

Economic Briefing

# Another US shutdown is looming

**If Congress does not reach an agreement, the US government will run out of money on Friday. Many agencies that do not perform critical functions would then have to close. Taken for itself, this would only put a slight dampener on the US economy. However, it would come at an inopportune time due to the already high level of uncertainty.**

## It's getting tight again...

Congress must agree on a new Continuing Resolution (CR) to keep the US government funded this week. Otherwise, government agencies risk closure at midnight on Friday (a so-called shutdown, see box below).

The Republican speaker of the House of Representatives, Mike Johnson, wants to put a six-month stopgap funding measure to the vote today. This essentially continues current spending, but wants to cut funding for the IRS by \$20 billion and increase spending on defense and immigration control slightly. Johnson has apparently been able to win the approval of the Freedom Caucus, the hard line wing of Republicans in the House, which increases his chances.

## ... and a majority in Congress is difficult to achieve

The Republicans only have a narrow majority of 218 to 214 votes in the House of Representatives (3 of the 435 seats are currently vacant). If the Democrats are united in their opposition to the package – and they are likely not happy about cuts to the IRS – Johnson can hardly afford any defections from his own ranks.

However, the necessary approval in the Senate is probably an even bigger problem. This is because a majority of 60 of the 100 votes is required there. The Republicans have 53 senators – and at least one has already promised a no vote. So far, only one Democrat has signaled his approval. It is unclear whether enough other Democratic senators will vote in favor to help the bill cross the 60-vote threshold.

Bipartisan cooperation is difficult because the Democrats are strongly opposed to the radical program of cuts to federal agencies implemented by the Trump administration. For example, the USAid development agency has been closed, Trump also wants to abolish the Department of Education and lay off tens of thousands of public sector workers. The betting markets therefore price in a 53% probability of a shutdown in 2025.

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### Table of contents

It's getting tight again...	1
... and a majority in Congress is difficult to achieve	1
Shutdown would come at a very inopportune time	2
Box: SHUTDOWN	2



However, if the Democrats refuse to give their consent, they risk being blamed by the Republicans for a shutdown. In the past, the party that was publicly perceived as causing a shutdown was politically damaged. However, it is questionable whether the Democrats will buckle in the face of the administration's aggressive behavior. Should they insist on concessions from the Republicans, for example on the budget cut for the IRS, the Republicans' approval for a CR could in turn falter.

## Shutdown would come at a very inopportune time

A shutdown has been looming on several occasions before. Even when government agencies had to close their doors for a short period, the economic impact was relatively minor. This time, however, a shutdown would come at a very inopportune moment. Business and consumer sentiment is already on the back foot due to the Trump administration's erratic economic policy, and the stock markets are under pressure. Uncertainty is currently extremely high, and fears of a US recession have increased sharply.

### Box: SHUTDOWN

The federal government often operates without a regular budget; since 1976, a budget has only been passed in time for the start of the fiscal year on October 1 in four cases. In these cases, a short-term stopgap financing measure, known as a Continuing Resolution (CR), is used. The current CR expires at midnight on Friday, March 14.

If Congress has not agreed on a new CR by then, government agencies face closure (shutdown). Since 1976, there have been 21 such shutdowns. The last – and so far longest – shutdown ended after 34 days in January 2019 (Chart 1).

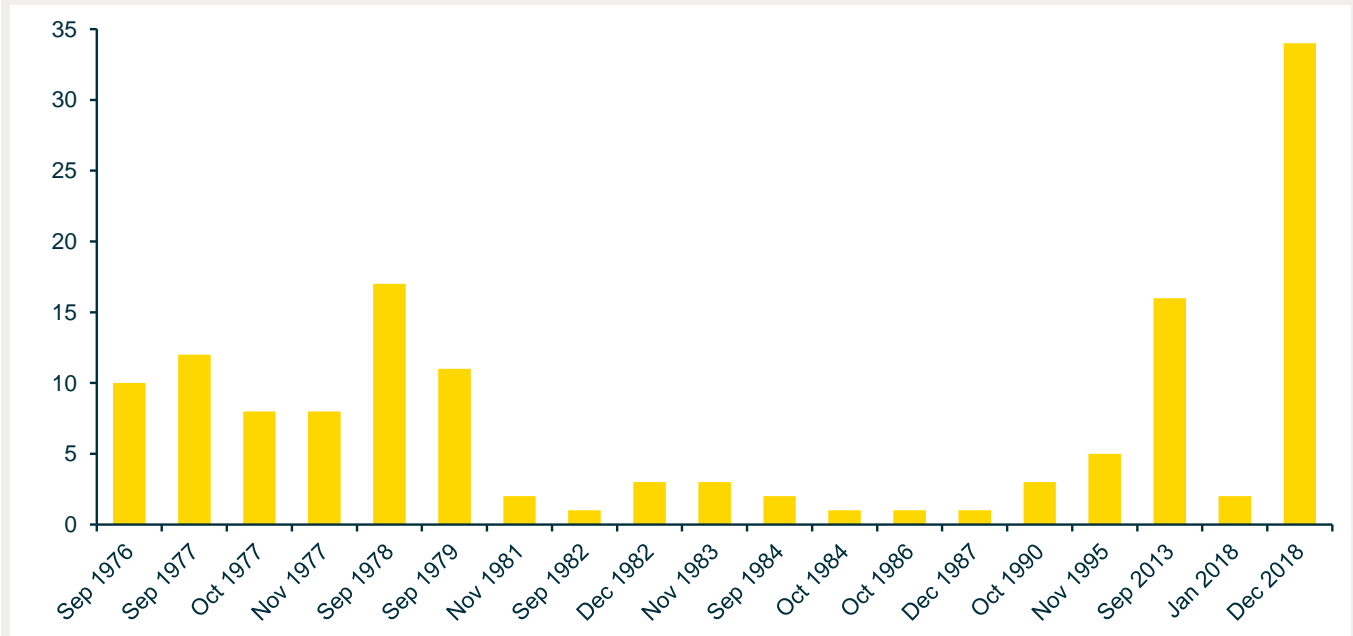
Without statutory approval of expenditure, the government ceases “non-essential” operations and sends federal employees on unpaid forced leave. However, the personnel necessary for central tasks such as defense or internal security remain in their posts without pay. In addition to these “essential” tasks, expenditure required by law, such as social security payments, also continues.

Possible consequences of a shutdown are:

- Because ultimately only a small part of the administration and spending is affected, the direct impact on growth is likely to be small, especially since furloughed employees have always received back pay. For example, the Congressional Budget Office (CBO) **estimates** that the last shutdown, at the turn of the year 2018/19, reduced gross domestic product by 0.2 percentage points in the first quarter of 2019. Most of this was later recovered, so the overall effect was negligible.
- From the point of view of the financial markets, it is important that debt service would not be affected by a shutdown. So interest payments and repayments would be guaranteed for US government bonds.
- Statistics agencies such as the Census Bureau (responsible for data such as new orders or housing starts) and the Bureau of Labor Statistics (labor market and price data) are affected by a shutdown. A lengthy shutdown could, for example, delay the publication of the next employment report.

**Chart 1 - 50 years of shutdowns**

Shutdown of federal government agencies, length in days



Source: House of Representatives, Commerzbank Research



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