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Joseph Lavorgna, Chief US Economist | 212.893.1528 | joseph.lavorgna@smbcnikko-si.com

Center Stage: The Debt Ceiling Debate

Over the weekend, Secretary Yellen repeated that the Treasury will lose its ability to use “extraordinary measures” as soon as June 1st to fund the government. Our best guess is that **Treasury could extend this “soft” deadline to the following week, probably until Friday June 9th but not much further**. The Treasury would lose credibility if the old, late July deadline was reimposed. The Congressional Budget Office also gave a similar deadline.

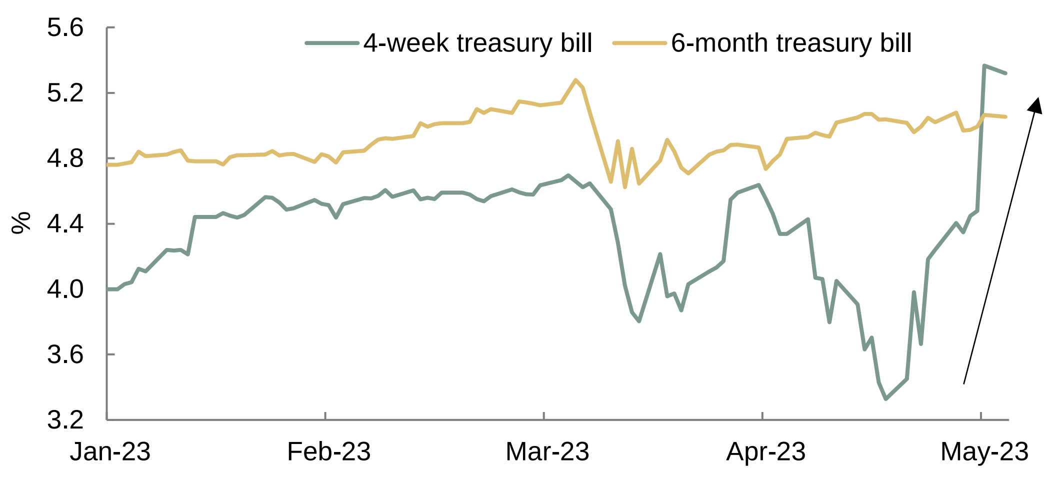
Tomorrow, President Biden meets with GOP House Leader McCarthy, Minority Leader Jeffries as well as Senators Schumer and McConnell. A deal extending beyond the 2024 Presidential Election is going to happen, but it may still come down to the 11th hour as almost all debt ceiling battles have in the past. The fact that a recent ABC News/Washington Post poll shows the public placing nearly equal blame on each side in the event of default is one key reason why it will not happen. But there is another factor to consider as well.

The Republicans only have a nine seat majority which means Speaker McCarthy can afford to lose only four votes. This was not the case in 2011 when the GOP held a record 49 seat majority. Back then, Speaker Boehner had to contend with a vocal “tea party” caucus that wanted substantial spending cuts from the Obama Administration. Implicitly, this made a deal more difficult as the GOP struck a hard stance.

Aside from today’s much smaller majority, **there are 18 current GOP House members that come from districts that Biden won**. As we get closer to the early June X-date and financial markets likely tumble, GOP “moderates” may force a deal.

However, **the fact we expect a debt ceiling agreement does not mean one is imminent**. History tells us that deals do not get done until the last minute. There is no reason to think time will be different. As we can see in the chart below, the Treasury market shares this view.

The four-week treasury bill is yielding substantially more than the six-month treasury bill, an oddity that reflects a nonzero probability of a missed interest payment or technical default. The sooner an agreement is brokered, the better for the economy and financial markets.



Sources: FRB, Haver, SMBC Nikko

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