



A Government Shutdown Would Pose a Small Threat to Markets

Theatrics aside, a budget agreement seems likely in the near term.

September 2023

KEY INSIGHTS

- T. Rowe Price legislative analyst Gil Fortgang believes that a possible government shutdown poses a manageable threat to markets.
- The Senate's earlier passage of appropriations bills underscores the lack of will for a prolonged closure of federal agencies.
- Republican House Speaker Kevin McCarthy is likely to turn to continuing resolutions to fund the government until an omnibus spending package is negotiated.



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With the end of the federal government's fiscal year approaching on September 30, the possibility has grown that Congress will not authorize funding past that date. If Congress fails to act, the result would be the shutdown of some government agencies and the furloughing of their employees for the 11th time since 1980.

While he is monitoring the situation closely, T. Rowe Price legislative analyst Gil Fortgang does not expect any shutdown to have a significant impact on the economy or markets. Gil points to two primary reasons for optimism:

1. The lack of will for a political showdown makes any prolonged shutdown unlikely. The most conservative members of the Republican House Caucus have made clear their determination to gain concessions from the White House before approving spending bills for fiscal year 2024. But Gil

notes that this group probably represents only around a third of the Republican House majority, which itself is razor thin.

Moreover, the Republican House does not have a Republican Senate on its side, as was the case with the prolonged shutdown in late 2018 and early 2019 (the Democrats regained the House majority in early 2019). Indeed, Senate Republicans have already cooperated with Democrats in passing the necessary 12 appropriations bills to fund the government over the coming year.

2. Even a prolonged shutdown, while improbable, would probably have only a minimal impact on the economy. This is primarily because furloughed workers, while they would certainly feel a short-term impact, would be highly likely to receive back pay, as was the case with the 35-day shutdown that began in late 2018. The Congressional Budget Office

later estimated that this shutdown, the longest in history, cost the federal government USD 11 billion and slowed growth by 0.1% in the fourth quarter of 2018 and by 0.2% in 2019.

To put all these numbers in perspective, as of June, the Congressional Budget Office was estimating that the federal government would spend around USD 24.3 trillion in the fiscal year ending on September 30.

Given that time has probably already run out for the House to craft 12 appropriations bills, Gil envisions two likely scenarios over the coming weeks:

1. A shutdown is avoided after Republican House Speaker Kevin McCarthy manages to get his caucus to agree to a series of continuing resolutions to fund the government at existing (fiscal year 2023) levels. This would allow time to craft an omnibus bill that closely resembles the spending limits agreed to as part of the extending the federal debt limit in early June. Gil believes this may be possible given the willingness of many Republican House members to

secure an agreed-upon 3% increase in defense spending by agreeing to no substantial cuts in other forms of discretionary outlays.

2. The other likely scenario, in Gil's opinion, is that **a brief shutdown of perhaps several days occurs** before Speaker McCarthy manages to persuade enough members of his caucus to support a continuing resolution. Gil estimates this situation may then persist for several weeks, perhaps into November, before a full set of appropriations bills is secured. The result would be a small but manageable fiscal drag.

While Gil believes that shutdown negotiations have generally become a form of regrettable but short-lived political theater, he does acknowledge that the deepening divide between the parties has consequences for individuals and companies. In particular, he will be paying close attention to the fate of the White House's request for USD 40.1 billion in supplemental spending for funding defense and humanitarian aid to Ukraine along with disaster relief for Florida and Hawaii.

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