Elite's grip on US bonds lays bare fiscal divide

Gillian Tett
INSIGHT

Who owns America's ever-swelling pile of government debt? This is a question that has provoked considerable angst among US politicians recently; or at least it has in relation to national identity.

Little wonder. Half a century ago, the share of US public debt held by foreigners was less than 5 per cent; but in 2008 that ratio breached 50 per cent. And while it has since fallen back slightly (because the Federal Reserve has been gobbling up bonds) the shift in ownership is nevertheless stark – along with the new power of creditors such as China.

But there is a second important point about America's debt that has hitherto received surprisingly little attention: the shifting nature of bond investors who hail from inside the US. In past decades, it has often been assumed that Treasury bonds were widely held by the public.

Bonds as a social glue

Indeed, since the days of Alexander Hamilton, who founded a strong central US Treasury, many politicians have thought (or hoped) that a broad involvement in the bond market – be that among widows, orphans, middle-class citizens or oligarchs – would be a source of common civic identity and social glue.

However, Sandy Hager, a postdoctoral research fellow at the London School of Economics, has recently crunched through the historical data. This research* suggests that if you look at the "publicly held" US government bond markets (ie the parts not held by another US government agency, such as the Fed), foreign ownership of federal bonds has risen from about 5 per cent in 1970 to 55 per cent today, at the expense of US households and business.

More specifically, the ratio of the bond market held by corporations during this period has declined from about 40 per cent to 30 per cent, while for households it has fallen from about 30 per cent to almost 15 per cent. But what is most interesting is the "household" category. Contrary to the usual assumption that government debt is widely held, Mr Hager's data suggests ownership has become far more concentrated recently, echoing a wider concentration of wealth in the US.

Back in the 1970s, for example, the richest 1 per cent of Americans "only" held 17 per cent of all the federal bonds that were in private sector hands. This was partly because during the second world war and in the immediate aftermath there was a strong attempt to distribute Treasuries widely. But since the 1980s, the proportion of debt owned by the top 1 per cent started to rise sharply, hitting 30 per cent in 2000 and 42 per cent in 2013. The last time it was this high was in 1922, when the ratio was 45 per cent.

This picture may not be entirely complete. Mr Hager himself admits that the historical data are often patchy, and it could be argued that modern citizens are also indirect owners of government debt through public agencies and pension funds, in ways that do not show in the data. But, if nothing else, this pattern gives new significance to the questions that Hamilton and other historical figures first grappled with three centuries ago: namely, is public debt a potential source of civic cohesion? Or merely a subtle way for elites to entrench their power?

Skin in the game

Mr Hager, for his part, takes the latter perspective; after all, he points out, this pattern means the richest are collecting more and more interest income, but not paying a proportionate increase in taxes.

"Over the past three decades, and especially in the context of the current crisis, the ownership of federal bonds and federal interest has become rapidly concentrated in the hands of dominant owners, the top 1 per cent of households and the 2,500 largest corporations [while] the federal income tax system has done little to progressively redistribute the federal interest income received by dominant owners," he writes. "Public debt has come to reinforce and augment the power of those at the very top of the social hierarchy," he adds, concluding that "[Karl] Marx's notion of a powerful 'aristocracy of finance' at the heart of the public debt is . . . a very real feature of the contemporary US political economy."

Even if you disagree with Mr Hager's leftwing political bent, the data certainly casts a new light on the political dynamic in the current fiscal rows.

To the wealthy elites in the US who hold government bonds, it seems self-evident that the government needs to preserve the sanctity and value of Treasuries; this group has a strong incentive to ensure this happens via fiscal reform (particularly if this entails budget cuts, rather than higher taxes.) But what is rarely debated is that millions of poor Americans have far less (or no) skin in the Treasuries game. Little wonder, then, that the debate is so polarised, and unlikely to become less so any time soon.

* *'Public Debt, Ownership and Power' by Sandy Brian Hager; unpublished PhD at York University, Canada*

gillian.tett@ft.com