretary GEITHNER. Yes, in some cases. That is why you see private investors and private banks on their own, in many cases, offering principal reduction to their borrowers.

Mr. CUMMINGS. How does Europe deal with this foreclosure situation?

Secretary GEITHNER. There is actually a very limited number of countries in Europe with quite that same mix. They are taking somewhat different approaches, but where they are different it is different because the nature of the problem is different in those cases. You can't see a common approach across the continent on the housing front yet. And I think it is fair to say they have not been as aggressive as we were in trying to move early to try to repair the damage in the housing market.

Mr. CUMMINGS. Mortgage banks across the Country already are doing principal reduction because they count their bottom line. They want to keep people in their homes paying lower mortgages instead of foreclosing and getting nothing at all. This helps the homeowners and shareholders.

The only official who does not share this view appears to be Ed DeMarco, the acting director of FHFA. Chairman Bernanke, his opposition is strange because his own data which he provided to us earlier this year shows that principal reductions would save the United States taxpayers billions of dollars compared to foreclosures. His data also shows that principal reductions would help the homeowners.

So based on his own data and based on the law Congress passed to create FHFA, Mr. DeMarco should be doing principal reductions now but he has refused.

Now, Secretary Geithner, I know that you are in negotiations with Mr. DeMarco and the Treasury has now offered triple incentives for principal reductions. Can you tell us why Treasury is doing that and why are these incentives important?

Secretary GEITHNER. I should point out that under the law the Treasury did not have any authority to compel the FHFA to undertake the activities. Under the conservatorship mandate they have to make sure they meet a very tough test, appropriately so, to make sure the things that they are doing are in the interest of reducing losses to the taxpayer, maximizing overall returns to the taxpayer.

But there are certain cases where we think there is a pretty strong economic case for principal reduction as part of a strategy to limit the future losses to the GSE. So we have been having some discussions with him about how to narrow the differences between us. But he will have to make these choices, and I think maybe on this question it would be better for me to come back and talk to you in more detail about it separately. Maybe in a couple of weeks we could give you a better sense of where he is going to come out.

Mr. CUMMINGS. Very well. In his letter to us he has said, so that you will have this when you talk to him, he said administrative costs would be too high to address his IT systems. Then he went on to say, and he has made that argument to you, I assume, has he not?

Secretary GEITHNER. He has, but again, I think he is in the process of looking again at those questions, as are we.

Mr. CUMMINGS. Yes. And so your response was look further?

Secretary GEITHNER. Yes. Again, we both have the same basic interest, which is we want to make sure that those institutions are doing things to not just help repair the damage in the housing market, but are doing so consist with their obligation established by Congress to make sure they are doing things that would limit the risk of future losses to the taxpayer.

Mr. CUMMINGS. Finally, Secretary Geithner, let me ask about the stakes here. Mr. DeMarco controls all of the loans guaranteed by Fannie Mae and Freddie Mac. How many families would be affected by his decision? Hundreds of thousands, I would think, or millions potentially.

Secretary GEITHNER. No, not millions. It is hard to tell. I know it is not part of the popular wisdom, but the GSEs were actually more conservative and more careful in their underwriting standards in the loans they took, and so the broader quality of their loans is actually better than the broader market in this context. But again, our job is to try to make sure that we are doing everything that we can to reach as many people as we can, where we think there is a good, strong case for the Country on the merits, not just for the taxpayer.

The CHAIRMAN. I thank the gentleman. The gentleman's time has expired.

Mr. Secretary, we will also send you a copy of the field hearing information from Brooklyn, which actually has Fed and other representatives' testimony to that point so that you are briefed before you come back to the Ranking Member.

With that we go to the chairman of the full Committee, emeritus, Mr. Burton, for five minutes.

Mr. BURTON. Is that what you call me?

The CHAIRMAN. Emeritus is a forever term, as is chairman around here.

Mr. BURTON. I got it.

The CHAIRMAN. Please, Mr. Chairman.

Mr. BURTON. According to CRS, the exposure that the United States has in Portugal as of September of last year was $54 billion, Ireland was $111 billion, Italy $310 billion, Greece $48 billion, Spain $244 billion, Germany $635 billion, and France $685 billion, for a total of $2.08 trillion.

I am concerned about what happens if the Euro starts to devalue and how it is going to affect the United States' ability to collect on the indebtedness that we are having with Europe.

My first question is, and I will combine some of these questions so you have more time to answer, we are printing money, have been printing money with QE1 and QE2 and I presume this may be continuing. Is there a mid-or long-term cost to loaning money that we have printed to Europe? And how much will that be?

The Federal Reserve has created this foreign currency swap mechanism and it has outstanding loans, as I said earlier, as high as 1.2 trillion. I understand you say now it is only 65 billion. But nevertheless, that is a considerable amount of money.

I would still like to ask what happens if you do have some defaulting over there and they can't repay those loans. I know the European Central Bank is printing money right now. That will cause some kind of inflationary pressures, as well. What will that do to the indebtedness that we have?

The foreign currency swaps takes our money and exchanges it for Euros. I presume we are getting the money from the money we are printing. I would like to have the answer to that.

And it appears as though we are providing dollars that are loaned to or swapped with Europe, and then it is used to buy European Central Bank bonds that are then lent to commercial banks. I believe that is correct. If that is the process, it sounds like we are cooking the books to make this all look legitimate.

Finally, I have been to a number of these countries, and the unrest is very apparent. Some of our European neighbors have not passed austerity measures, and even when they had passed some of these reforms you still have an awful lot of dissention in the countries. They have had changes in those governments. I think there is still a big question whether or not Greece can survive and maybe Italy, Spain, Portugal and so forth.

So to what extent are we exposed if this so-called European recovery does not take place? And can you give us the figures or at least roughly the figures, both directly and indirectly, as far as the exposure is concerned? And do your numbers include foreign currency swaps or other assistance from the Federal Reserve or the Treasury?

I know that is a lot, but if you could kind of run through that I would appreciate it.

Mr. BERNANKE. May I respond?

Mr. BURTON. Sure.

Mr. BERNANKE. On the swaps, as you said, the maximum was $109 billion. It is down to $65 because it has been very constructive and it has helped improve the market. It has been beneficial to the United States, as well as to Europe.

If the Euro devalues or depreciates, it has no affect whatsoever in our value of our liability because we get paid back in dollars, so the European Central Bank takes any foreign exchange risk. If the banks that they lend the money to don't repay, we still get paid back in full because the ECB also takes all the credit risk. So we are not taking any credit risk, we are not taking any foreign exchange risk. The chances of losing any money is very, very low and the benefits are quite significant.

On exposure, you mentioned some numbers. I wasn't clear whose exposure you were talking about, but let me just say briefly that obviously our banking system is exposed to Europe. They are a major trading partner and we have many investments there. But it was exactly what we tried to do in our stress test scenario that we just released the results last week. We considered a very severe scenario that included a sharp new recession in the United States, a sharp decline in activity in Europe, major financial stress, including 50 percent drop in stock prices, so all of this is sort of an attempt, at least in part, to measure the impact in our banking system of a new crisis in Europe.

Of course, there would be significant losses, but what we found was that all the banks essentially were able to meet a reasonable level of capital, even following the losses associated with such an event. The losses would be large, of course.

Mr. BURTON. Thank you, Mr. Chairman.

The CHAIRMAN. I thank the gentleman.

The gentleman from Illinois, Mr. Quigley.

Mr. QUIGLEY. Thank you, Mr. Chairman.

Gentlemen, I guess the academic question is that balance that I talked about in my opening statement about austerity measures and how they impact recovery. Your view in general on that issue, and how the European plan seems to strike that balance, or how effectively it might do that? Either or both of you, please.

Mr. BERNANKE. Well, I think the answer to your question depends on which country you are talking about. I mean, there are countries like Greece, Ireland, and Portugal which are currently under European Union, Eurozone, and IMF support, which have essentially no alternative but to do whatever they can to reduce their fiscal deficits, and they have been trying to do that, although the slowing in growth has made it more difficult.

More broadly, there are some countries that have some fiscal space, as it is called, and there they might consider a balanced approach which leaves some flexibility in the short-term to deal with the fact that Europe is slowing, their economy is slowing, at the same time addressing longer-term fiscal issues in a comprehensive, long-term plan which, for example, they are trying to do through their fiscal compact. So that is analogous to an approach the United States might take, which is a comprehensive plan that has both a short-term and a long-term component to it.

Mr. QUIGLEY. Okay.

Secretary GEITHNER. I think the chairman said it exactly right. You have to distinguish the countries that lost the ability to borrow on their own without support from those that still have that capacity. In general, for the countries not still in the acute stage of crisis, you want there to be a medium-term plan to gradually phase in the reductions and deficits that have to come, and you want that to be balanced and complemented by reforms that are focused on trying to improve the growth performance of the economy, make it easier to start a business, things like that. It is very important to get that balance right.

As I said, it is going to take a bunch of financial support to make sure those reforms have time to work, and you want to make sure they are phased on gradually over tim, and you want to avoid the risk that, again, every time growth disappoints and therefore the short-term effects in the deficit or increase the deficit, you want to avoid the risk that that has to be matched by immediate cuts in spending or tax cuts or tax increases, because if you do that the risk is you add to the challenge on growth and harder to dig you out of this problem. So that is the balance I think you want to have.

Mr. QUIGLEY. And how did they do? I mean, how are they doing? If you want to talk about the countries that are more acute, like Greece and Italy and others, how did they do striking this balance? How optimistic are you? The concern is if we are so dependent on their recovery, and perhaps we can learn some lessons there, did they go too far with these countries that are really hurting and stymie the opportunity for recovery?

Secretary GEITHNER. I don't believe you can say that in Greece and Ireland and Portugal because, again, once you get to that point there is really no choice, no alternative available to them except to do this mix of very tough reforms across the board.

The other countries in Europe are in a different position. They have a bit more time and space to bring a bit more care and balance to the path.

Of course, Greece and Ireland and Portugal are very small economies, even aggregate, in that context. What hurts the United States is the risk of a longer period of weak economic growth in the major economies in Europe, and that is why it is so important that, as they calm the financial tensions across Europe, that they are able to shift some of the attention, some of the focus in Europe to broader strategies that would make growth stronger across the continent.

Mr. QUIGLEY. And your overall assessment, their chances for recovery, why are they perhaps less optimistic, or you are less optimistic or more optimistic about what Europe faces versus the U.S.?

Secretary GEITHNER. I think the fundamental reality of Europe is that this is going to take a very long time for them to work through, and I think just realistically looking at the prospects ahead, even if Europe is able to be successful in avoiding a catastrophic financial crisis and they have the means to do that, even if they are successful in avoiding that, then the risks are that Europe is still growing, on average, at very weak levels, and that will mean that growth in the United States is weaker than it otherwise would be.

Again, this process has a lot of risk in it, very fragile, lot of political challenges in this, as your colleagues have said. That is why it is so important that they are doing everything they can, not just to restore some financial stability, but help lay a foundation for stronger growth, and it is why we have such a compelling economic interest in trying to work with them to help make that happen.

Mr. QUIGLEY. Thank you. My time has expired.

The CHAIRMAN. Thank you, Mr. Quigley. A very good line of questioning.

With that, we go from the chairman of the Subcommittee to the Ranking Member of the Subcommittee, Mr. McHenry, for five minutes.

Mr. MCHENRY. Thank you, Mr. Chairman.

Thank you both, Secretary Geithner and Chairman Bernanke, for your service to our Government. You certainly have both served in some challenging times, not just in the last three years but over the longer run, as well.

Chairman Bernanke, I just want to ask about your legal authority, the Fed's legal authority. So the Fed can purchase sovereign debt of the United States, and has. Does the Fed have legal authority to purchase other countries' sovereign debt?

Mr. BERNANKE. It does for the purposes of reserve holdings, and we currently hold a relatively small amount of debt of very high quality. I think it is France, Germany, and Japan. But we are not engaging in purchasing debt of troubled countries.

Mr. MCHENRY. But that could be considered?

Mr. BERNANKE. We are not considering it.

Mr. MCHENRY. Okay.

Mr. BERNANKE. Congress made clear in earlier discussions some decades ago when this issue came up that the purpose of this authority was to maintain foreign exchange reserves. I don't think that it was the intent of Congress that we get involved in sovereign debt issues. It is not our intent to do so.

Mr. MCHENRY. But beyond that, does the Fed accept as collateral for foreign debt sovereign debt of foreign countries?

Mr. BERNANKE. Well, some of the debt we simply own as part of our foreign exchange reserves. In other cases we have various kinds of short-term repurchase agreements and other kinds of arrangements where we do take collateral for a short period. Again, we are making sure that we have sufficient hair cuts and so on to make sure that we are comfortable with the safety of those short-term arrangements.

Mr. MCHENRY. Okay. Thank you.

Secretary Geithner, I have a few questions about the International Monetary Fund. Within Treasury you have a designee who serves on the 24-member executive committee of the IMF. In terms of the actions taken with the recent IMF loan to Greece, were you involved in that process? Was that a discussion you were engaged in?

Secretary GEITHNER. Absolutely. We are the largest shareholder in the IMF, and so we pay a lot of attention to any decision, any meaningful decision the IMF makes in that context.

Mr. MCHENRY. Okay. Now, looking at that, is the Treasury, I know you have mentioned this before, but I just want to raise the issue again. Are you considering additional contributions to the special IMF European bailout fund?

Secretary GEITHNER. No, we are not. Our judgment is that the IMF already has $400 billion of available resources it can use if necessary to help support the needs of its members. Europe, of course, has very substantial financial capacity to put behind their strategy to resolve this crisis, and therefore we do not see the case for coming to Congress and asking for more authority in this context.

Mr. MCHENRY. Okay. Now, is the Treasury considering being involved in the IMF's NAB, the new arrangement to borrow facility?

Secretary GEITHNER. We are in that already. Congress has authorized us to participate in that, so yes, when the IMF draws on the new arrangements to borrow, which is like a supplemental pool of resources, then yes, like when the IMF draws on its quota resources, we do participate in those drawings. As I said, we have 60 years of experience with how the IMF acquits itself in that context, and the record supports our judgment that there is very substantial strong financial safeguards that protect the interests of the U.S. taxpayers in that context.

Mr. MCHENRY. Under Dodd Frank, and I know you have been support of this, a number of provisions in there, one in particular dealing with the IMF. When our designee, your designee and our Country's designee to the IMF, engages in a decision to the IMF to loan money to a country that has greater than 100 percent debt-to-GDP ratio, they have to present Congress with the understanding of why they made this decision and what the credit risk is. Is that being done?

Secretary GEITHNER. Absolutely. Of course, there is a rich history, a long history of Congressional mandates on the votes we can cast in the institution. That is one of the more recent ones, and we will meet the test to that provision.

Mr. MCHENRY. And it is a 30-day provision, so we would expect that within the next three or four weeks in front of Congress, the decision-making there.

Secretary GEITHNER. And the way that provision is structured, as you said, in some circumstances where the existing level of debt in the country is high, there is a higher burden on all of us to make sure that the reforms that come with this assistance give us a reasonable prospect that it is going to be improving the path to sustainability.

Mr. MCHENRY. Well, we look forward to that report. Thank you.

The CHAIRMAN. I thank the gentleman.

Just to clarify for the record, if I heard correctly, the IMF doesn't maintain a whole pile of money. They maintain the ability to draw by the members, based on an allocation. So for the American people to understand, you are not coming to us for new money, but there will be distributions at times within the current limit that just occur as a result, a trigger so that they don't sit there with all our money, but the fact is they will be taking our money; is that correct?

Secretary GEITHNER. You are exactly right. The way the law of the land is structured, we can't lend money to the IMF without the authorization of the Congress of the United States. Congress authorizes the scale of the financial commitments we can make. What happens is, as members ask the IMF for resources, they meet the IMF's conditions and can draw on those resources, then we provide a part of those resources. But again, the exposure we take is backed by not just a substantial amount of IMF gold, but a set of other financial safeguards so our interests are protected.

The CHAIRMAN. I thank the gentleman.

The gentleman from Virginia, Mr. Connolly.

Mr. CONNOLLY. Thank you, Mr. Chairman.

Welcome to both of our guests this morning.

Mr. Geithner, you noted in your testimony that Ireland and Spain actually ran large fiscal surpluses, yet they were victims of financial crisis contagion. You also noted that Spain reduced its structural deficit through austerity measures since the onset of the crisis.

Do you believe that there is some lesson in that? I would have guessed that, in order to have this kind of crisis, both Ireland and Spain would actually be deeply in the hole of debt. How did that work?

Secretary GEITHNER. Well, you are right. I think the popular perception is that the crisis in Europe is overwhelmingly the result of decades of fiscal profligacy, and that is not really quite right. It was certainly true in Greece where, following the advent of European Monetary Union, Greece did substantially expand how much it borrowed, and the government grew as the size of the economy to unsustainable levels.

Mr. CONNOLLY. I am going to come back to Greece.

Secretary GEITHNER. In those other countries what you saw was a very large rise in private borrowing in the banking system and by the private sector, huge rise in private debt as a share of the economy, and a damaging loss in the relative competitiveness of their businesses relative to Germany in that context. And when the crisis hit and confidence eroded, their fiscal positions did deteriorate dramatically, as always happens in that context. But the fundamental cause of the crisis was not a long period of extreme fiscal profligacy.

Mr. CONNOLLY. Mr. Bernanke, one of the medicines recommended here obviously is draconian fiscal austerity measures. We have a new budget out yesterday that certainly subscribes to that philosophy. Many European countries actually adopted that policy in terms of austerity measures. Did those economies grow faster or slower than the United States since 2009?

Secretary GEITHNER. Well, the economies of Europe, with the exception of Germany, to some extent, have grown significantly slower than the United States over this period of time, partly for the reasons you said. Their crisis was more acute than ours. They are in the earlier stage of adjusting to it. They reacted more tentatively and with less overall force than we did in the United States. And for those reasons and the scale of the challenges they faced beforehand, growth has been weaker in that context.

I think the basic lesson in this context is yes, you want to be very careful to try to balance the imperatives of restoring fiscal sustainability with the recognition that ultimately both long-term fiscal sustainability, not just the immediate health of your economy, depends on your ability to get the economy growing again.

Mr. CONNOLLY. One of the comparisons that often is cited by some even here in this body is that the United States, if it is not careful, given its debt posture and its lack of fiscal discipline, is going to look alarmingly like Greece. I personally find the comparison invidious, and upon any examination lacking in any serious comparison, given the fact, I refer, for example, to Michael Lewis' book on the European crisis, it is shocking what went on in Greece. They did not have macro economic data that was reliable. They actually engaged in outright deception when E.U. officials came to examine the books. They didn't know how much debt they had. They didn't have any kind of central control over their own economy at all, unlike the United States.

But I would like each of you, if you would care, to comment on that comparison. Is the United States headed toward going down the road of Greece?

Mr. BERNANKE. Congressman, it is certainly true that situations are not directly comparable. First, Greece's debt trajectory looks a lot worse than ours or that of other industrial countries. Secondly, the economy is a small, less-diversified, less-strong economy in general, less competitive. And their short-term issues cannot be ameliorated by an independent monetary policy since they are part of the Eurozone. So there are some very important differences.

That being said, I think we all understand that there are long-term fiscal sustainability issues in the United States, and what we need to do is find a strategy that will credibly and convincingly put us on a path towards long-term sustainability without doing undo damage to the recovery.

Mr. CONNOLLY. Thank you, Mr. Bernanke.

Secretary Geithner?

Secretary GEITHNER. Yes. No basis for comparisons with Greece. It is important for people to recognize that our fiscal position, long-term fiscal position, is actually we are in a much stronger position than the continent as a whole, and it is partly because our economy will grow faster than Europe's over time. It is partly because we are a younger country. It is partly because the commitments we have made to health care and retirement security, even if unsustainable, are much less generous than is true in Europe, as a whole. And those factors and the ones that the chairman mentioned mean that we are in a fundamentally different position, a more comfortable position.

But of course, in the United States, as well, we have made unsustainable commitments. Our deficits are unsustainable over the long run. We have a little bit more time and substantially more room for maneuver in how we address those. And very important as we address them, and we need to address them. We can't put them off indefinitely, we do so in a way that achieves the necessary balance between helping the economy repair the damage from a terrible crisis, making sure we can invest in things we need to grow, but still restoring us some gravity to our long-term fiscal positions.

Mr. MCHENRY. [Presiding] The gentleman's time has expired.

Mr. CONNOLLY. Thank you.

Mr. MCHENRY. Mr. Gowdy from South Carolina is recognized for five minutes.

Mr. GOWDY. I thank the gentleman, Mr. Chairman, from North Carolina.

Mr. Chairman, is there an interconnectivity between cost of energy and economic recovery?

Mr. BERNANKE. Yes, there is, particularly when there is a supply side element, which there appears to be, given some reductions in available supply and tensions in Iran and so on. Higher energy prices create at least short-term inflation pressures. Moreover, they act as a tax on household purchasing power and reduce consumption spending, and that also is a drag on the economy. So yes, higher oil prices, higher energy prices, are a concern.

Mr. GOWDY. And I think the price per gallon in Europe is about double, if not more, than what it is in the United States.

Mr. BERNANKE. Yes, because of much higher taxes.

Mr. GOWDY. So can you imagine any scenario under which someone would advocate for boosting our price per gallon to European levels?

Mr. BERNANKE. There are a lot of policy issues relating to that.

Mr. GOWDY. I mean an economic reason, not environmental, economic.

Mr. BERNANKE. Well, the question is whether or not there are other goals that are served: environmental goals, congestion goals, and the like.

Mr. GOWDY. I am just asking from an economic standpoint.

Mr. BERNANKE. From a purely GDP growth perspective, I think higher energy prices would probably slow growth, at least in the short run.

Mr. GOWDY. Well, what word would you use to describe it if our price per gallon talismatically doubled?

Mr. BERNANKE. That would have a——

Mr. GOWDY. Catastrophic?

Mr. BERNANKE. I wouldn't say catastrophic, but it would have obviously a very negative effect on consumers, consumer confidence, consumer real incomes, at the same time that it would push up inflation.

Mr. GOWDY. Thank you.

Mr. Secretary, what is our debt as a percentage of GDP currently?

Secretary GEITHNER. I can give you the precise numbers in writing, but as we measure it, which is——

Mr. GOWDY. I am not going to hold you to a precise number. Just something round that a lawyer can understand.

Secretary GEITHNER. As we measure it, which is debt held by the public, and we try to measure it net of financial assets, which is the appropriate way to do it financially, our debt-to-GDP ratio is somewhere between 60 and 70 percent of GDP today.

Mr. GOWDY. All right. Since I have been here there has been one request for an increase in the debt ceiling. I understand there is another one coming. I don't know whether it will come before the first Tuesday in November or after the first Tuesday in November. I want you to assume, and, again, I am not going to hold you to the number. You don't need to go research it. You are smart enough. I have seen you testify before enough to know that you probably will be able to answer this question off the top of your head.

If this were the last debt ceiling increase you could ask for, the final one, and you had to make it large enough for all current and future obligations, what would the request need to be?

Secretary GEITHNER. I don't know how to answer that question. Let me answer it slightly differently. It makes no sense for the Country, since Congress controls how much we can borrow every year, we have no independent authority to spend beyond what Congress authorizes, for Congress to put itself and its Members in the position every six months or every year to hold a separate vote, politically difficult vote, on whether they should continue to authorize us to do things they have already authorized us to do. But I don't know how to answer that question, because you are talking about the future. The best way to——

Mr. GOWDY. Well, the last debt ceiling increase was for how long and for how much?

Secretary GEITHNER. Well, under the deal we reached last August, we set up a mechanism, I believe, where Congress imposed on itself three votes over a 15-month period.

Mr. GOWDY. What will be the amount of the increase in November or December?

Secretary GEITHNER. Well, it depends. Congress makes this choice, and Congress has to make the choice based on how much time they want to give themselves.

Mr. GOWDY. Right. But you have seen the numbers. In fact, I made a note. You used the exact same word that Chairman Ryan uses. And I hope they don't run any ad showing you pushing a senior citizen off a cliff in a wheelchair for using that word, but you just used the word unsustainable.

Secretary GEITHNER. Right.

Mr. GOWDY. So my question to you is: if we had one more chance to borrow all the money that we need, assuming current variables, how big would that number have to be?

Secretary GEITHNER. I don't know how to answer that. I think that if you—let me try this a little differently. You will have to decide, as a Member of Congress, how much time you want to give Congress before you have to vote on it again, and you can choose that amount of time. The larger the number you create, but again, the debt limit doesn't decide how much we can borrow. You decide how much we can borrow, because every year you decide what you can authorize.

Mr. GOWDY. How much debt would we need to meet current and future obligations, assuming the status quo indefinitely?

Secretary GEITHNER. I would be happy to give you that in writing. I can't do it in my head.

Mr. GOWDY. How about a round number?

Secretary GEITHNER. No idea. But if your question is if Congress authorized no additional increase in spending or revenues——

Mr. GOWDY. Right.

Secretary GEITHNER.—forever, how much we would have to borrow? I can do that question in math, but I have to——

Mr. GOWDY. Twenty trillion?

Secretary GEITHNER. I just can't do it in my head.

Mr. GOWDY. Fifty trillion?

Secretary GEITHNER. I don't know.

Mr. GOWDY. I have seen you work before. You are smart. You are quick.

Secretary GEITHNER. I am not smart enough to answer that question.

Mr. GOWDY. A lot? Can we agree it would be a lot?

Secretary GEITHNER. It would be a lot. It would make you uncomfortable.

Mr. GOWDY. Right. Thanks.

Thank you, Mr. Chairman.

The CHAIRMAN. It would make you uncomfortable. Interesting transition.

Ms. Holmes Norton is recognized for five minutes.

Ms. NORTON. Thank you, Mr. Chairman.

And thank you, Secretary Geithner and Chairman Bernanke, for being here.

Every country and every culture, of course, is very different, and it is very risky to go looking at cultures, whether it is Greece or some culture or country that you perhaps admire. I do want to ask you about Germany. There are some in the Congress who believe that the way out of our present recession and dilemma is to impose draconian cuts repeatedly, even forsaking the budget deal that was very difficult to reach, was reached at a huge sacrifice, the loss of our triple-A rating.

I look to Europe, this was a worldwide recession, and look at the difference among the various countries. The British seem to have adopted something of that approach, approach to emphasize retrenchment over growth. I am intrigued by Germany, everybody's favorite example of the strongest economy in Europe, perhaps the strongest in the world today, and do not understand and believe we need to come to grips with the theory that they have embraced during this recession. They are one of the few countries in Europe not to cut the budget deficit. I take it it wasn't terribly out of control but I don't know. I am going to ask you. In fact, they have added to their deficit, certainly in 2009 and 2010, one of the few countries in Europe to do so.

I am truly intrigued by a country that did not abandon its working class, did not abandon its social net, has a national policy that is maintained of keeping unemployment low. I know they have some things that are culturally oriented toward them, like work sharing and the rest. They also, of course, subsidize employers to keep people on the job. We do that in a scattered fashion.

But I believe we have to come to grips with why this country continues. It is a country that we identify we so closely. We need to come to grips with their model and how they do it, so I have to ask you, how has Germany maintained its strength, continued to grow, without cutting its budget deficit?

Mr. BERNANKE. Let me take a first stab at that. Germany has achieved quite a bit. When they had reunification a couple of decades ago, there were significant problems with the competitiveness and efficiency of their industries, trying to integrate the two parts of Germany together, and so on. And they made a very sustained and successful effort to increase the competitiveness and efficiency and productivity of their industry, which is all to their credit.

In addition, though, as part of the Eurozone, they have benefitted quite a bit from that arrangement. First, because they have sort of an export market that they have easy access to, and, secondly, because the Euro, which reflects an average of the economic strength of the different parts of the Eurozone, is probably weaker than a Deutschemark would be, which means that they have something of a currency advantage to some extent in their ability to export.

Ms. NORTON. Just like we have a currency advantage.

Mr. BERNANKE. I don't know about that.

Ms. NORTON. Not today, all right.

Mr. BERNANKE. This is more or less permanent, I think.

Ms. NORTON. Go ahead.

Mr. BERNANKE. As you point out, they also had work sharing policies, which in this particular case it is a question whether that is a good strategy in general, because sometimes it could promote inefficiency because there is not movement of workers between different industries and so on, but——

Ms. NORTON. Of course, nobody claims that the Germans are inefficient. Go ahead.

Mr. BERNANKE. In this particular case, they avoided some of the sharp layoffs we saw in the United States, and their unemployment rate remained lower. In fact, it is lower today than it was before the crisis. That in turn meant that their fiscal stresses haven't been as great as some in the United States or some other countries.

So they have had a number of things supporting their economy, and certainly they deserve credit for their improved competitiveness. But it is the case that not every country in the world can be a major exporter. Somebody has to buy. So that model is not necessarily exportable in itself to every country in Europe.

Mr. McHENRY. The gentlelady's time has expired. Mr. Turner from Ohio.

Ms. NORTON. Could I ask for a second——

Mr. McHENRY. The gentlelady's time has expired.

Ms. NORTON. I have wanted to hear from——

Mr. McHENRY. The gentleman from Ohio, Mr. Turner, is recognized for five minutes.

Mr. TURNER. Thank you, Mr. Chairman.

Secretary Geithner, the title of this hearing is Europe's Sovereign Debt Crisis, Causes, Consequences for the United States, and Lessons Learned. Focusing on that portion of lessons learned, I have a concern as we look to the issue of Europe that stems from my concern from the bailout process that has gone through in the United States. Largely, as we look to what occurred in the U.S. with bailouts, I think many people like me have a significant concern of conflicts of interest, issues of lack of transparency, and a lack of openness.

Mr. Secretary, as we look to the auto bailouts you served in three different roles. You served as the Secretary of the Treasury, looking at issues of the taxpayers' dollars, and exercising the ownership interest of the United States to the extent the United States became an owner frequently in the auto bailouts. You served as co-chair of the auto task force and a board member of the Pension Benefit Guaranty Corporation. You were not merely involved in the GM bailout, but you were simultaneously leading all of the agencies on every side of the deal in one role or another.

Throughout these processes, you have refused and Treasury has refused to answer questions. You have provided unredacted documents or disclosed relative information that people have asked to try to hold accountable the Treasury to find out what has occurred, where the tax dollars have gone.

One of those issues obviously affects Delphi salaried retirees, where 20,000 people across this Country lost a significant portion of their profits as the three roles of the Treasury, the co-chair of the auto task force, and the Pension Benefit Guaranty Corporation picked winners and losers, and they were ones that, with our tax dollars, were picked as losers.

If you looked at that hardship that was imposed on tens of thousands of Delphi salaried retirees left in the wake of the GM bailout and then you have concern as to how we look to the European crisis and whether or not similar conflicts of interest, taxpayers' dollars, and a lack of openness or transparency, as you know, as the Delphi salaried retirees have tried to get the information as to what happened, how they lost their pensions, the three roles of yourself, both in Treasury, PBGC, and the auto task force, have been closed. Documents have not been provided. Redacted documents have been provided, if at all. And most recently we have the PBGC acknowledging your role as the ultimate authority in the decision to terminate Delphi pensions. With the GM bailout you were involved in many of the decisions to terminate these.

But yet there is this sense of how do we have a system through bailouts where a person like yourself would have the three roles that conflicts exist, and yet Congress have no ability for oversight. Individuals who lost their pensions, who don't have an ability to hold you or Treasury accountable in seeking additional information.

As you know, this comes at a significant price. We have the $1.3 billion loss on the Chrysler deal, the $25 or so billion that is at risk in the GM bailout. If we look to the European issue, how can we be assured, looking at the performance of what occurred in the prior bailouts, that we are not going to have this issue of conflicts of interest, of lack of transparency, that there will be some openness, that Congress, that people who are impacted by this, will have access to information?

I sit here as a Member of Congress knowing that Treasury is not answering the basic questions about the decision-making that occurred with the Delphi salaried retirees losing their pensions and wondering how then can we look to perhaps a European issue and not know whether or not our own Government is going to be willing to tell us the decisions that are being made and the basic financial underpinnings of the decisions that occur? Mr. Secretary?

Secretary GEITHNER. Good questions. Let me try to be responsive.

Our financial crisis caused enormous damage across the Country, not just in the case of Delphi, but that is a good example of how much damage caused by the causes that led to this crisis.

We have, of course, cooperated very closely with this Committee and every other Congressional Committee in making sure we are as responsive as possible for all your requests for information, and will continue to do that.

Mr. TURNER. But Mr. Secretary, does that mean that you would be willing to release unredacted versions of the documents? You say you have tried. If you send us documents that are redacted or you, in litigation that is pending, send redacted documents, you are not being forthcoming. That is not: here is what your Government did.

Secretary GEITHNER. Of course I disagree with you on that, but we will try to be as forthcoming as we can. But let me just point out every action that we took in this crisis has been subject to not just the oversight of four separate independent bodies established by the Congress to oversee our actions, but by all the Congressional committees involved. All the actions we took in the auto context were reviewed and validated by the courts. There is a good set of checks and balances in our Country.

Mr. TURNER. Wait a minute, sir. The one with the Delphi retirees is still pending, and you have not been participating——

Mr. MCHENRY. The gentleman's time has expired. The Secretary can summarize his answer.

Secretary GEITHNER. I just want to point out that we have provided an incredible level of transparency over every decision we made with the taxpayers' money in that context. The roles you described to me are roles Congress gave me and my predecessors. There is no conflict in those roles. Again, we have a very strong, robust set of checks and balances in this Country, appropriately so, that gives you the ability and the authority and the right to oversee everything we have done in this context, which I know you will continue to do, and I respect and honor that process.

Mr. MCHENRY. The gentleman's time has expired.

Mrs. Maloney from New York is recognized for five minutes.

Mrs. MALONEY. Thank you.

I would like to join my colleagues in welcoming Chairman Bernanke and Secretary Geithner. Secretary Geithner is a former resident of New York, and I think I speak for all New Yorkers when we say we are so proud of you and your service, and thank you, Chairman Bernanke.

I would like to follow up on my good friend's questioning. There is a consensus in this Country that if we had not invested, he uses the term bailout, but if we had not invested in the American auto industry we would have totally lost it. Lost it. I don't know about my colleagues on the other side of the aisle, but it is hard for me to imagine an America that doesn't make its own cars.

I would prefer to see more things made in America with American jobs. It was at a hearing at this Committee where GM testified they are now the leading car producer in the world, that they are employing 1.3 million Americans, and that they are now exporting the Volt. I would call that an American success story. I would call that American dream.

If it is true that you are the architect of this program—I am not so sure that you are. Many people, I am sure, worked on it. But if it is true that you were the architect of it, we should be carrying him around on our shoulders and thanking him for saving American jobs, building American exports, building up the economy of our Country.

So I would like to say thank you, Secretary Geithner.

Now, I would also like to continue on Mr. Turner's questioning that I think was a really valid one in that we need to learn. We need to learn from the crises that we just went through. I would like to ask both of you what lessons we have learned as a Country and how we are going to be better prepared in the future.

Very specifically, how would you compare the actions that were taken by the American Government in the face of the crisis that we faced in 2008 and 2009 and the actions we took with the actions that have been taken by Europe. And I would like to begin with Chairman Bernanke and then Secretary Geithner on what was the difference in the response? What are the lessons that we have learned to make us stronger in preventing it?

And I would just like to close by saying that Christina Romer testified before Congress that the economic shocks of this particular downturn in our economy was three times greater than the Great Depression. So because of the lessons and reforms that we put in after the Great Depression we were better able to combat it. Hopefully, the lessons we have learned now will help us not only to combat it but to prevent it in the future.

Chairman Bernanke? And thank you for your service.

Mr. BERNANKE. Thank you, Congresswoman.

We did make a very strong effort to arrest the crisis. It was a global crisis. We worked with the Europeans in order to do that. I think, relative to the history of financial crises and given the size of this one, I think we were pretty successful in stopping it.

Since then, I think the United States has been somewhat more aggressive in trying to restrengthen our financial system. I would cite, for example, our 2009 stress tests, which were highly credible and led to substantial capital races by our banking system. Our capital in our largest banks has increased in the last two years by about 75 percent, something in the order of $300 billion.

So we have, I think, taken a lot of positive steps to strengthening our system. There are many aspects of dot frank, including orderly liquidation and macro prudential oversight, which have been, I think, very constructive.

That being said, I think we also have to learn lessons from how we got into the mess in the first place, and there clearly were gaps and weaknesses in our regulatory system, mistakes by supervisors and regulators, including the Federal Reserve. Obviously, lots of problems in business practices, which we are still seeing. I think we will not have really learned the lesson unless we can correct those issues, as well.

Mrs. MALONEY. Thank you.

Mr. Geithner?

Secretary GEITHNER. I think the best way to look at what we did is to judge us on the results, and if you look at the path of the American economy since the beginning of 2009, you compare that record against the record in Europe and the record in the United States or other countries in past financial crises——

Mrs. MALONEY. Thank you, Mr. Geithner. My time is almost over. I just would like to put in the record I have been researching you and getting all your quotes that are very positive about this crisis, that Europe has the ability to avoid the debt crisis, Geithner. And a direct quote was, "And he said that the European Union has the ability to avoid a worsening crisis and urged E.U. members to speak with one voice about plans to solve their debt problems."

I have no time left, but a yes or no. Chairman Bernanke, do you agree with that statement that Europe has the ability to solve this debt problem?

Mr. BERNANKE. They certainly have the economic and financial resources. As was pointed out, their economy is about the same size as that of the United States. They face very difficult political problems getting agreement among 17 countries on a path forward, so it is not going to be easy, but yes, I do think they have the capacity.

Mrs. MALONEY. Thank you.

Mr. MCHENRY. Thank you.

Mr. Meehan from Pennsylvania is recognized for five minutes.

Mr. MEEHAN. Thank you, Mr. Chairman.

Let me express my appreciation to both of you as public servants for making this commitment that you have at a tremendously challenging time not just for our Nation but for our world. I am grateful for your efforts. Obviously, there are many complexing questions that are part of this overall equation, but, Chairman Bernanke, as I was listening to your testimony, one of the things that struck me was in your review of the totality of the circumstances in Europe.

One of the places where, in my estimation, you seemed to identify a little bit of the hesitancy was with respect to this issue of the currency swaps in which we take American dollars, make them available to the European banks, as I understand it, and then they are going to be paid back again in American dollars by the central bank.

Now, what is the real purpose behind that? Is that any distinction from the other kinds of IMF funding and other things? It is a liquidity issue, primarily?

Mr. BERNANKE. It is a liquidity issue, not a long-term loan. The longest of these loans ever made is three months. We have our counterparty is not the country; the counterparty is not the bank. Our counterparty is the central bank, the European Central Bank, which we have every confidence will repay. As I said, we have the collateral of the currency.

So we have a lot of confidence in the financial integrity of those swaps. They have very substantial benefits to the United States. European banks do a lot of their business in dollars for two main reasons. One is that they lend in the United States, and so it directly affects their ability to make loans to American businesses and households. Secondly, they do a lot of lending support trade globally, a lot of which takes place in dollars, and that activity strengthens the role of the dollar as the principal trade currency and as the leading reserve currency.

So our interests are very much involved, and at no financial cost. We have achieved a significant improvement in funding conditions in Europe and, as I mentioned earlier, because of that improvement the demand for those swaps is actually going down, and so we think that has been a successful step.

President Draghi of the ECB has made a point of saying how important the contribution of the swaps was to the stabilization we are seeing.

Mr. MEEHAN. You mentioned a three-month period. Is this more or less a rolling line of credit, so to speak, that over the course of the three-month period you get repayments and then you make new available credit, as well, or access to the——

Mr. BERNANKE. Yes, but we approve not just the program but every single draw, so we can, there is never a point where we couldn't end the program with——

Mr. MEEHAN. Well, what is our exposure currently? What is the totality of our exposure?

Mr. BERNANKE. The totality of our exposure currently is $69 billion, of which $54 billion is to the ECB and the rest is mostly to the Bank of Japan.

Mr. MEEHAN. Just $64 billion. What is our total exposure in terms of other things by the United States to the European sovereign debt and other forms?

Mr. BERNANKE. As our stress test analyzed, the exposure of our banking system to the debt of the weaker countries is, on net, about zero, because even though they hold some such debt and they have written some insurance on that debt. They have hedges in the other direction that protect them from loss, and we are comfortable in the security of those hedges.

Mr. MEEHAN. What is the credibility of the hedges? Where does the strength of the hedges come?

Mr. BERNANKE. The hedges are written by a variety of stronger European institutions, and we are quite comfortable that we can't imagine a scenario when essentially every major European institution——

Mr. MEEHAN. Well, explain to me the qualification, because, if I am not incorrect, in your testimony you did express some reservation. One area of exposures was currency swaps. I thought I heard that in your testimony.

Mr. BERNANKE. No. No, we are quite comfortable with the security of the currency swaps.

Mr. MEEHAN. Okay. Let me ask just one closing question from either of you. We are also living in a very dangerous world. I know you run these with respect to models. The instability that is currently existing in our relationship with Iran and what may happen, to what extent may these models be impacted by what may be a very problematic future with regard to global unrest? Can this whole system be subject to a complete reordering if we have significant instability in the middle east?

Mr. BERNANKE. You mean our banking system?

Mr. MEEHAN. Yes.

Mr. BERNANKE. So we haven't done directly a stress test based on a shock to oil prices, but we have done a stress test based on a much more severe U.S. recession, 13 percent unemployment and a 50 percent drop in stock prices. So I think a geopolitical event that caused oil prices to double, as I think Mr. Gowdy perhaps was suggesting, would have effects of that sort. We believe our banking system has sufficient capital to deal with that.

Of course, it would be very costly to the American economy and to the banks and to the financial system more generally.

Mr. MEEHAN. Okay. Thank you.

Mr. Chairman, my time has expired.

The CHAIRMAN. [Presiding] The gentleman yields back.

The gentleman from Pennsylvania, Mr. Kelly.

Mr. KELLY. Thank you, Mr. Chairman.

I would like to yield my time back to the Chair.

The CHAIRMAN. Thank you. I will use it briefly.

This has been very instructive. Before we go to a second round, originally we said we would get you out of here before 1:00. If we get you out of here before 12:00 are you willing to stay for a second round?

Mr. BERNANKE. Of course.

Secretary GEITHNER. Yes, sir.

The CHAIRMAN. Good. But before we go to that, a couple of quick questions.

I just want to clarify. The European Central Bank can print an unlimited amount of Euros, is that correct, the same as we can print, theoretically, an unlimited amount of dollars?

Mr. BERNANKE. Yes, but it has an inflation objective, which it is very scrupulous about.

The CHAIRMAN. And we know they have only cheated on that a few hundred times; is that right, Mr. Chairman?

Mr. BERNANKE. They have had a good record of keeping inflation around 2 percent.

The CHAIRMAN. But they have cheated on a lot of other monetary things? The fact is that Greece is where it is because nobody was watching what Greece was doing while Greece was pumping up its debt; is that pretty much true?

Mr. BERNANKE. Well, I would argue that was basically both Greece and some of the other authorities rather than the ECB that was responsible for that.

The CHAIRMAN. But isn't the European Central Bank somewhat the fair arbiter of whether or not they are obeying it? Who is responsible to prevent, within the Eurozone, violations by the Eurozone, because ultimately the debt affects the value because on a common currency they are agreeing to live within certain guidelines which clearly nobody was watching, when many countries just ignored the guidelines, at least as to debt.

Mr. BERNANKE. Right. There was a stability in growth pact, which in principle was supposed to limit debt and deficit, and it was violated, and for political reasons there wasn't sufficient enforcement of that. They have tried to strengthen that now with the fiscal compact that they have agreed to more recently.

The CHAIRMAN. Well, going back to my original question, then, within the obligation we have for currency swaps, are they obligated, notwithstanding political pressure, to make us whole? In other words, if, hypothetically, the Euro were to drop in half, they would have to give us back twice as many Euros to get dollars. Is that within their jurisdiction, or would they have to go back to that kind of interesting vote of so many members?

Mr. BERNANKE. No. That is entirely within the jurisdiction of the ECB, and I have no doubt whatsoever they would honor their obligation.

The CHAIRMAN. Okay. So that is the underpinning of your confidence that the swaps are, in fact, extremely safe?

Mr. BERNANKE. Yes, sir.

The CHAIRMAN. And I appreciate that, because I think the American people have to understand that the swaps that we are talking with today are not the swaps we were talking about in the AIG era.

One more question that I know the answer to but I want to make sure the American people hear. Secretary Geithner, I think the Ranking Member addressed it toward you. He talked about the huge amount of debt built up in this Country in mortgages, and you may have noticed that the word principal reduction comes out of the Ranking Member in every question. He is very good at it. He is very disciplined.

Isn't it true that in Europe, in fact, their loans are recourse, and in the U.S., almost uniquely within the world, ours are non-recourse, meaning in Europe they can't walk away from their loan until they have exhausted all of their resources. In the U.S., you could have a pile of money of millions and you could walk away from your mortgage if it is upside down and you don't want to deal with it.

Is that essentially your understanding?

Secretary GEITHNER. I am sure you are right in some countries, but I can't speak to the broader pattern across Europe.

The CHAIRMAN. Okay. We found no countries in Europe that were non-recourse. And that doesn't mean that you can't have a loan chosen to be non-recourse, but the ordinary default in Europe apparently is you sign like you would for any personal loan. They take the house and then they come at you for the deficit.

Secretary GEITHNER. You did see very, very substantial increases in borrowing by households, not just against mortgages, not just for mortgages, but generally in many of those countries in Europe anyway. So even with that slightly different system, you saw in some countries in Europe, very, very large rises in debt by individuals.

The CHAIRMAN. Now, I went to the debt clock. That may not be the best one but, Mr. Chairman, it is the one we all tend to use because it is on the Internet. I looked and, in round numbers, at the time of the crisis we were at, like, $14 trillion, about a trillion more in mortgage debt than we have today. That shows me that overall debt of mortgages has fallen, if you will, a relatively small amount, certainly less than 10 percent.

What does that really say to you from a standpoint of debt to equity of debt is down by that relatively small amount but housing values are down less? And how does that make you feel relative to the security of home mortgages?

I realize that is outside the original scope of this hearing. You don't have to respond if you are not prepared.

Mr. BERNANKE. Well, there has been about $7 trillion of homeowner equity lost by declining house prices, and so obviously leverage in the housing sector is up. But things are moving in a deleveraging direction as home purchases have gone down and home ownership has gone down and as there have been write-downs and as people have paid down their debts.

The CHAIRMAN. Okay. I will now take advantage of this opportunity to call on one last first-round member, the gentleman from Texas, Mr. Farenthold.

Mr. FARENTHOLD. Actually, Mr. Chairman, I would like to yield my time to Mr. McHenry.

The CHAIRMAN. The gentleman is recognized.

Mr. MCHENRY. I thank my colleague for yielding.

Chairman Bernanke, is the current fiscal trajectory sustainable?

Mr. BERNANKE. In the United States?

Mr. MCHENRY. In the United States.

Mr. BERNANKE. No, it is not.

Mr. MCHENRY. What is a sustainable debt load for a country such as ours?

Mr. BERNANKE. Well, there is no exact number. I think that the current levels would be sustainable if they were kept more or less constant relative to the GDP. I think that is an important criterion. If we could, over a period of years, get the debt-to-GDP ratio to some level like 75 percent and then over time even begin to improve that, I think that would be a much better situation. But as it stands, the CBO projections show that under current law the debt-to-GDP ratio begins to explode in the next couple of decades.

Mr. MCHENRY. So explain what happens. You have mentioned this before, and just to clarify, what happens at the end of this year in terms of our fiscal situation?

Mr. BERNANKE. Well, for a number of reasons, under current law if no further action is taken there will be what I have termed a fiscal cliff on January 1 of 2013 as a number of tax and other provisions expire, including the Bush tax cuts, the payroll tax, UI benefits, and at the same time on the spending side is the sequestration arising from the failure of the Super Committee to agree kicks in. And if all those things happen, I think there would be a very sharp and rapid fiscal contraction that would be a serious negative for the recovery.

I hope that Congress will take the opportunity to think through where they want fiscal policy to go, and this will be in some sense a forcing event.

Mr. MCHENRY. So austerity too fast and spending cuts too soon and tax increases that would have a negative impact in economic growth, that is the fiscal cliff that you are speaking of?

Mr. BERNANKE. A very sharp change in fiscal stance in a short period of time would have a negative affect on growth, yes. Again, it is important to achieve sustainability over a longer period, but one day is kind of a short period to have such a big change in the position.

Mr. MCHENRY. Secretary Geithner, I know you have spoken of this. You are obviously the economic spokesman for the Administration, and you have taken that role on in a vigorous fashion. I have heard you speak about the tax increases, the component of the President's budget, and raises a number of folks' taxes at the end of this year, but can you speak to this cliff, because under that scenario of sustainability the President's budget that he submitted to Congress falls short of that, and there is only one fiscal plan that actually puts us on that sustainable path over the long term, over the next decade, over the next 20 years, over the next 30 years, and that is the budget that we passed out of the House last year. The President's budget that he submitted this year puts us in a very harsh spiral based on the debt-to-GDP ratio, based on the tax increases, and for not addressing the cost drivers of our budget.

I will give you an opportunity to respond, obviously.

Secretary GEITHNER. Obviously, I have a different view, but let's look at it this way: CBO just did an assessment of the implications of the President's budget on the long-term fiscal path, and they concluded, as did we, that if Congress were to adopt those policies then we would reduce our deficits over the next three to five years to a level that makes them sustainable over time.

What that means is they would bring the deficits down as a share of GDP to the level where our debt burden would stop growing as a share of the economy and would start to fall. That is for the next ten years.

Mr. MCHENRY. And that is done through a number of increases in the revenue to Government as a percentage of the economy above the historical norm?

Secretary GEITHNER. I will explain the mix. If you go back to where we were last summer, before the agreement last summer, we needed to find savings of roughly $4 trillion over ten years to achieve that objective, meaning getting the deficits down low enough so the debt stops growing as a share of the economy and starts to decline, so we had to hit a $4 trillion target.

The Congress agreed on about $1 trillion of cuts last summer, which we are obligated to hold to. That leaves us with about $3 trillion left to do.

What we propose to do is about half of that through an increase in the effective tax rates of the top 2 percent of Americans, very few number of Americans affected by that, and to find a balance of other savings across the Government.

Mr. MCHENRY. Unspecified or specified?

Secretary GEITHNER. Very specified. We have a very detailed set of savings in Medicare, in Medicaid, and other mandatory, like farm subsidies and civil service retirement, things like that, that would provide an additional $1.5 trillion of savings. And so the overall balance we propose is roughly $2.5 of spending cuts for every dollar in revenue increases. And the reason why we propose that is not because, we know no one likes to raise revenues or raise taxes, is because if we don't find that additional tax revenues out of our current system, then we have to find a trillion-and-a-half dollars in spending cuts in Medicare or low-income programs or education or infrastructure or defense, which we don't think we can justify, or we have to ask somebody else to pay higher taxes, and we don't think that is a fair thing to do for the American people.

So that is the proposal we made. We have got some other differences between us, of course, and those mostly relate to, over the longer term, how we bring our commitments in health care to a more sustainable level. As you know, we have fundamental disagreements on what it is going to take to do that. We have laid out an approach designed to reduce the rate of growth in cost but still preserve that basic commitment to Medicare, to retirees, and we have millions and millions and millions of more Americans retiring in the coming decades. And that is an approach which is very different from the approach you guys embrace in that budget.

The CHAIRMAN. I thank the gentleman. I would also mention we will ask that the record indicate the CBO scoring for Obamacare be put in at the same time to sort of complement the two CBO claims.

Secretary GEITHNER. That helps us though.

The CHAIRMAN. Not so much.

Mr. Burton, would you like to lead off the second round as chairman emeritus? The gentleman is recognized.

Mr. BURTON. Sure.

My colleague, My colleague, I think Mr. Meehan, asked a while ago about the exposure of the United States and our financial institutions. According to CRS, in U.S. dollars in 2011, September 2011, our total exposure is $2.08 trillion. Can you quantify that? You said you didn't know what I was talking about.

Mr. BERNANKE. I am not clear whose exposure you are talking about, the banks or the U.S. economy? I am not quite sure what it refers to.

Mr. BURTON. Well, since you don't understand it, if I submit this to you will you check it out and let me know?

Mr. BERNANKE. Certainly.

Mr. BURTON. Could you answer that for me? I would really appreciate it.

Mr. BERNANKE. Certainly.

Mr. BURTON. The second thing I would like to ask is one more time. I am not a banker. I am not a financier or a financial expert, but I would like to ask this question one more time, and that is, If there is a default in Europe by Greece, Italy, Spain, Portugal, some of these other countries, and the European Central Bank has to start printing more Euros, which would cause an inflationary problem and devalue their currency, you said a while ago that we were not in any trouble because they would pay us back in dollars they are holding. But what if they can't?

Now, they are going to have to pay for the dollars that they are going to repay us with currency that has been devalued substantially. How are we going to get our money, number one, and, number two, would we refinance that debt?

Mr. BERNANKE. Well, Congressman, first of all, the ECB has been very clear that they are not going to be financing sovereign debtors, and they have not, and their primary commitment is to the low inflation rate, the 2 percent inflation rate in the Euro. So I don't see any necessity or even likelihood that the ECB would print inflationary amounts of money in order to address sovereign default.

Mr. BURTON. I know, but it seems like to me Europe is absolutely committed to keeping Greece in the European Union and make sure that nobody is leaving, and if these expenses continue in Greece and they have these civil disorders, and possibly in Italy and these other countries, the European Central Bank and Germany and other countries are going to have to pay the freight to keep these countries afloat.

Now, if they do that it seems to me that the European Central Bank, and I talked to some of the leaders over there, they said that they would, of course, do like we did we quantitative easing and they would print whatever currency they needed.

Now, if they did that there would be an inflationary spike, it seems to me, at some point, and if we had to recover our debt how would they repay us?

Mr. BERNANKE. Well, first, the European Central Bank, itself, has capital.

Mr. BURTON. You mean they have U.S. dollars?

Mr. BERNANKE. Well, I guess their capital is in Euros. That is correct.

Mr. BURTON. Well, how would they repay us then?

Mr. BERNANKE. Well, I guess they get repaid from the banks they lend to in dollars. That would give them dollars to repay.

Mr. BURTON. Well, many of those banks could go belly-up, as well, so they are going to have trouble recovering that, so the inflationary problem is a real problem, so how would we get our money back?

Mr. BERNANKE. Well, again, the European Central Bank is a highly solvent institution. It is committed to low inflation. It is, in turn, supported by a whole network of central banks of the 17 countries which have their own——

Mr. BURTON. I understand, but that is not really answering my question.

Mr. BERNANKE. The kind of scenario you are envisioning where they couldn't pay us back would be absolutely apocalyptic. It would mean a collapse of major governments in Europe. It would mean a collapse of——

Mr. BURTON. Let me follow up with this question then.

Mr. BERNANKE. Yes.

Mr. BURTON. Let's say that Greece defaults and they leave——

Mr. BERNANKE. It has already defaulted.

Mr. BURTON. I understand, but let's say they are forced to leave the European Union because they don't comply with the new demands. And we have a cascading effect into Italy and maybe Portugal and Spain and some of those other countries. In a worst-case scenario, the European Central Bank and the other countries say, okay, we are going to try to keep this from becoming a catastrophe, and they start printing Euros. We are obligated and we are involved, to a large degree, according to the figures I have. How would we fare in the United States and how would we get repaid and what kind of impact would that have on our Country?

I know you used the term apocalyptic. I would like for you just to explain a little bit more thoroughly.

Mr. BERNANKE. Well, again, the money we have lent, first of all, the swap that we have made, the collateral, we have taken collateral for it, which is coming down, is backed, first of all, by the European Central Bank, which, in turn, has behind it 17 national central banks which have gold, they have other kinds of assets. Those central banks, in turn, are backed by the governments of the Eurozone. So it is an extraordinarily unlikely situation that we would lose any money.

Again, it is a three-month obligation. You are talking about a situation where national governments are defaulting across the Eurozone.

Mr. BURTON. If I might follow up?

The CHAIRMAN. Thirty seconds for a brief follow-up.

Mr. BURTON. Thirty seconds. I know some of those governments over there are having political problems and they are not anxious to pour more of their money and their resources into saving other countries. Germany in particular has had some political problems, and maybe more severe. So when you say these 17 other central banks are going to come across and help keep everything afloat, there is a political problem that is involved in that, too. That is why I asked about a worst-case scenario.

Mr. BERNANKE. I didn't say they were——

Mr. BURTON. I think it is important that we understand all the problems that we might be facing.

Mr. BERNANKE. I didn't say they were going to support the individual countries; I said that they would pay the United States back the swap money.

The CHAIRMAN. Thank you.

We now go to the Ranking Member, Mr. Cummings, for a second round.

Mr. CUMMINGS. Thank you very much, Mr. Chairman.

The Chairman had mentioned a little bit earlier that I am very disciplined with regard to this foreclosure issue, and I am, because so many of my neighbors and people across this Country are suffering tremendously. I think it was you, Secretary Geithner, who mentioned the $7 trillion in wealth that has been lost. That is why I do that. And I also do it because I realize it is going to be kind of difficult to address this recessionary problem that we all want to deal with unless we do that.

Several Republicans have likened the fiscal situation of the United States to that of Greece. Chairman Issa likened it, the U.S. financial situation, to the sovereign debt crisis. They argue that the social safety net in this Country as we know it, which provides critical support to the Nation's 99 percent, should be tossed aside. Those Republicans have used the European crisis to justify arguments for draconian austerity in the United States, just as it is now being imposed in Greece.

Chairman Bernanke and Secretary Geithner, can the financial situation of the United States be reasonably compared to that in Greece? Just curious.

Mr. BERNANKE. As I responded earlier on this, I think a direct comparison is not appropriate. Greece has a much higher debt-to-GDP ratio. They have a much weaker and less diversified economy. They are a very small economy. And they don't have an individual central bank, a separate monetary policy, so there are lots of differences.

With that being said, I think everyone needs to acknowledge, and I am sure you do, that in the long run every country, including the United States, has to have a sustainable fiscal path, and we do need to pay attention to that.

Mr. CUMMINGS. I agree. And so would you agree with that, Secretary Geithner?

Secretary GEITHNER. Of course. I think it is very important to point out the contrast. The additional policies we have to agree to in the United States to bring our deficits to a more sustainable level over the medium term are very modest as a share of our economy, completely within our capacity to do, without asking the economy to suffer some undo burden or without dismantling our safety net, or without abandoning commitments to retirees in Medicare and Social Security.

The gap between where we are today and where we are expected to be and what is sustainable in economic terms is roughly 2, 2.5 percent of GDP, which is a very small challenge relative to what many countries around the world are starting to face. And the existing level of benefits we give our retirees are very, very modest. No one could call them excessively generous. We ask Americans to bear a much, much larger portion of the risks in retiring or in paying for health care than is true in really most of the other economies in Europe in that context.

So I see really no comparison in our situations. We are a much stronger Country, much stronger position, both fiscally and financially, probably because we were much more aggressive in responding to our crisis. And even with all our challenges—and we have many challenges, and fiscal sustainability is one of them—we are in a very strong position as a Country to address those challenges.

Mr. CUMMINGS. Now, Greece failed to have a firm understanding of what its deficit actually was. In 2009 Greece reported a deficit of about 7 percent. Months later this figure was revised to 12 percent, and again later to 15 percent. When Greece's sovereign debt was reported, it had no explanation as to how such a monumental error had taken place.

Chairman Bernanke and Secretary Geithner, I cannot imagine the U.S. failing to have a firm grasp of what our debt actually is; would you agree with that?

Mr. BERNANKE. Well, our debt obligation is complicated. We have unfunded liabilities with respect to our entitlement programs and so on, but yes, I think I have confidence in our Government's accounting system. In Greece there were obviously questions about whether or not the numbers were being accurately reported, and that clearly made things much worse.

Mr. CUMMINGS. Now, in Greece any monetary stimulus aimed at mitigating financial stress must be channeled through a third party, the European Central Bank, and it must be agreed to by several other nations in the Eurozone; is that right?

Mr. BERNANKE. I am sorry? Repeat the question?

Mr. CUMMINGS. In other words, in Greece any monetary stimulus aimed at mitigating financial stress must be channeled through a third party, the European Central Bank, and be agreed to by several nations within the Eurozone; is that correct?

Mr. BERNANKE. That is correct. There is one central bank for the whole Eurozone, and it makes decisions based on the whole Eurozone, not on the situation in one given country.

Mr. CUMMINGS. I guess that makes their situation a little bit more complicated than ours.

Mr. BERNANKE. It does.

Mr. CUMMINGS. To remedy anything to do with the deficit and spending and whatever.

Mr. BERNANKE. The main difference is that both the United States and Europe have a single monetary policy, but in the United States we have a Federal Government and a national fiscal policy; in Europe they have 17 different national fiscal policies.

Mr. CUMMINGS. Thank you very much, Chairman.

The CHAIRMAN. You are very welcome.

The gentleman from Pennsylvania, Mr. Kelly.

Mr. KELLY. I thank the Chairman.

Mr. Secretary, Mr. Bernanke, thank you so much for being here today. I know you are in a difficult position. I have been in that same spot myself very many times. I am an automobile dealer and have really gone through some times that were very difficult.

My question deals more with prime rate and where prime rate goes. I think if you go back to 47 until present it averages somewhere around 9.5 to about 9.8. Right now we are at 3.25. But I remember, and with not really pleasant memories, in the early 1980s where it went to 21.5 percent for prime rate. Now, people tell me, Are you out of your mind? That couldn't possibly happen. The reason I remember is because we paid 1 percent over prime for our floor plant so borrowing money to buy cars at 22 percent made it a little bit crazy, because that meant that we were paying 2 percent per month on every car that sat in the lot, so the idea then was not to have too many cars on the lot.

What I worry about is our dollar starts to drop in value. If we start to pump more money into the equation to raise the levels, what do you see happening in the future. I know that right now at 3.25 it looks awfully attractive. In fact, we just negotiated a loan to build a new building, but it was the certainty, Mr. Bernanke, thank you, by the way, that the banks came to us. We had about five bidding for our business, and we came up with what we thought was a real attractive package.

But again, the driver for all of us in small business is the certainty of what the markets are going to be, or, as we look into the future, how we plan our purchases, our equipment buys, our employee hires, and everything like that.

What do you see happening right now dollar-wise, our value of the dollar, because it does drive what lenders are going to ask for us to give back. I know for me it became very difficult because the covenants changed every quarter, the fact that we had a single-purpose building they say, you know what? Your collateral is not worth what it was before, so you become a difficult risk for us.

So risk is the key that drives everybody throughout the whole world. We are looking at great risk in Europe, because I really look at us as mountain climbers all attached to the same rope, and so as they start coming off the side of the mountain it is going to pull all of us down.

Tell me about prime rate. What do you see happening with prime rate? I know we have some certainty, at least in the very near future. Where is it going to go?

Mr. BERNANKE. Well, first, of course, the Federal Reserve's policy has been to try to keep interest rates low to stimulate our economy, and in that respect auto dealers and auto purchasers have obviously benefitted from low cost in funding. In fact, what we are seeing now is that auto purchases are going back close to where they were before the crisis, so that is a very significant improvement.

So that is part of the plan is to try to get the economy growing and get people back to work, and that can only be good for auto sales, as well as for the economy, in general.

With respect to the dollar, there are two definitions. One is the value of the dollar in terms of other currencies, which may matter for international competition in autos and so on, but there the dollar has been pretty stable. There has not been any real trend in the dollar over the last few years.

The other measure of the value of the dollar is the inflation rate, and there also, with some exception relating to gas prices, inflation has been low and stable. In particular, we haven't had the problem of high inflation that we saw in the 1970s, which led to the 21 percent interest rates that you were referring to earlier. So I think our policies are achieving support for the economy without damaging the value of the dollar.

Going forward, as the economy strengthens over a period of time, I don't know exactly how long, obviously interest rates will go up to some extent. The dollar will react to the change in interest rates, it will react to expectations about growth in the United States, but we think that meeting our mandate of maximum employment and price stability is the best way to get a strong dollar in the medium term, and that is what we are trying to do.

Mr. KELLY. And I would agree with you when it comes to auto sales, but again the SAR in 2009 at 16.5 million units a year dropping to 9.5 million units a year, just through attrition, right now we are seeing people whose cars are no longer operable so they are coming back into the market. But still, I have got to tell you, when

I am on the lot or when I am in the showroom, when I look across the desk at people it is the uncertainty of where they are going to be three, four, and five years down the road drives their decision to make a purchase or not to make a purchase. So I have got to tell you, the stability of our economic recovery is so critical.

I look at energy prices right now and I am watching the value of used cars drop almost daily, especially cars that are deemed to be gas guzzlers. If they start to drop off you can lose 35 or 40 percent very quickly as the price point goes up, and that is the one thing I fear. I watched it happen before, and we are very quickly reaching that tipping point again at about $4 where all the sudden the whole world stops and we start to go in a rapid decline.

But I do appreciate your being here today and I appreciate what you are trying to do.

Mr. Chairman, I yield back.

The CHAIRMAN. I thank the gentleman. We now go to the gentlelady from New York for five minutes.

Mrs. MALONEY. I thank the gentleman.

I would like to ask unanimous consent to place in the record quotes, an article from Secretary Geithner, the President of the United States, Simon Johnson, a former IMF chief economist, all that say that Europe is working hard to address the problem and has the ability to handle the problem. I think it is an important statement.

The CHAIRMAN. Without objection.

Mrs. MALONEY. Thank you very much.

I would like to come back to the stress test that came out last week, Chairman Bernanke. Fifteen of our largest banks examined have sufficient capital to withstand a crisis, according to this test. By my calculation, that is roughly 78 percent of all the banks tested. I would call this overall positive news, although our banks do need to do more. Would you agree?

Mr. BERNANKE. Yes, there has been a very substantial increase in capital and ability to withstand stress.

Mrs. MALONEY. I have a specific question that pertains to the European situation. What should we be doing here at home in order to ensure that American banks stay well positioned to manage their exposure to Europe and the European financial situation?

Mr. BERNANKE. Well, as supervisors, the first thing that we look at is capital, and the capital situation is much improved. And, as I said, the stress tests mimic, to some extent, the effects of intensification of the European crisis on the United States. Beyond that, though, we are looking more specifically at the exposures they have and how they are managing those exposures. We talked about the credit default swaps and other kinds of insurance.

We are also looking at liquidity and other types of aspects of bank safety. So again, we have come a very long way in the last couple of years, and although a blow-up in Europe, let me be clear, would be very costly and create a lot of problems for our banks and for our economy, I think we are much better prepared to meet such a challenge today than we would have been a couple years ago.

Mrs. MALONEY. Thank you very much.

You have testified before the Financial Services Committee. Specifically, on February 29th you testified and expressed concern about sharp spending cuts that would take place next year due to the inability of the Super Committee to reach an agreement on a plan. I would like to place in the record some of your statements, because there is a debate now before Congress on the stimulus versus austerity.

May we place in the record the chairman's statement before the Financial Services Committee?

The CHAIRMAN. I am assuming this is his opening statement?

Mrs. MALONEY. No, no. It was in response to questions. No, it was in his opening statement.

The CHAIRMAN. Of course, without objection.

Mrs. MALONEY. Secretary Geithner, I would like to ask you basically do you think the U.S. Government would have been worse off if, instead of passing the stimulus package in 2009, it passed an austerity plan? Would you consider, since we now have before us a blueprint of how we are going to go forward with the budget, proposed budget that Congressman Ryan put out yesterday, and it is the equivalent of a severe, would you call this a severe and damaging austerity plan? His proposed plan cuts even more than the final agreement with the Super Committee.

I want to know if you agree with this statement that was in the New York Times by Paul Krugman when he stated, "The truth is that if you want to know who is really trying to turn America into Greece, it is not those urging more stimulus for our still-depressed economy; it is the people demanding that we emulate Greek style austerity, even though we don't face Greek-style borrowing constraints, and thereby plunge ourselves into a depression."

Would you agree with this statement by Mr. Krugman? And what is your response to those who demand that our Nation take austerity measures that have not particularly worked well in other countries?

Secretary GEITHNER. If the United States had not, in the early part of 2009, put in place $800 billion of tax cuts and emergency spending increases, then our economy would have been dramatically weaker than it has been and we would be in much worse shape today. The estimates, of course you know, and maybe it is worth recalling that in the last quarter of 2008 the economy was shrinking at an annual rate of 9 percent, and it was only the actions in the Recovery Act, combined with those of the Fed and our plans to stabilize the financial system that we had, that we had growth resume really, really quite quickly.

As you know, we have some very fundamental disagreement with the President's opponents on the fiscal side. The Ryan plan, as I understand it, would not just cut spending too deeply and prematurely in the short term, but it would dramatically erode our capacity not just to meet our commitments to retiring seniors and Medicare, but would dramatically erode what is already a very weak safety net and leave us without the ability to fund critical investments in education or innovation which we think are essential to our ability to grow in the future.

So we would not support those policies, do not believe they are in the interest of the United States, and do not believe they would be responsible to adopt at a time where the economy is still healing from a devastating crisis.

The CHAIRMAN. Thank you.

The gentleman from Vermont, Mr. Welch.

Mr. WELCH. Thank you very much, Mr. Chairman.

Thank you, Secretary Geithner and Chairman Bernanke, for your incredible service in a pretty tumultuous time.

I want to go back to this question. It really is a central issue for Congress. I will start with you, Mr. Bernanke. We are having a debate, as you know, in Congress about, with the levels of debt, is austerity the policy that we should be pursuing, or should it be investment, putting it in broad terms, and on the investment side have it be something where, in the short term, we try to maintain low interest rates and rebuild our economy, but have a long-term plan to make for a sustainable fiscal future?

On this question of austerity, the budget that has recently been introduced I think has implicit in it two assumptions. One is austerity will be beneficial to growth, and the budget that has been proposed in the House for our consideration would cut spending across the board in many of the domestic discretionary areas: infrastructure, housing, medical research, education. It would fence off the Pentagon. In fact, the sequester cuts would be avoided.

So, number one, the implicit assumption is that austerity is the path in this budget, the path to progress and growth.

The second assumption in this budget appears to be that if we reduce taxes on folks who have substantial incomes, that likewise will lead to growth.

My question to you is: is there any evidence that either the assumption about cutting taxes on high incomes in these economic circumstances does lead to growth, number one. Number two, is cutting some expenditures in these items I mentioned, medical, research, education, is there evidence to indicate that that will also lead to growth and a lower debt?

Mr. BERNANKE. I think the general approach, without talking too much about specific policies, again is a balanced approach which works to achieve financial stability and fiscal sustainability in the longer term, while being respectful of the need to maintain the recovery at the current stage. I think that is a balanced approach that could be managed.

On the other issues, I think it is also important not just to look at the size of the debt or the debt-to-GDP ratio, but ask ourselves what is the quality of the fiscal programs being undertaken. On the spending side, if we are making investments, are they a bridge to nowhere or are they a type of infrastructure investment that will pay a return and improve economic activity and be worth the investment that is being made.

On the tax side, is it smart tax policy? Is it broadening the base and lowering rates and achieving a fair and more efficient tax code?

So on both of those things I think a balanced approach to fiscal sustainability, but also looking at the specific programs with the eye of trying to achieve healthier, long-term growth is very important.

Mr. WELCH. Thank you.

Secretary Geithner, do you have anything to add on that? This is the central debate in the House, certainly.

Secretary GEITHNER. The fundamental debate we have to face and the things that happened at the end of this year require Congress to confront these things, provide a huge incentive to deal with them now, and the choices are: how fast should we cut our deficit? Be careful not to do it in a way that would undermine the economy in the short run and the long run.

What mix of cuts and tax increases is most appropriate for the long run? What should be the role of Government in helping support investments in infrastructure, education, high returns over time? And what commitments should we leave in place to our retiring seniors in health care and Social Security? Those are the things which separate us fundamentally.

You know our approach, which is a balanced approach which phases in savings over time as we recover and preserves room to make investments in education and infrastructure so that we are growing over the long run, and maintains a commitment made by Republicans and Democrats for decades in this Country to guarantee our seniors a retirement security and health care security in their retirements. Those are things we can afford to do.

Now, we can't put off these fiscal challenges indefinitely. Our fiscal position is unsustainable over the long run. But that is not an argument to go and dramatically erode the capacity of this Country to make the economy stronger, provide more opportunity over the longer run.

Mr. WELCH. Thank you.

The CHAIRMAN. Thank you. I will now recognize myself for a second round. I will try to be brief and keep our promise to get you out of here before 12:00.

Chairman Bernanke, you alluded to how much of our debt is not really on budget. If you take our on-budget debt, our inter-government debt, and our off-budget liabilities, contingent liabilities, as a percentage of GDP, roughly what is our debt?

Mr. BERNANKE. I would have to get back to you. I think the biggest component of off balance sheet is the unfunded Medicare liabilities, 75 years, which is a tremendous number, and more than $30 trillion, something like that, according to the Medicare trustees. That assumes essentially continuation of the increased costs we see in health care delivery out into the indefinite future.

The CHAIRMAN. So at about 100 percent of GDP on budget we could be at 300 or 400 percent of GDP including what is off budget?

Mr. BERNANKE. As I said, if we don't make any changes to our current fiscal trajectory, it is definitely not sustainable.

The CHAIRMAN. Well, Secretary Geithner, and I am only entering this subject because he brought it up, talked about these costs being small, but isn't it true that America already spends a bigger percentage of GDP than our European allies do on health care? In other words, we already are more generous in health care in the sense of what we spend. Maybe not what we get for our money.

The Secretary is absolutely right, more than half of all health care is paid for outside of Government, but it doesn't mean that what is paid for in Government isn't already larger than what Canada pays in Government for total health care. Isn't that right?

Mr. BERNANKE. I am not sure about the government comparison, but it is true that the United States spends more total on health care as a share of GDP than other industrial countries.

The CHAIRMAN. Well, I would like to go on looking at that for a couple of reasons. There has been a lot of discussion about austerity and this brings it back home a little bit. I am an Art Laffer economic model guy. I am not a Keynesian, clearly. But I think we can all understand, I knew that was good for a laugh, Peter, that all economists tend to believe that there is probably a sweet spot, in other words, a right balance of public and private spending, a right balance, and so on.

As we talk about austerity in Greece or in Portugal or in any country and we talk about austerity here, and particularly, Mr. Secretary, aren't we agreeing that we are trying to get to the same position, whatever that sweet spot is, of promoting growth through not taking it all to the Government, and that we are only debating, when you talk about the rate of austerity, we are not debating where we need to get to.

Where we need to get to so that the private sector can flourish is probably very similar to where we are telling the countries of Europe to get to, so that the difference of the austerity we ask for others and the austerity we need to get to may be about how much time we have to get there more than it is about what we need to achieve; isn't that true?

Secretary GEITHNER. That is probably right. The fundamental reality, the fundamental constraint we all have to live with, whether you are European or American or Japanese, is you have to get the deficit down to a point where the debt stops growing as a share of the economy and starts decline, and you have to stabilize at a level that is acceptable.

The CHAIRMAN. Right. And I want to follow up on that, just for the record.

Secretary GEITHNER. But the difference, just on your first question, is it is partly a debate about how fast and what is appropriate.

The CHAIRMAN. Right.

Secretary GEITHNER. But it is also a debate about the composition, and the composition, if you look at what divides the Country——

The CHAIRMAN. The left and the right will never agree on where Government should spend/invest, so we will assume that that part is probably very much ours.

Chairman Bernanke, you had already, I think, provided a little bit of a mea culpa, and I am not going to ask for it again, but you put out a white paper related to the housing and what banks and so on should do. If you don't mind, I would like to follow up to a great extent in support of the Ranking Member. In your white paper, and, again, your representative from Richmond, Virginia and others may have chastised you over this, but since it is out there in the record, one of the things that was in the white paper had to do with the possibility that banks should essentially flip their properties into rentals, that that was an element.

And the Ranking Member, very disciplined, talked about principal reduction. When we are looking at what is best for people who find themselves in homes that they could not originally afford, I mean, principal reduction in these low-interest times assumes that they can no longer or could not when they bought the home afford what they bought.

When we look at the potpourri of options both for Freddie and Fannie and FHA and for the banks in their roles, would you comment further for this Committee on the record to try to understand why these alternatives of perhaps you can't afford the rent for this home for a period of time, perhaps that is the best transition, perhaps it is best for the community, I think that is an element that has not been discussed, if you will, by the left or the right, and you did put it in your paper, and to the extent that it exists I would like to have it fully vetted.

Mr. BERNANKE. The theme was that we need to attack the housing issue at different points. Obviously, if we can avoid unnecessary and uneconomic foreclosures we should do that, and there are multiple ways of doing that. We didn't come down in favor of any specific approach. I think it depends on the situation.

But what we noted was that, no matter how hard we work, and the Country has been working pretty hard on this issue, that there are going to be still a number of foreclosures that occur, people who lose their homes or leave their homes, investors who abandon their properties, and it is bad for the housing market, it is bad for neighborhoods, for empty houses to stand in a row on a street.

So we still think that we should be looking at ways to avoid unnecessary and uneconomic foreclosures, but another part of the problem is the fact that we have got so many empty houses overhanging supply in the housing market, which pushes down prices and reduces construction.

So there are various possible approaches to that. One of them is REO to rental, which we described and talked about in our paper. There are other things. For houses that are in bad condition, land banks can purchase them and perhaps bulldoze them if necessary.

So our point is only that loan modifications have a role to play, but there is a whole number of different things that can be helpful in the housing market.

The CHAIRMAN. And I will give the Ranking Member some additional time if he would like it, but I want to follow up with one more, and this is much more broadly in your purview, both of you.

A number of cities, even States, have found ways to extend dramatically the amount of time it takes to foreclose on somebody that isn't paying. In Brooklyn where we were they basically got it out to three years, if your papers are all in order, between the time someone stops paying and perhaps stops maintaining the home and the time that the institution can take possession. In the case of Illinois, I am sorry the gentleman is not here right now, they have tried to have Freddie and Fannie, during the foreclosure process, which is being elongated, maintain the home on behalf of the homeowner who is not maintaining it on behalf of the community.

I don't want to presume your answer, but would you say that these are probably not helpful to either the long-term credit market because of certainty, or to the process that we are trying to get beyond and get to where we have a positive market and positive neighborhoods? And feel free to answer as you think is appropriate.

Mr. BERNANKE. Well, I think delay for the sake of delay is not constructive. The homes deteriorate. The process drags on and the healing of the housing market drags on.

That being said, obviously we have seen a lot of cases where servicers have not performed their due diligence where they have foreclosed in appropriately, et cetera, and when there are situations where there are questions about the integrity of the process then we have to take the time necessary to make sure that things are being done correctly.

The CHAIRMAN. Yes. Mr. Secretary?

Secretary GEITHNER. I think the chairman said it right. There are, of course, huge numbers of innocent victims in this crisis, and there are lots of people who can afford to stay in their homes, and you want to make sure you give them a chance to do it. And there are some people that have already left their homes or need to pursue a more affordable option, and we should help make that easy for them to do it.

You want to make sure that when you foreclose that process has complete integrity, and so you want to have some checks and balances on that, but I agree with you that the process is taking too long in many parts of the Country, and if that could be sped up without compromising those other fundamental objectives, that would probably be better for those communities.

The CHAIRMAN. Thank you.

Mr. Cummings, a couple minutes.

Mr. CUMMINGS. Thank you very much.

I want to just go back to a matter that the Chairman brought up on Monday in Brooklyn at our hearing and just get your opinion on this. We had major banks there, and we asked a question about how, when interest rates are lower, and let's say somebody has a mortgage at 6 percent now, and dare I say underwater, we were asking or he was asking the banks what is the negative side, and you can correct me if I am wrong, Mr. Chairman, of trying to make sure that those people are able to take advantage of lower interest rates?

Do you all see that as one of the, we talked about a number of remedies. In other words, do you understand my question? I mean, I just wanted your opinion on that. It seems like a lot of people would fall into that category.

Secretary GEITHNER. No, exactly right. That is why it is so important that you give people the opportunity to refinance and take advantage of the lower rates, and one of the most important things that we have done and what the head of the FHFA has done over the last six months is to put in place a much better-designed program to help people who are significantly underwater take advantage of lower interest rates, but we want that to happen on a much larger scale.

That program is actually getting quite a lot of traction now. You are seeing, as you may have heard in New York, a very substantial increase in refinancing by people who are significantly underwater, and we think we are at the early stage of that increase, expect much more to happen.

Now, those programs now only apply to the loans that have been guaranteed by Fannie and Freddie, and so we have also suggested that Congress consider authorizing the FHA to provide an additional program in that context too, just to be fair. You know, most people are not sure who guaranteed their loan, and we want to make sure those opportunities are available to everybody who owns a house.

Mr. CUMMINGS. Just one last question. One of the things that I looked at is this whole idea of when the banks did their settlement, FHFA did not bring them under those provisions for writing, as a matter of fact, they said we don't want to be a part of that. I know that you are talking to Mr. DeMarco. Was that a concern of yours, particularly when we have tripled the incentives for those kinds of things? I am just curious.

Secretary GEITHNER. As I said, there is a very strong economic case in some circumstances, and that is why you are seeing private investors do it, to reduce principal for people who are deeply underwater but can afford to stay in their own and meet a reasonable payment. And that case will be equally compelling in parts of the people whose loans were guaranteed by Fannie and Freddie, and so what we are trying to do is encourage Mr. DeMarco, who is fully independent and has——

Mr. CUMMINGS. I understand that.

Secretary GEITHNER.—to take another look at the evidence because we think there is a place for doing more in a way that is completely consistent with the mandate that Congress gave him appropriately to make sure he is protecting the interest of the taxpayer as he helps the housing market. So we are working through those numbers with him and I expect to hear some more in the next couple of weeks.

Mr. CUMMINGS. On the behalf of the many millions of Americans who are dealing with this issue, I would ask you to use your most convincing voice to try to get him to move off the dime.

Thank you very much, Mr. Chairman.

The CHAIRMAN. I thank you.

I want to thank our witnesses. We did get you out pretty close to the 12:00 o'clock. You extended your willingness to answer far beyond the initial scope. I would only ask one more item. Please, the next time we invite you back, remember that this was a Committee that has worked a lot in areas that overlap, and accept our invitation, as you so graciously did this time.

With that, we are adjourned.

[Whereupon, at 12:05 p.m., the committee was adjourned.]

Chairman Darrell Issa Hearing Preview Statement

"Europe's Sovereign Debt Crisis: Causes, Consequences for the United States and Lessons Learned"

March 21, 2012

The United States and Europe together account for 50 percent of world GDP and 40 percent of the world's trade in goods and services. With these two economies inexorably linked, a downturn in one immediately and broadly impacts the other. A catastrophic failure in Europe would threaten our own economic situation at a time we can least afford it.

Today, the Committee on Oversight and Government Reform will ask key questions of Treasury Secretary Timothy Geithner and Federal Reserve Chairman Ben Bernanke regarding the future outlook of the U.S. economy and the impact that Europe's sovereign debt crisis is having on us.

This is a continuation of efforts begun in this Committee and at the Subcommittee level throughout the past year. In a time of a global economy, understanding the problems of one nation so we can avoid repeating their mistakes here is essential to our nation's standing as a global leader.

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Opening Statement
Rep. Elijah E. Cummings, Ranking Member

Hearing on "Europe's Sovereign Debt Crisis: Causes, Consequences for the United States and Lessons Learned"

March 21, 2012

Mr. Chairman, thank you for calling today's hearing on the financial crisis in Europe and the lessons that can be learned here at home.

Since the last hearing we held on this topic in December, European officials have taken decisive action to reestablish financial stability in the eurozone. And American officials have helped diplomatically, through consultation, through our participation in the IMF, and through central bank support. No one is declaring "mission accomplished," but the signs of improvement are impossible to miss.

Unfortunately, it appears that some in the majority see the eurocrisis as justification for imposing extreme austerity measures here at home. Yesterday, the House Republicans released a budget proposal to cut $5.3 trillion over the next ten years, end Medicare as we know it and shift costs onto seniors, and give further tax breaks to corporations.

Today, the majority will seek to draw parallels between Greece's financial troubles and the United States. At our last hearing, a majority witness called Greece a "wake-up call," arguing that the U.S. should shred our nation's safety net and cut taxes to avoid Greece's fate.

Don't believe it. While strong medicine is needed, it is the banks that caused the financial crisis who should be taking it.

What we have learned from Greece is that austerity measures imposed during an economic downturn have very real negative consequences for working people, while they leave economic elites unscathed. Nevertheless, some Republicans believe we should implement similar extreme austerity measures here at home in the form of deep, across-the-board, spending cuts.

Secretary Geithner, on past occasions, you have warned against such actions. For example, you said this: "We need to stay intensely focused on strengthening [our] economy in the short-term. ... We can't cut our way to growth. Severe austerity now would be very damaging."

But House Republicans have ignored this key point.

Different problems require different solutions. In the case of the United States, economists largely agree that the housing bubble and risky investment products created by Wall Street were the chief causes of our economic collapse. As Mark Zandi, Chief Economist of Moody's Analytics stated, "[h]ousing is ground zero for the economy's problem, high unemployment and lost jobs."

Although the recent $25 billion settlement with five of these banks is commendable, the sad truth is that millions of borrowers will not receive the relief they so desperately need because one important entity refuses to cooperate. The Federal Housing Finance Agency (FHFA), Fannie Mae and Freddie Mac's regulator, will not allow them to participate in the settlement, reportedly because much of the relief will be in the form of principal reductions.

If we want to ensure that our economy at home is strong enough to weather the Euro crisis or turbulence from slowdowns in other foreign economies, we must end the housing crisis here at home. We must have principal reduction as one tool for borrowers who are underwater and who owe more than their homes are worth.

FHFA's own data shows that principal reductions would save taxpayers billions of dollars. But Edward DeMarco, the agency's Acting Director, maintains what appears to be an ideological opposition.

It is my hope that, as we examine the Euro crisis, we keep in mind what should be our ultimate goal: rebuilding and protecting a strong economy for the millions of middle-class American families here in the United States.

Remarks of the Honorable Dan Burton
Committee on Oversight and Government Reform
"Europe's Sovereign Debt Crisis: Causes, Consequences for the United States and Lessons Learned"

March 21, 2012

****As Prepared for Delivery****

As Chairman of the Subcommittee on Europe and Eurasia, I have visited and met with officials from many countries in the region over the past year, including Italy, Ireland, Greece, Portugal, and France. I have also met with European Union leaders in Brussels.

During these meetings, European representatives have routinely painted an overly optimistic picture of the crisis. The Italians told me that everything is on track and parliament is passing reforms. Weeks later, the government fell and a new Prime Minister took office making new promises. Greek officials told me that they would succeed in passing austerity measures, even as riots took place on the streets of Athens. Weeks later, the Greek government fell and a new Prime Minister took office making new promises. The governments of Ireland, Spain, and Portugal have suffered similar fates.

Meanwhile, my questions to these leaders have gone unanswered. That is, who will pay for these bailouts and where will this money come from? Sometimes I hear that this is a European problem and the Europeans will pay. However, I have also heard that China and Japan's foreign currency reserves will rescue the European financial community. Recently in Brussels, I was informed that the European Central Bank is conducting its own quantitative easing, something the U.S. knows too well as a tool of our own financial policy – a tool that I strongly oppose, as it is a cause of inflation.

I believe the most important question for us to ask today is: how the United States is involved? By this I mean, what is our total direct and potential exposure to Europe? How is the Treasury Department working to support its European counterparts? How much are we helping from Central bank to Central bank and how exposed is the Federal Reserve? We have trillions at stake and are lending hundreds of billions. I want to know precise numbers.

Meanwhile, the European Council meets repeatedly. After each meeting, the only result we see is the considerable plunge or rise of the stock market. It is clear to me that the rest of the European Union is only keeping Greece afloat to provide time to get their houses in order. This is not healthy for U.S. and global markets as speculators and hedge funds wreak havoc with our markets and economic stability. Europeans are whistling past the graveyard. It is in the U.S. national interest to mitigate our risks.

As a major economic power the United States has a vested interest in Europe's financial stability. The continent remains a major partner in trade and investment. However, a solution to this crisis should not involve our printing of money that puts Americans at greater risk. No one wants to see the crisis averted more than myself. However, we must be prudent, we must be transparent, and we must be accountable to the people.

Statement of Congressman Gerald E. Connolly

March 21st, 2012

The European Union is facing a paradoxical Goldilocks challenge, with too much economic interdependence and too little centralized authority to fix crises of confidence in particular member nations' finances. That the United States has neither the decentralized financial governance of the European Union nor the debt levels nor the interest rates of some European countries which are in crisis has scant bearing on whether or not some would demagogue the issue of American debt. As Mr. Geithner's testimony notes we must not be misled about the nature of the crises in Europe: Some nations like Spain which have been victims of European Central Bank (ECB)-imposed austerity following financial crises did not have high levels of debt.

America has a similar level of debt today as it did after World War II, measured against the size of our economy. When Congress and a series of Administrations reduced that debt, they did so by facilitating strong economic growth instead of self-defeating austerity measures. Proposals to cut spending on discretionary programs and gut economic security programs like Medicare, such as those proposed in the latest Ryan budget, actually would slow if not reverse economic growth. A quick review of the facts shows that spending in America is fairly consistent with historic trends; expenditures today are within 0.5% of what they were when Ronald Reagan proclaimed morning in America. By contrast, revenues have fallen to their lowest levels since 1950, an era which predated Medicare and Medicaid. That is no coincidence: It is precisely those programs which provide economic security for working Americans that Congressman Ryan and the Republican House leadership have in their crosshairs. Last year the House majority passed legislation to privatize Medicare by turning it into a voucher system, capping payments, and raising costs for Americans. The majority of House members have taken a "no tax" pledge, which would make it impossible to balance the budget over the long term *without* eliminating programs like Medicare and Medicaid, which is precisely the goal of Grover Norquist and his allies on the right.

In contrast to the fictitious problems peddled by ideologues, Europe has genuine problems with the financial solvency of individual members as a result of a single regional currency. Before the Euro, companies experiencing a recession would undergo currency devaluation relative to other currencies, which has the impact of helping manufacturers in those countries which have experienced currency devaluation. For the same reason, China has manipulated its currency to gain an advantage over European and American competitors. Devaluation of a peso in Spain versus a franc in France now cannot happen, and as a result recession-bound economies in certain European countries have one fewer tool for economic recovery. Moreover, in a problem which those who crafted America's Constitution in 1787 would have recognized, Europe does not have a centralized government to craft economic rescue packages based on stimulus of aggregate demand. Instead, it has a central bank which can lend money but has chosen to only under terms of austerity which actually exacerbate recession in affected countries. Fortunately, America still has a currency which can and did devalue relative to the Euro when we experienced a recession starting in 2008. We still have a federal government which can institute fiscal stimulus, as the Recovery Act did in 2009. Compare the results: All but one European country undergoing austerity measures continue to experience economic shrinkage while America's economy has been growing since the third quarter of 2009. The Recovery Act, quantitative easing, and low interest rates produced growth in America while austerity and inflation paranoia have stifled growth in Europe.

Today we will hear once again about the need to cut government spending and eliminate the debt, which is a logical impossibility. The data shows that collapsing revenues have produced large deficits, but since Congress exercised fiscal prudence in the not-so-distant past our total debt and debt as a percentage of GDP are manageable, and allow the federal government to borrow at extraordinarily low interest rates to finance economic recovery. To slash spending now only would risk a return to recession, just as spending cuts in 1937 reversed what had been stimulus-driven economic recovery following the Depression. We have seen that this House majority is not particularly interested in restoring economic growth, which is why the Republican leadership has opposed fiscal stimulus (the Recovery Act), opposed monetary stimulus (quantitative easing and low interest rates), and called for draconian austerity measures that would swell the ranks of those in poverty (the Ryan budget). Taken as a totality, Republican economic proposals call for a return to 19th century Darwinism, to an era when governments made economic decisions for the benefit of the wealthy and leave the working classes to suffer the consequences without the encumbrance of any social security programs.

The Republican insistence on the comparison between Greece and the U.S. is particularly invidious. Greece, as demonstrated recently by Michael Lewis, lacked even a system for capturing economic data, boasts a culture of tax avoidance and seemingly fabricated macroeconomic information when examined by E.U. officials. Greece's government bordered on the dysfunctional and resorted to deception to deny and avoid its problems. Maybe Republicans see similarities, but no serious economist would. The comparison is both cynical and risible, a cheap shot which has no validity.

MAY 1 ...

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

BEN S BERNANKE
CHAIRMAN

May 16, 2012

The Honorable Darrell Issa
Chairman
Committee on Oversight
and Government Reform
House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

Enclosed is my response to the written question you submitted following the March 21, 2012, hearing before the Committee on Oversight and Government Reform. A copy has also been forwarded to the Committee for inclusion in the hearing record.

Please let me know if I can be of further assistance.

Sincerely,

Enclosure

cc: The Honorable Elijah Cummings

Questions for The Honorable Ben S. Bernanke, Chairman, Board of Governors of the Federal Reserve System, from Chairman Issa:

1. The United States has considerable investments in the sovereign and commercial sectors within Europe. With reference to the table below, can you confirm the total U.S. direct and potential exposure to the European Market?

Exposures as provided by CRS in U.S. dollars from September 2011 figures

	U.S. Direct Exposure	U.S. Potential Exposure	Total
Portugal	$5.2 billion	$48.6 billion	$53.9 billion
Ireland	$53.5 billion	$57.7 billion	$111.3 billion
Italy	$46.8 billion	$262.8 billion	$309.7 billion
Greece	$8.3 billion	$48 billion	$48.4 billion
Spain	$66.7 billion	$177.3 billion	$244 billion
Germany	$234.7 billion	$400.4 billion	$635.2 billion
France	$271.6 billion	$412.8 billion	$684.5 billion
Total	$686.8 billion	$1.4 trillion	$2.08 trillion

Response to Question 1

U.S. banks' credit exposure to residents of Europe

Table 1 shows the credit exposure of U.S. banks to residents of selected European countries. Credit exposure is the sum of bank lending and bonds held, net of third-country guarantees and certain liquid collateral, and is reported to the U.S. bank supervisory agencies on the Country Exposure Report, or FFIEC 009 report. Aggregate data for U.S.-headquartered banks are sent to the Bank for International Settlements (BIS), which publishes the data along with that of other countries. The table corresponds to the column titled "U.S. Direct Exposure" provided by the CRS.[1] It is important to be aware that the FFIEC 009 report provides a broad measure of exposure. For example, exposures to counterparties to resale agreements and securities lending are not adjusted for the collateral backing these claims, even though these are collateralized transactions. In addition, claims arising from long positions in the trading book are not adjusted for offsetting short positions. As a result, the exposures shown in the table can greatly overstate what realized cross-border losses would be.

Table 1
Credit Exposures of U.S. Banks to Residents of Europe
as of end-December 2011

	billions of dollars
Greece	4
Ireland	44
Portugal	5
France	182
Germany	175
Italy	37
Spain	46
Total	**493**

Source: Bank for International Settlements, Table 9E at http://www.bis.org/statistics/consstats.htm.

[1] The numbers are not identical, because the CRS figures were as of end-June 2011, whereas Table 1 shows data as of end-December 2011.

Table 2 shows the sources of contingent credit exposures of U.S. banks to residents of selected European countries. Column 1 shows undrawn credit commitments to European borrowers, which exceeds $10 billion only for borrowers in Germany and France. Column 2 shows the positive fair value of all types of derivatives contracts (interest rate, foreign exchange, equity, commodity, and credit derivatives) with European counterparties, which exceeds $10 billion only for counterparties in Germany, France, and Italy. Column 3, guarantees, is composed primarily of the *gross notional* amount of credit default swaps (CDS) sold on European borrowers. Because column 3 takes no account of CDS protection that U.S. banks have *purchased* on European borrowers, it provides a very inaccurate measure of the likely effect on U.S. banks of the triggering of CDS on European borrowers. The banks that report large amounts in column 3 tend to be market-makers with large CDS trading books, which means they have also purchased significant CDS protection on the same borrowers. Column 4 is the total of the first three columns and corresponds to the column titled "U.S. Potential Exposure" provided by the CRS. Column 3 is the largest component--85 percent, on average--of column 4, and as a result, column 4 greatly overstates the contingent credit exposure of U.S. banks to Europe.

Table 2
Contingent Exposures of U.S. Banks to Residents of Europe
in billions of dollars, as of end-December 2011

	Undrawn credit commitments (1)	Derivatives contracts (2)	Guarantees, primarily CDS sold (3)	Total of columns (1), (2), and (3) (4)
Greece	0	1	45	46
Ireland	4	10	37	52
Portugal	0	2	52	55
France	35	37	384	456
Germany	29	60	347	436
Italy	5	27	264	295
Spain	8	6	168	182
Total	**81**	**143**	**1,296**	**1,520**

Source: Bank for International Settlements, Table 9E at http://www.bis.org/statistics/consstats.htm.

Secretary Geithner Testimony before the House Oversight and Government Reform Committee: "Europe's Sovereign Debt Crisis: Causes, Consequences for the United States and Lessons Learned". March 21, 2012.

Question for the record from Rep. Dan Burton:

1. ***The United States has considerable investments in the sovereign and commercial sectors within Europe. With reference to the table below, can you confirm the total U.S. direct and potential exposure to the European market?***

As your question indicates, U.S. firms have considerable investments in the sovereign and commercial sectors within Europe. The Euro Area accounts for about 18 percent of global GDP, and about 15 percent of U.S. exports of goods and services. When growth slows in Europe, it damages confidence and slows the momentum of the recovery around the world.

Due to the wide variation in methodologies for measuring exposures, different sources may yield different results. For example, European exposure estimates may vary significantly for firms that do not report their information to supervisory agencies, and some information monitored by the regulatory agencies is confidential and supervisory in nature. In general, U.S. financial firms and money market funds have had time to adjust their exposures and hedge their risks to some degree as the European situation has evolved, but the risks of contagion remain a concern for both these institutions and their supervisors and regulators.

Treasury continues to collaborate with other agencies – both bilaterally and through the Financial Stability Oversight Council – to help to ensure that exposures are being monitored appropriately and to improve the ability of U.S. financial institutions to withstand a variety of possible financial contagion stress scenarios emanating from Europe. Treasury has also worked closely with Europe's leaders over the past two years, and with the members of the IMF, to help support a stronger European response to the crisis.

Question for the record from Rep. Trey Gowdy:

2. During the hearing, Representative Gowdy asked you: "If this were the last debt ceiling increase you could ask for, the final one, and you had to make it large enough for all current and future obligations, what would the request need to be?" After you declined to answer, Representative Gowdy asked you again: "[I]f we had one more chance to borrow all the money that we need, assuming current variables, how big would that number have to be?" You offered to provide a number in writing, before commenting that the figure would be "a lot. It would make you uncomfortable." Please provide a written calculation in response to Representative Gowdy's question. In your response,

please list all assumptions you make and clearly demonstrate how you arrive at your conclusion.

Treasury's borrowing depends on the difference between two main factors: (1) spending obligations that have been authorized and appropriated by Congress and (2) the revenues of the United States Government.

Treasury borrows money to fund obligations that have previously been authorized and appropriated by Congress. The debt limit does not authorize new spending obligations. Because Treasury borrows in order to fund obligations that Congress establishes, future borrowing needs depend upon Congress's future actions. It is impossible to know what decisions this Congress and future Congresses will make with respect to spending.

Treasury's borrowing also depends on the revenues of the U.S. Government (Treasury borrows to fund obligations in excess of revenues). As with spending, it is impossible to know what future decisions this Congress and future Congresses will make with respect to revenue.

In addition, even under current law, estimating in any given year the amounts of many authorized payments and the amounts of revenues that will be collected is inherently variable. Payments for programs such as Medicare, veterans benefits, and unemployment benefits, as well as tax receipts and other cash inflows, are subject to considerable fluctuation due to changes in economic and other external factors.

Treasury's best estimates of its future borrowing needs are published quarterly, and are available on our website at: http://www.treasury.gov/resource-center/data-chart-center/quarterly-refunding/Pages/Latest.aspx.