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Remarks by

Alan Greenspan

Chairman, Board of Governors of the Federal Reserve System

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I thank the members of the Public Securities Association for bestowing upon me this award for distinguished public service I am particularly honored by the company that I keep as a winner of this award, as previous recipients have included Senators Daniel Patrick Moynihan, Christopher Dodd, and Kay Bailey Hutchison and my predecessor as Chairman of the Federal Reserve, Paul Volcker

I trust that everyone in this audience would agree that the U S government securities market works as well as any on earth and generates widespread macroeconomic benefits In one sense, that is regrettable The market has become so efficient in part because of the economies of scale associated with the large volume of Treasury debt issued over the years While the massive federal debt has allowed traders to refine their skills, it has also implied that much of the small pool of national saving has gone toward funding the government Moreover, the interest burden of this debt has kept tax rates higher than we might have wanted

In another sense, though, the efficiency of the government securities market stands as testimony to decisions by policy makers in the formative days of our nation that convinced the world that the United States honored its commitments and valued the rule of law Every time I visit Secretary Robert Rubin, I am reminded of the power of the first Secretary of the Treasury's decisions that laid the foundations for this nation's financial credibility Engraved at the base of the statue of Alexander Hamilton outside the Treasury building are the words of Daniel Webster "He touched the dead corpse of the public credit, and it sprung upon its feet "

Everyone knows the short version of the events that prompted that praise

Hamilton convinced the new Congress to honor the debts of the Continental Congress Under his prodding, the federal government also assumed responsibility for the debts of the individual states incurred in fighting the War of Independence But there are five details of the debate at that time that we all would be well served to remember

First, Hamilton insisted on full payment of the debt Many at that time counseled discrimination among those obligations--perhaps by favoring vendors and veterans over bond holders or perhaps by paying original holders of debt more than those who purchased securities in the secondary market Hamilton recognized that an obligation was an obligation, no matter how it was incurred or who held it Repayment had both a moral and practical dimension The debt, in Hamilton's words, was the "price of liberty" because it financed the successful completion of the War of Independence Those who extended aid at a time of peril, or supported the debt subsequently, deserved to be repaid But repayment would also send an important message to investors, particularly those abroad, that the United States could be trusted in the future Hamilton recognized, and we should never forget, that investors have many choices on world markets Even the whiff of the possibility that the United States would not honor its debt would push up the cost of borrowing for years to come Following Hamilton's lead, the Treasury has never defaulted on any debt security, notwithstanding the abrogation of the gold clauses in 1933

Second, Hamilton was practical in his understanding that economic policy making cannot be divorced from the broader discourse on public priorities The debate on the assumption of state debts generated arguments so heated as to make our weekend television talk shows appear as civil as tea parties Reflecting on those days in his later years, Thomas Jefferson--by no means an admirer of the first Secretary of the Treasury--was led to write that "this measure produced the most bitter and angry contest ever known in Congress, before or since the Union of the States " But those bitter enemies, Hamilton and Jefferson, compromised with an old-fashioned horse trade Jefferson threw his support for the assumption of the state debts in return for Hamilton's advocacy of placing the nation's capital on the banks of the Potomac

Political realities have not changed in that regard in the succeeding two centuries It is inevitable that consideration of the budget be included as part of a wider debate on public policies However, Alexander Hamilton drew a line that no one should cross The government of the United States must never default on its debt

Third, Hamilton's plan to honor the old debt provided a sinking fund to help repay new debt as it came due The first Secretary saw that Treasury debt was a burden to future generations And it was his responsibility to provide the means to lighten that load In those simpler times, before we became too sophisticated for our own good, deficit financing was a necessity prompted solely by peril, not as a tool of active demand management or as an excuse to put off hard decisions In one sense, though, Hamilton's job of planning for the retirement of the debt he was issuing was easier than the problems confronting today's policy makers In 1789, government obligations could be measured by the amount of debt outstanding Today, debt comes in many forms, including promises to pay that have become embodied in unfunded entitlement programs

Fourth, Hamilton's refunding scheme provided for the issuance of securities of long maturity that would be repaid in specie Thus, his Treasury locked in longer-term funding and did not have to test continually the market's willingness to finance the new government At the same time, investors were given some assurance that holding government securities would preserve their purchasing power Those same incentives have led our present-day Treasury to issue securities across a wide range of maturities and, I am pleased to note, to begin soon to offer debt indexed to consumer prices

Fifth, and this should come as no surprise from one of the authors of the *Federalist Papers*, Hamilton explained his policies in well written, logically constructed arguments that remain pleasures to read, even two hundred years later

Hamilton's lessons speak across the generations, both to policy makers in mature democracies and those coping, as he did, with financing newly independent states If we are to protect his creation, the U S Treasury market, we must remember two facts he could not afford to forget For one, buyers of Treasury securities do so through their own volition Investors have alternatives, and more so now than ever before For another, the issuer of those securities, the U S Treasury, must finance an amount, on net, that is determined by the political judgments of the congressional and executive branches of government If the government makes purchasing its debt harder--by imposing onerous reporting or bookkeeping requirements--or riskier--by following capricious macroeconomic policies--buyers will pull back and the cost of servicing the debt will rise We at the Federal Reserve will do our part to contribute to financial stability, which is to preserve the purchasing power of money over time

To be sure, the dollar sums that preoccupied Alexander Hamilton were small The national debt totaled $75 million, or $18 per capita But the issues at stake were large I can only hope that, by following his precedent, today's policy makers show some of the same wisdom in dealing with the public debt the congressional and executive branches of government If the government makes purchasing its debt harder--by imposing onerous reporting or bookkeeping requirements--or riskier--by following capricious macroeconomic policies--buyers will pull back and the cost of servicing the debt will rise We at the Federal Reserve will do our part to contribute to financial stability, which is to preserve the purchasing power of money over time

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