

U.S. Flash

Partisanship puts government at risk of shutdown

Once again, legislators are shuffling to reach a last-minute agreement to avoid a government shutdown, the first since President Clinton and Newt Gingrich failed to reach a budget resolution in 1995. To avoid the shutdown, the House, Senate and White House must agree on a continuing resolution, an ad hoc stop gap measure, or a longer-term resolution that would establish budget appropriations for FY2014. It is still unclear whether an agreement can be reached before the end of FY2013 (i.e., end of day on September 30th), but it is almost certain that at best, a continuing resolution could be reached that would appropriate resources to existing federal programs at post-sequestration rates (\$986B). Moreover, current resolutions passed by the House do not include a statutory increase in the Treasury's borrowing capacity (debt-ceiling) and were amended to include riders that delay and defund the Affordable Care Act (ACA) and repeal the tax on medical devices. As a result, it is unlikely that any of the current proposals will receive enough bipartisan support to avoid the partial government shutdown.

- **Essential programs to operate if no agreement is reached**

Without the passage of a continuing resolution before the end of FY2013, the federal government will partially shut down. Programs deemed essential by the U.S. government such as air traffic control, border security, food inspections and the U.S. Postal Service would continue to operate under this scenario. In addition, entitlement programs are not considered during the annual budgeting process and as a result payment to Social Security, Medicare and Medicaid recipients will occur regardless.

- **Amendments to the continuing resolution reduce the probability of passage**

The Democrats' insistence on a clean continuing resolution could soften if Republicans are willing to eliminate provisions that would defund or delay ACA or if there are firmer, non-contingent increases to the Treasury's statutory borrowing limit. One resolution that could be a part of a ratified continuing resolution is the elimination of the medical device tax, which has bipartisan support. However, any resolution that alters the implementation of the ACA would almost assuredly be dead in the Senate, and if passed, would be vetoed immediately by President Obama. Moreover, language that ties statutory increases in the debt-ceiling to spending cuts would also face challenges from the White House and Senate.

- **The duration of the government shutdown will determine the extent of the damage**

If Congress fails to pass a continuing resolution, hundreds of thousands of government workers could be furloughed. Some estimates suggest that during the most recent government shutdown in 1995 800,000 jobs were furloughed in the first four days. Moreover, the estimated cost of the 21-day shutdown was \$1.94B (in 2012 dollars); however, it is unclear whether a shutdown now would have lasting economic consequences given that furloughed wages are most likely to be paid retroactively. Nevertheless, further evidence of political brinksmanship and another failure by the U.S. Congress to respond to a fiscal crisis could force credit agencies to revisit and possibly downgrade the U.S. credit rating. As a result, policy uncertainty could return to levels seen during the lead-up to the fiscal cliff and debt-ceiling debates of 2011 which threatens to derail an economy that is still vulnerable to policy-related shocks ([see our latest sequestration watch](#)). Our baseline scenario of 1.8% annual growth for 2013 does not assume a government shutdown of any duration, and thus a longer government shutdown implies a greater bias to the downside for 2H13 growth.

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