

The National Debt



ECONOMICS FOCUS In 1790 the federal government owed foreign and domestic creditors \$54 million. The states owed \$25 million. The questionable ability of the nation to repay that debt jeopardized its future existence.



As you read, keep in mind that the government of the United States has never been entirely unburdened by debt.

In his capacity as secretary of the treasury, it naturally fell on Alexander Hamilton's shoulders to address the problem of the national debt. Looking to history for guidance, Hamilton seized upon the example provided by the British. In 1690 Britain had established a national bank. In establishing that bank, the British had sought to establish an entity responsible for funding, or making regular payments on, their national debt. Those payments would be made with funds collected specifically for the purpose.

The effect of that policy was understood clearly by Alexander Hamilton. In clearly establishing its willingness as well as its ability to repay creditors, the British government had given potential investors the assurances they needed to be willing to invest large sums in the government. The increased level of funding had enabled the British to establish a colonial empire, as well as a Royal Navy, which, while not unbeatable, was certainly a formidable foe.

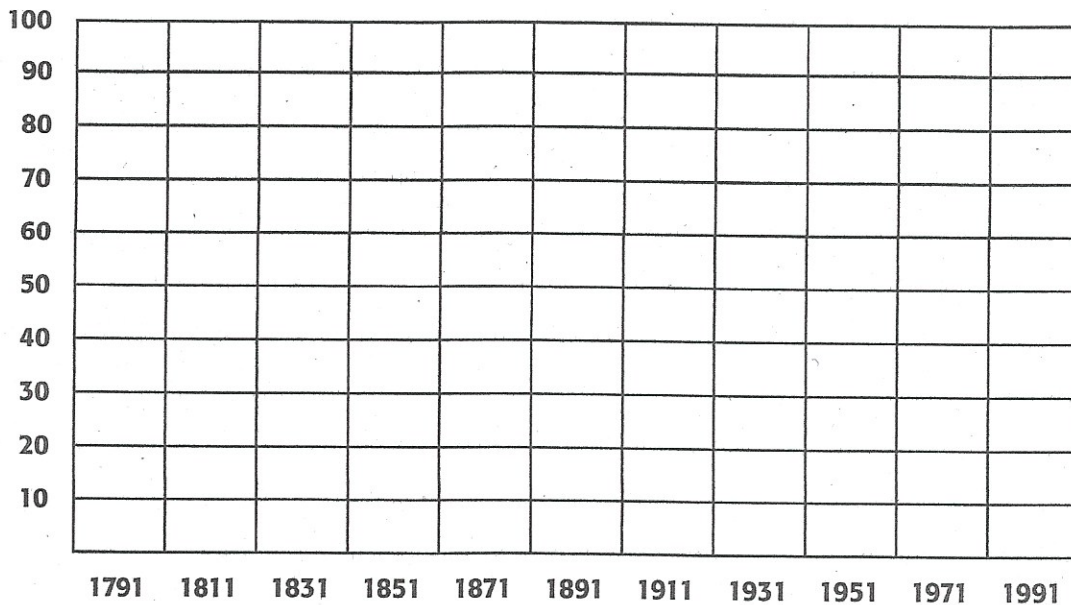
Alexander Hamilton saw in the British model the successful implementation at a national level of one very basic financial principle: access to credit is determined by one's willingness and ability to repay any debts accrued. Furthermore, Hamilton understood that the financial viability of the nation depended upon proving from the onset that the government could be trusted to live up to its word. To achieve that end, Hamilton proposed the assumption of state debts to assure a unified and consistent repayment policy. Furthermore, repayment was to be funded over a period of time so that the full value of the debts could be guaranteed to creditors. After considerable debate, as well as some backroom political maneuvering, Hamilton's policies were implemented. And though the nation has never been entirely without debt, it has proven its willingness and its ability to repay.

The National Debt, *continued*

Economics and History

Use the data in the table to create a bar graph in the space provided below. You may wish to use a different color or pattern to make the columns of your graph easier to distinguish. When you finish, answer the questions that follow.

Year	U.S. Debt as Percentage of GDP
1791	15%
1811	4%
1831	2%
1851	1%
1871	22%
1891	7%
1911	6%
1931	23%
1951	80%
1971	38%
1991	61%



WHAT DID YOU LEARN?

1. According to your graph, in what year was the debt closest to zero percent of GDP?

2. In what year was the debt the highest percentage of GDP?

3. In 1929 the Great Depression began. How did this influence the debt?

4. Consider the data provided for the years 1871 and 1951. In comparison to the data for 1851 and 1931, what can be said of the debt in the years in question? What major events occurred just prior to 1871 and 1951, respectively?

5. **Critical Thinking: Synthesis** In general, what effect do you think war tends to have on the debt as a percentage of GDP? Explain your answer.
