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# Debt Limit Analysis

JULY 2011

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- **Congress does not raise the debt limit before recessing on August 5, 2011**
- **Estimates for daily receipts and payments constructed from publicly available data from Daily Treasury Statements**

**1. What is the date after which Treasury will not have sufficient cash to pay ALL of its bills (the “X Date”)?**

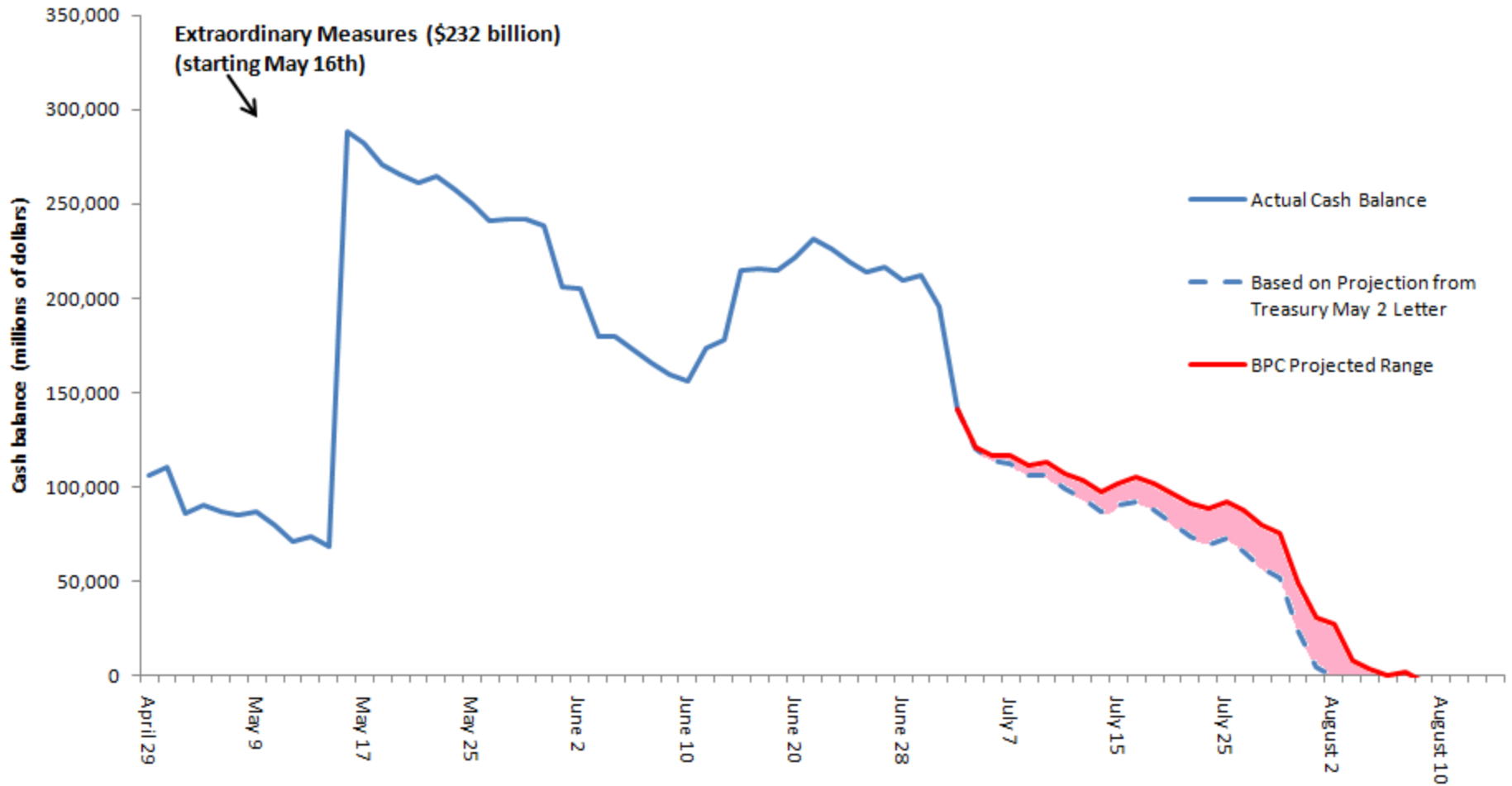
**If we pass the X Date, and Treasury is forced to “prioritize” its payments to avoid a debt default:**

**2. What would be the effects on government operations?**

**3. What would be the market risks?**

- **The X Date is the date after which Treasury can no longer pay all of its bills**
  - After X Date, bills must be paid solely out of incoming cash flows
  
- **On May 2, Secretary Geithner estimated that the X Date will be August 2, adding:**
  - *"This is a projection and is subject to change based on government receipts and other factors during the next three months."*

### Treasury Cash Balance - April 29th, 2011 to "X Date"



- **Our analysis also shows that the X Date will fall on August 2**
  - On July 1<sup>st</sup>, Treasury publicly reaffirmed their estimate of the X Date as August 2
- **The 14<sup>th</sup> Amendment does not provide a reasonable basis for challenging the constitutionality of the debt ceiling**
  - The Administration will not attack the debt ceiling on this basis
- **Treasury has no secret bag of tricks to finance government operations past August 2**
  - Treasury will not attempt to “firesale” assets during a crisis
  - Other ideas are impractical, illegal and/or inappropriate (gold loans, IOUs)



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# Prioritization

- **There is no precedent; all other debt limit impasses have been resolved without passing the X Date**
  - Treasury has never failed during a debt limit impasse to meet any payment obligation
- **The government shutdown of 1995 – 96 does not provide a precedent:**
  - Mandatory spending continued without interruption
  - Defense, Transportation, Treasury, and legislative branch spending was fully appropriated
  - Disruption of government services was modest



- **Rating agencies:**
  - **S&P:** “[If you] prioritize payments ... you would have to contract your payments in a massive way overnight [creating a] very sharp negative fiscal impulse.” (4/18/11: Credit Watch Negative)
  - **Fitch:** “If the debt ceiling is not raised ... and timely and full payment of its obligations, including Treasuries, is not secure, the U.S. sovereign rating will be placed on Rating Watch Negative.”
  - **Moody’s:** “ ...the probability of a default on interest payments [is] low but no longer de minimis. An actual default, regardless of duration, would fundamentally alter Moody’s assessment ... and an Aaa rating would likely no longer be appropriate.”
- **Bernanke concurs:**
  - “[Going past the X Date] would no doubt have a very adverse effect very quickly on the recovery. I’m quite certain of that.”

- **Treasury would have to choose from among 80 million monthly payments so that 40-45% of bills are not paid**
  - Inflows and outflows do not match up well and are quite “lumpy,” as our daily analysis shows
- **The reality would be chaotic:**
  - Unfair results, unanswered questions
  - Treasury picking winners and losers
  - Public uproar
  - Intense global media focus
- **We assume that Treasury would nonetheless be forced to attempt to “prioritize” payments despite difficulty of doing so**

## Two areas of risk evaluation:

- Effect on Federal Government operations
  - Month of August
  - Day by day analysis
- Market Risk



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# August 2011 Analysis

Month/Year	Inflows	Outflows	Deficit	Business Days
August 2009	173,254	316,299	143,045	21
August 2010	194,280	342,381	148,101	22
August 2011*	203,327	362,674	159,348	23
Truncated (3 <sup>rd</sup> – 31 <sup>st</sup> ) August 2011*	<u>172,400</u>	<u>306,713</u>	<u>134,312</u>	21

All numbers are pro forma for the exclusion of net debt issuance

\* BPC Projections (in millions of dollars)

## If you choose to pay...

Program	Cost
Interest on Treasury Securities	<b>\$29.0 b</b>
Social Security Benefits	<b>\$49.2 b</b>
Medicare / Medicaid	<b>\$50.0 b</b>
Defense Vendor Payments	<b>\$31.7 b</b>
Unemployment Insurance Benefits	<b>\$12.8 b</b>

For a total of **\$172.7 billion**

## Then you can't fund these programs, worth **\$134 b...**

Program	Cost
<i>Military Active Duty Pay</i>	<b>\$2.9 b</b>
<i>Veterans Affairs Programs</i>	<b>\$2.9 b</b>
<i>Federal Salaries + Benefits</i>	<b>\$14.2 b</b>
<i>Dep. of Education (e.g., Pell grants, special ed. programs)</i>	<b>\$20.2 b</b>
<i>Food/Nutrition Services + TANF</i>	<b>\$9.3 b</b>
<i>Dep. of Labor (e.g., training and employment services)</i>	<b>\$1.3 b</b>
<i>Dep. of Justice (e.g., FBI, federal courts)</i>	<b>\$1.4 b</b>
<i>Dep. of Energy (e.g., energy research, national nuclear programs)</i>	<b>\$3.5 b</b>
<i>Health and Human Services Grants</i>	<b>\$8.1 b</b>
<i>Federal Highway Administration</i>	<b>\$4.3 b</b>
<i>Environmental Protection Agency</i>	<b>\$0.9 b</b>
<i>IRS Refunds</i>	<b>\$3.9 b</b>
<i>Small Business Administration</i>	<b>\$0.3 b</b>
<i>Federal Transit Administration</i>	<b>\$1.3 b</b>
<i>HUD Programs (e.g., housing assistance for the poor)</i>	<b>\$6.7 b</b>
<i>Other Spending</i>	<b>\$52.8 b</b>

Inflows: ----- \$172.4 b

Outflows: ----- \$306.7 b

Running Total:

• Interest on Treasury Securities:	\$29.0 b	
• Social Security Benefits:	+ 49.2 b	78.2 b
• Medicare/Medicaid:	+ 50.0 b	128.2 b
• Defense Vendor Payments:	+ 31.7 b	159.9 b
• Unemployment Insurance Benefits:	+ 12.8 b	172.7 b
• Military Active Duty Pay:	+ 2.9 b	175.6 b
• Veterans Affairs Programs:	+ 2.9 b	178.5 b
• IRS Refunds:	+ 3.9 b	182.4 b
• Food/Nutrition Services + TANF:	+ 9.3 b	191.7 b
• Federal Salaries + Benefits:	+ 14.2 b	205.9 b
• Small Business Administration:	+ 0.3 b	206.2 b
• Education Department:	+ 20.2 b	226.4 b
• Housing and Urban Development Programs:	+ 6.7 b	233.1 b
• Other Spending*:	+ 73.6 b	306.7 b
<b>TOTAL</b>	<b>306.7 b</b>	<b>306.7 b</b>

\*e.g., Justice, Labor, General Services Administration, Commerce, NASA, Health and Human Services, Energy, EPA, Interior, Federal Transit Administration, Federal Highway Administration, AID, etc.



## If you choose to pay...

Program	Cost
Interest on Treasury Securities	<b>\$29.0 b</b>
Social Security Benefits	<b>\$49.2 b</b>
Medicare / Medicaid	<b>\$50.0 b</b>
Food/Nutrition Services + TANF	<b>\$9.3 b</b>
HUD Programs (e.g. housing assist. for the poor)	<b>\$6.7 b</b>
Veterans Affairs Programs	<b>\$2.9 b</b>
Unemployment Insurance Benefits	<b>\$12.8 b</b>
Special Education Grants	<b>\$3.6 b</b>
Tuition Assistance	<b>\$10.4 b</b>

For a total of **\$173.9 billion**

## Then you can't fund these programs, worth **\$132.8 b...**

Program	Cost
<i>Military Active Duty Pay</i>	<b>\$2.9 b</b>
<i>Defense Vendor Payments</i>	<b>\$31.7 b</b>
<i>Federal Salaries + Benefits</i>	<b>\$14.2 b</b>
<i>Dep. of Education (e.g., Pell grants, special ed. programs)</i>	<b>\$6.2 b</b>
<i>Dep. of Labor (e.g., training and employment services)</i>	<b>\$1.3 b</b>
<i>Dep. of Justice (e.g., FBI, federal courts)</i>	<b>\$1.4 b</b>
<i>Dep. of Energy (e.g., energy research, national nuclear programs)</i>	<b>\$3.5 b</b>
<i>Health and Human Services Grants</i>	<b>\$8.1 b</b>
<i>Federal Highway Administration</i>	<b>\$4.3 b</b>
<i>Environmental Protection Agency</i>	<b>\$0.9 b</b>
<i>IRS Refunds</i>	<b>\$3.9 b</b>
<i>Dep. of Interior</i>	<b>\$1.2 b</b>
<i>Federal Transit Administration</i>	<b>\$1.3 b</b>
<i>Centers for Disease Control</i>	<b>\$0.5 b</b>
<i>Other Spending</i>	<b>\$51.4 b</b>

Inflows: ----- **\$172.4 b**

Outflows: ----- **\$306.7 b**

Running Total:

• Interest on Treasury Securities:	\$29.0 b	
• Social Security Benefits:	+ 49.2 b	<i>78.2 b</i>
• Medicare/Medicaid:	+ 50.0 b	<i>128.2 b</i>
• Food/Nutrition Services + TANF:	+ 9.3 b	<i>137.5 b</i>
• Housing and Urban Development Programs:	+ 6.7 b	<i>144.2 b</i>
• Veterans Affairs Programs:	+ 2.9 b	<i>147.1 b</i>
• Unemployment Insurance Benefits:	+ 12.8 b	<i>159.9 b</i>
• Special Education Grants	+ 3.6 b	<i>163.5 b</i>
• Tuition Assistance	+ 10.4 b	<i>173.9 b</i>
<hr style="border-top: 1px dashed red;"/>		
• Defense Vendor Payments:	+ 31.7 b	<i>205.6 b</i>
• Military Active Duty Pay:	+ 2.9 b	<i>208.5 b</i>
• IRS Refunds:	+ 3.9 b	<i>212.4 b</i>
• Federal Salaries + Benefits:	+ 14.2 b	<i>226.6 b</i>
• Other Education Department:	+ 6.2 b	<i>232.4 b</i>
• Other Spending*:	+ 73.9 b	<i>306.7 b</i>
<b>TOTAL</b>	<b>306.7 b</b>	<b>306.7 b</b>

\*e.g., Justice, Labor, General Services Administration, Commerce, NASA, Health and Human Services, Energy, EPA, Interior, Federal Transit Administration, Federal Highway Administration, AID, etc.

- ***Housing/Urban Development* – \$6.7b total**
  - Rental assistance: **\$3.9 billion**
  - Public Housing Fund (operates and maintains public housing areas for 1.2 million American households): **\$900 million**
  
- ***Dep. of Education* – \$20.2b total**
  - Federal Pell grants (tuition assistance for qualifying college students): **\$10.4 billion**
  - Special education state grants: **\$3.6 billion**
  
- ***Food and Nutrition Services* – \$6.7b total**
  - Food stamps, Child nutrition programs, and the Women, Infants, and Children program: **\$6.7 billion**

To create your own scenario, visit this link, which we developed jointly with Bloomberg Government:

**[Try It Yourself](http://bit.ly/pAorgl)**

**<http://bit.ly/pAorgl>**

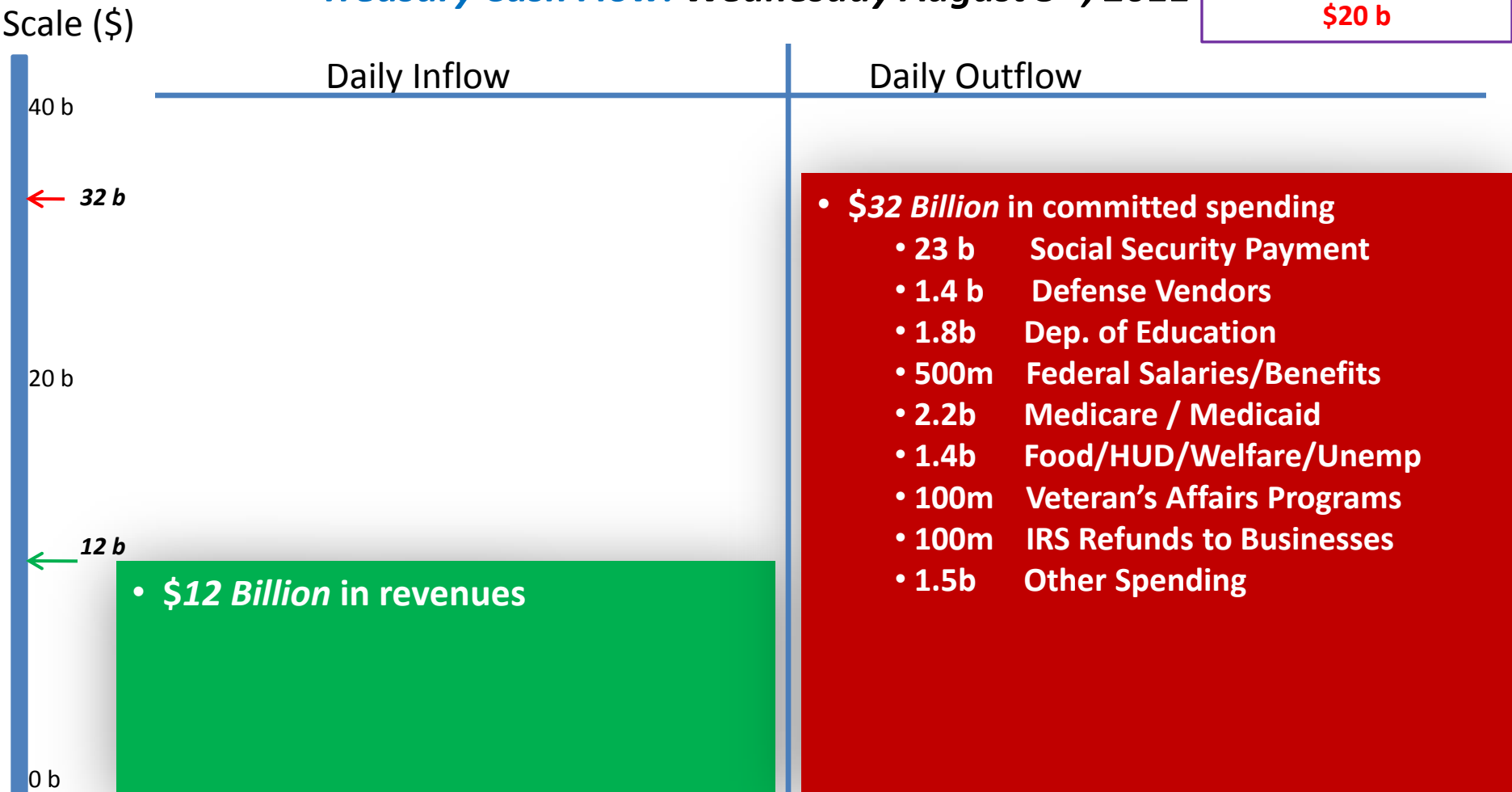


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# Daily Analysis: August 3<sup>rd</sup> – 15<sup>th</sup>, 2011

**Treasury Cash Flow: Wednesday August 3<sup>rd</sup>, 2011**

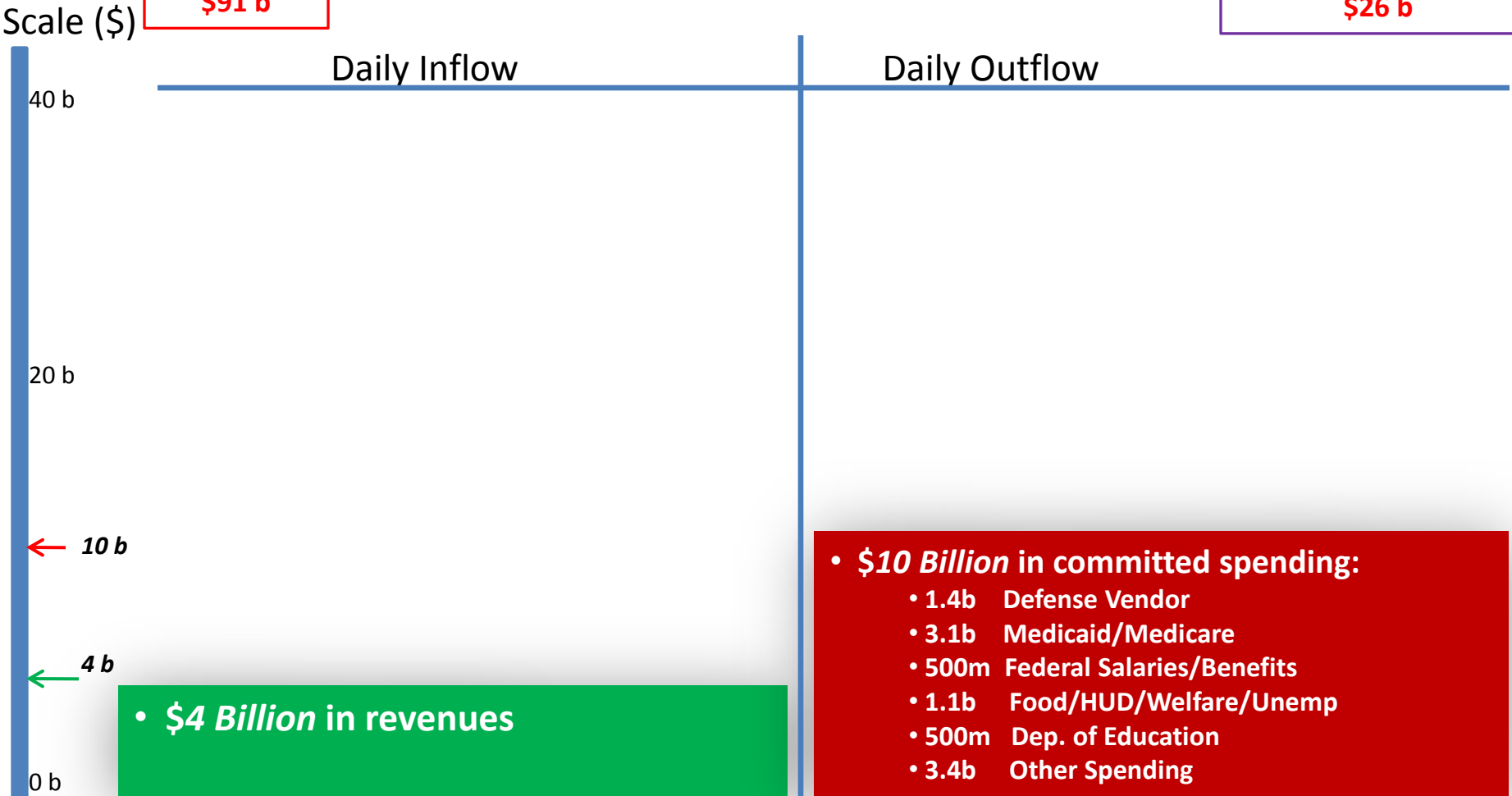
Running Cash Deficit:  
**\$20 b**



Debt Maturing:  
**\$91 b**

### Treasury Cash Flow: Thursday August 4<sup>th</sup>, 2011

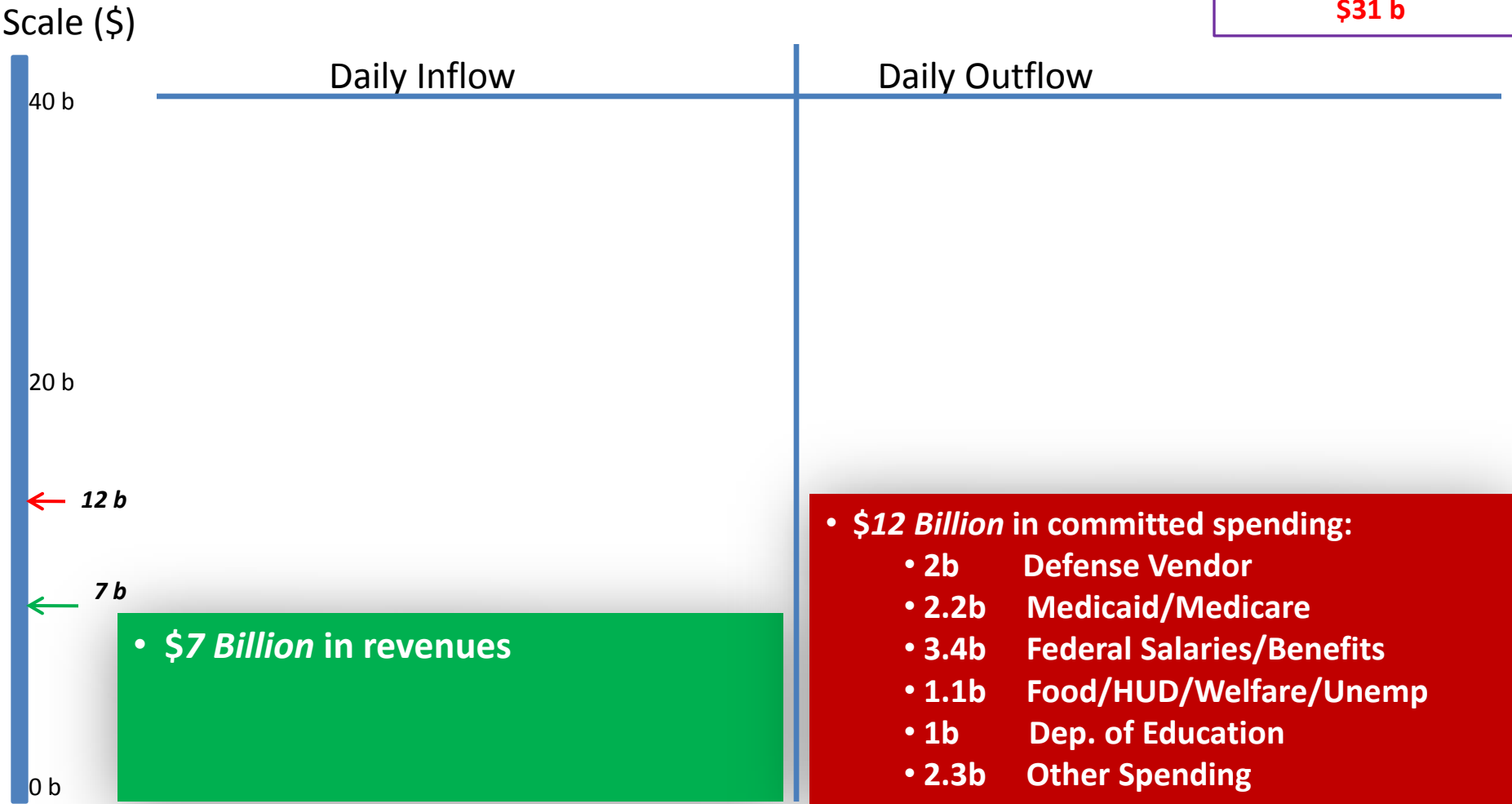
Running Cash Deficit:  
**\$26 b**





**Treasury Cash Flow: Friday August 5<sup>th</sup>, 2011**

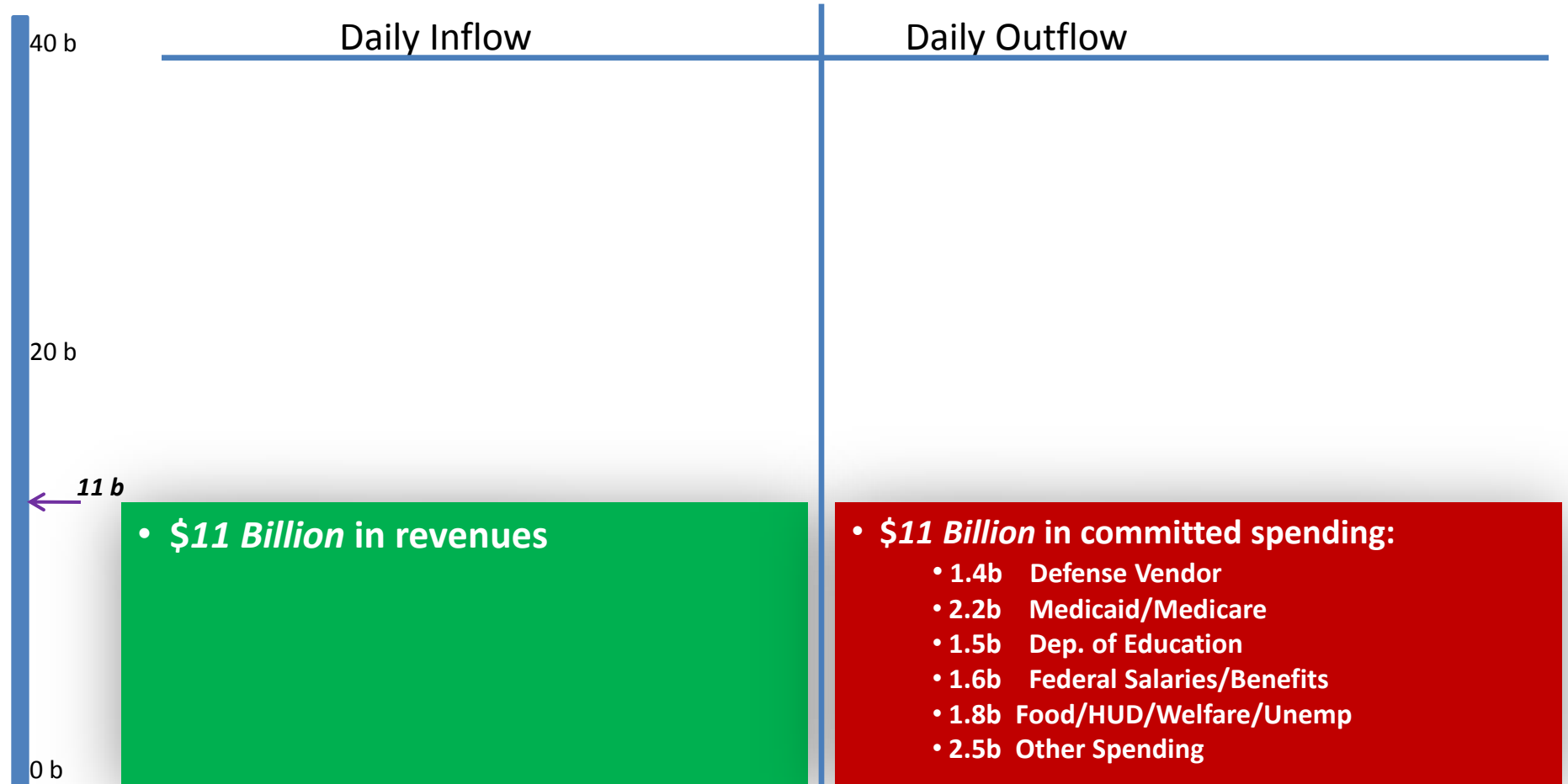
Running Cash Deficit:  
**\$31 b**



**Treasury Cash Flow: Monday August 8<sup>th</sup>, 2011**

Running Cash Deficit:  
**\$31 b**

Scale (\$)



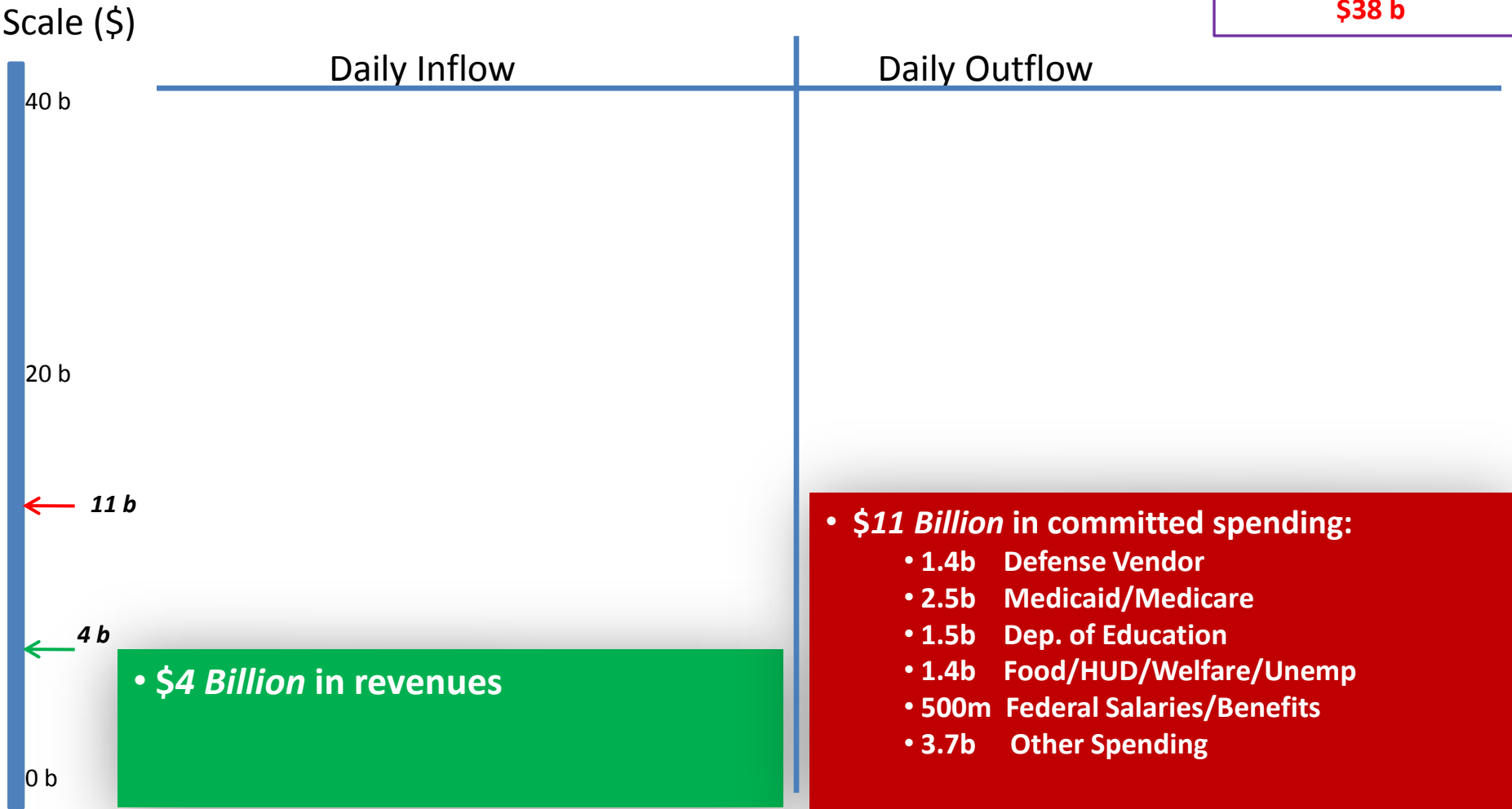
• **\$11 Billion** in revenues

• **\$11 Billion** in committed spending:

- 1.4b Defense Vendor
- 2.2b Medicaid/Medicare
- 1.5b Dep. of Education
- 1.6b Federal Salaries/Benefits
- 1.8b Food/HUD/Welfare/Unemp
- 2.5b Other Spending

**Treasury Cash Flow: Tuesday August 9<sup>th</sup>, 2011**

Running Cash Deficit:  
**\$38 b**



### Treasury Cash Flow: Wednesday August 10<sup>th</sup>, 2011

Running Cash Deficit:  
**\$47 b**

Scale (\$)

Daily Inflow

Daily Outflow

40 b

20 b

← 19 b

← 10 b

• \$10 Billion in revenues

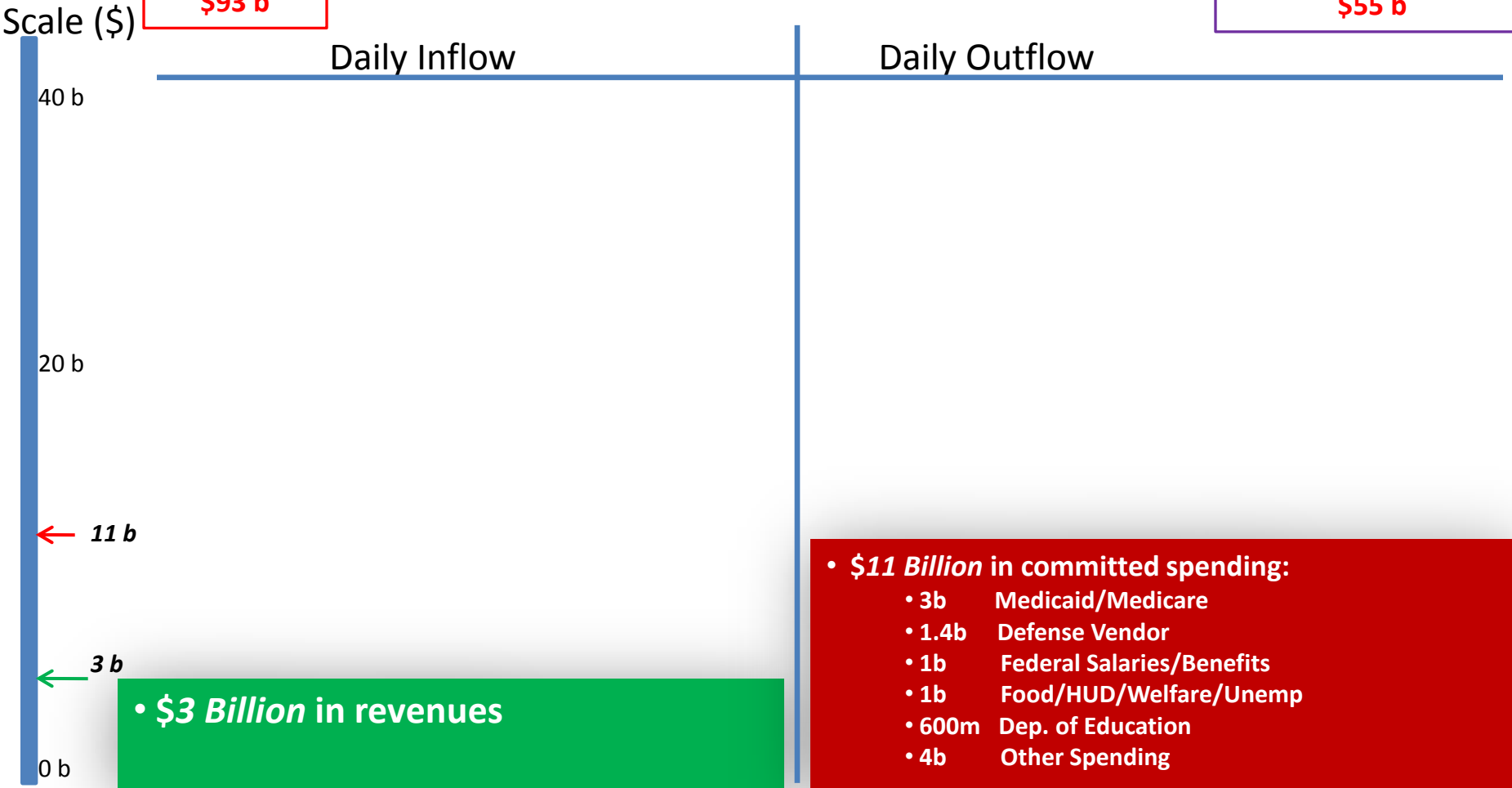
• \$19 Billion in committed spending:

- 8.5b Social Security
- 1.4b Defense Vendor
- 2.2b Medicaid/Medicare
- 1.4b Food/HUD/Welfare/Unemp
- 800m Dep. of Education
- 500m Federal Salaries/Benefits
- 4.2b Other Spending

Debt Maturing:  
**\$93 b**

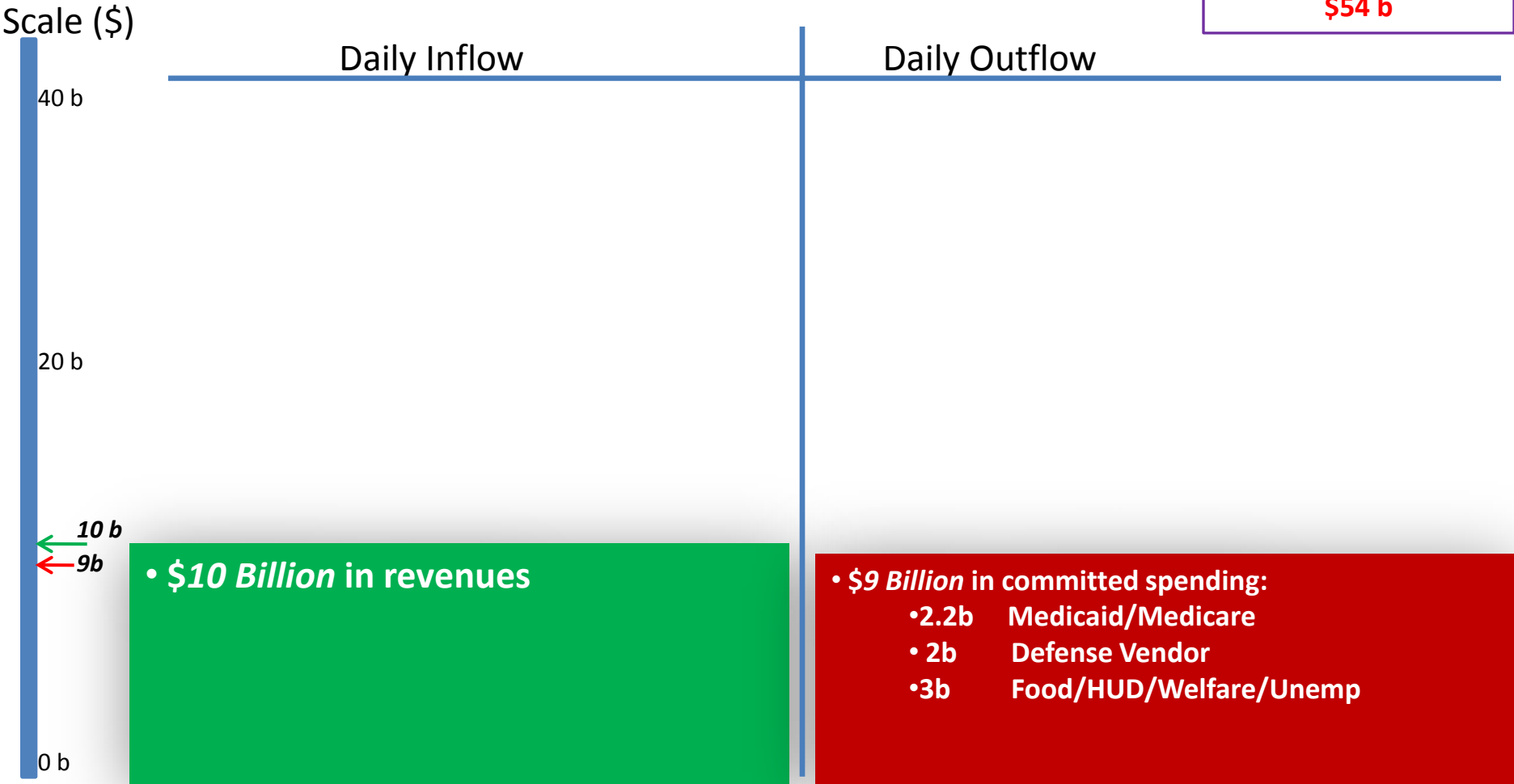
### Treasury Cash Flow: Thursday August 11<sup>th</sup>, 2011

Running Cash Deficit:  
**\$55 b**



**Treasury Cash Flow: Friday August 12<sup>th</sup>, 2011**

Running Cash Deficit:  
**\$54 b**



Debt Maturing:  
**\$27 b**

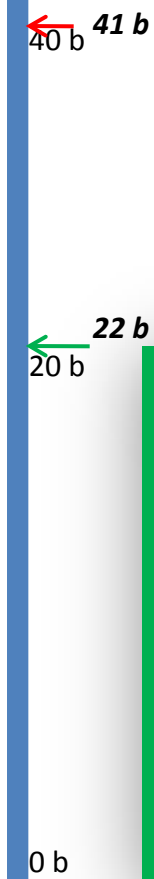
**Treasury Cash Flow: Monday August 15<sup>th</sup>, 2011**

Running Cash Deficit:  
**\$74 b**

Scale (\$)

Daily Inflow

Daily Outflow



- **\$41 Billion** in committed spending:
  - **29b** Interest Payment
  - **2.2b** Medicaid/Medicare
  - **1.4b** Defense Vendor
  - **500m** Federal Salaries/Benefits
  - **2.1b** Food/HUD/Welfare/Unemp
  - **800m** Dep. of Education
  - **200m** IRS Refunds
  - **1.8b** Other Spending

- **Handling *all* payments for important and popular programs (e.g., Social Security, Medicare, Medicaid, Defense, active duty pay) will quickly become impossible**
- **Economic disruption:**
  - Immediate 44% cut in federal spending would affect broader economy
  - Many service providers unpaid
    - Medicare and Medicaid providers
    - Defense vendors
  - Individuals not receiving government checks
  - Widespread uncertainty as decisions are made day by day





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# Market Risk

- **Treasury must “roll over” almost \$500 b in debt that matures during August 2011**
  - When a Treasury security matures, Treasury must pay back the principal plus interest due. Under normal circumstances, Treasury would simply “roll over” the security
  - As one security matures, the principal + interest for that security would be paid for with cash from the issuance of a new security
  
- **During prioritization, this operation may not run as smoothly**
  - Two elements of market risk:
    - Treasury will have to pay higher interest rates to attract new buyers
    - It is possible, if unlikely, that not enough bidders would appear

## Securities Maturing in August 2011

Maturity Date	Amount (billions of dollars)
8/4	90.8
8/11	93.3
8/15	26.6
8/18	87.0
8/25	112.0
8/31	60.8
<b><i>SUM</i></b>	<b><i>470.5</i></b>

Based on actual maturities for all securities, except for our conservative estimates of one month bills to be issued in July 2011

- **If the debt ceiling is not raised by August 2, all three ratings agencies will put the United States on watch for a downgrade, at a minimum**
- **An actual downgrade could cause major losses among holders**
- **Even without downgrade, it is likely that rates would increase, perhaps significantly**
  - Less likely, but possible, that Treasury would lose market access during such an unprecedented event and default

## Conclusions

- **The risks are real:**
  - The Treasury market, interest rates
  - Level and status of the dollar
  - Our economy
  - The global financial system
  
- **No guarantee of the outcome; risks are risks**



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