U.S. gets busy printing money

Jacqueline Thorpe, Financial Post, With Files From Wires
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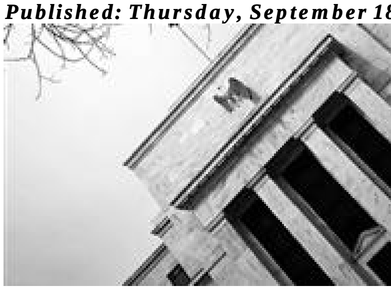
Chip Somodevilla, Getty Images

The U. S. Treasury cranked up its printing press yesterday to help the Federal Reserve extend an US$85-billion loan to American International Group Inc., the latest in hundreds and billions of dollars of government assistance that will undoubtedly end up in the lap of U. S. taxpayers.

But while anxiety is rising over the United States' ability to foot the gargantuan bill for the credit crisis, analysts say the US$14-trillion U. S. economy should be able to absorb the shock.

The key risk is the threat to inflation posed by the seemingly endless expansion of the government's balance sheet if several more financial institutions go belly up.

"Clearly this will widen the deficit by quite a bit," Nariman Behravesh, chief economist of Global Insight, said at a presentation in Toronto yesterday.

The U. S. Treasury swung into action yesterday, selling US$40-billion of cash-management bills to transfer to help cover the Fed's loan to AIG.

The borrowing is separate from the Treasury's ongoing borrowing program and marks a departure from the Fed's strategy thus far of taking private debt in exchange for treasuries. John Chambers, chairman of Standard & Poor's sovereign ratings committee, said the rescue weakened the fiscal profile of the United States and put pressure on its AAA credit rating.

"There's no God-given gift of a 'AAA' rating, and the U. S. has to earn it like everyone else," Mr. Chambers told Reuters in an interview, though S&P reaffirmed the rating yesterday.

The loan to AIG is only the latest in a string of manoeuvrings by the Fed and the Treasury to ward off financial disaster. The Fed has already announced it will inject up to US$200-billion into mortgage agencies Fannie Mae and Freddie Mac; it has taken on at least US$200-billion of loans to banks through its term auction facility and extended US$29-billion in financing for JP Morgan Chase's buyout of Bear Stearns & Co. On the fiscal stimulus side, the government has doled out US$168-billion in stimulus cheques, given US$300-billion to help refinance failing mortgages and US$4-billion in grants to local communities to help them buy up abandoned homes.

While the federal deficit may well head toward US$600-billion from a projected US$407-billion this year, as a percentage of GDP losses should still only come in around 3.3%. Still, the question is how many more skeletons there may be in the cupboard. "We don't know how many bailouts are ahead of us," said Alex Jurshevski, CEO of Recovery Partners, an investment banking boutique. "There are several that are high probability and there are many, many more that are a non-trivial probability."