Point of View

**Government Shutdown vs. Debt Ceiling: The Differences and Likelihoods**

A lot is being discussed about the possible U.S. government shutdown and debt ceiling, and the talk will only increase and become especially heated in late September and likely into early October. Here is my point of view on the likelihood of these events occurring:

**DEBT CEILING/TECHNICAL DEFAULT ON U.S. TREASURIES**

**LIKELIHOOD:** less than 10%

**MARKET RISK ASSESSMENT:** Severe

This has never happened before. Market risk will likely be short lived and, if it occurred, would only be a technical default and not a default on a coupon or principal debt payment. Note also that there is no cross-default for U.S. Treasuries (i.e. a delayed coupon or principal payment on one bond does not mean ALL Treasuries (a.k.a. the issuer, the U.S. Treasury) go into default).

**GOVERNMENT SHUTDOWN**

**LIKELIHOOD:** 35% likely. The probability has been reduced from over 50% a few weeks ago because a supplemental funding bill for Hurricane Harvey might get wrapped together with an increase in the debt ceiling and a continuing resolution to fund the government.

**MARKET RISK ASSESSMENT:** Minimal

This is just politicians being politicians. Think of the 2013 shutdown over Obamacare funding versus Trump and The Wall; both very partisan and highly divisive issues. Shutdowns have happened before, and are not unprecedented. They have historically always been resolved quickly.
When assessing market risk, it is important not to conflate a government shutdown with the debt ceiling.

A shutdown would occur if Congress fails to pass legislation to authorize government spending to cover all or part of fiscal year 2018 before it begins on October 1. That legislation needs the president’s signature.

It would take a 2/3 vote in each house of Congress to override a Presidential veto of such legislation.

Key Information

The spending authorization bill is technically separate from the legislated increase in the debt limit that will be required at some point to allow the U.S. Treasury to continue fulfilling its obligations.

The debt limit is the maximum amount that the U.S. Treasury is allowed to borrow and Congressional authorization is needed to change it. It was suspended by Congress from November 2015 until March 16, 2017 and then was reinstated at a higher level. Since that time, the U.S. Treasury has used a variety of what it calls “extraordinary measures” to avoid exceeding the debt limit, but the U.S. Treasury has indicated that it will exhaust its ability to use those measures near the end of September.

For more information on the debt limit, you can visit the below which I consider a useful description of the debt limit.1


Definitions

As you may recall, the federal government experienced a shutdown in the first two weeks of October 2013 due to the failure of Congress at that point to pass a spending authorization bill, over a dispute between House Republicans and the Obama administration regarding whether to discontinue funding for the Affordable Care Act.

The shutdown subsequently ended in mid-October when Congress passed legislation that contained both a spending authorization provision and a measure to effectively raise the debt limit. That increase was needed to avert a default that would have occurred around that point if debt limit legislation did not pass.2

1 The website is provided for informational purposes only. We have not verified the information on the site, and we make no representations whatsoever as to its accuracy or completeness.

2 We acknowledge Ed Keen from the Observatory Group for his helpful insights and facts.
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