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Shutdown Would Shave Fourth-Quarter U.S. Growth as Much as 1.4%

By Jeanna Smialek and Ian Katz - September 27, 2013

A shutdown of the U.S. government would reduce fourth-quarter economic growth by as much as 1.4 percentage points depending on its length, economists say, as government workers from park rangers to telephone receptionists are furloughed.

Mark Zandi of Moody's Analytics Inc. estimates a three-to-four week shutdown would cut growth by 1.4 points. Moody's projects a 3 percent rate of growth in the fourth quarter without a closure. A two-week shutdown starting Oct. 1 could cut growth by 0.3 percentage point to an annualized 2.3 percent rate, according to St. Louis-based Macroeconomic Advisers LLC.

A shutdown would slow the expansion because output lost when workers are furloughed subtracts from gross domestic product. The combined prospect of a budget standoff between the White House and Congress and haggling over the debt ceiling could have a bigger impact on the economy as businesses hold off on investment and households delay spending.

"What we have is a political and not economic maelstrom," said **Bernard Baumohl, chief global economist at Economic Outlook Group LLC** in Princeton, New Jersey. "What everyone is watching right now is if the uncertainty is affecting consumer and business psychology, that they are postponing spending until they get more clarity about what's going to happen in Washington."

The Republican-controlled House has passed a measure that would deny funding for President Barack Obama's health-care law as part of a bill to pay for government operations after the Sept. 30 end of the fiscal year. The Democratic-controlled Senate will vote today on a stopgap spending bill, which party leaders said will exclude the Republican language ending funds for the law.

Clinton-Gingrich

A shutdown wouldn't be unprecedented: 17 funding gaps happened between 1977 and 1996, based on a Congressional Research Service analysis. In 1995 and 1996, interruptions lasted from Nov. 14 to Nov. 19 and from Dec. 16 to Jan. 6, as Republicans led by then-House speaker Newt Gingrich clashed with President Bill Clinton's administration.

Those back-to-back shutdowns cut GDP by 0.25 percentage point in the fourth quarter of 1995, almost entirely because federal employees were furloughed, according to an analysis by Joel Prakken, senior managing director at Macroeconomic Advisers.

Prakken, in his estimate of the impact on GDP this time, assumes that 36 percent of the federal government's 2.1 million civilian employees would be furloughed. Non-essential employees may include park rangers and most workers at the Internal Revenue Service. Zandi, on the other hand, assumes that about half of government employees would be furloughed.

Back Pay

Spending by government workers is unlikely to be affected because they will expect to receive back pay after returning to work, according to Macroeconomic Advisers.

A shutdown of just a few days would have little impact on the economy, analysts say. On the other hand, a closure of more than two months would "likely precipitate another recession," Zandi said Sept. 24 in testimony to the Senate Budget Committee. Even a three- or four-week gap would "do significant economic damage."

Haggling over a continuing resolution to fund the government past the end of the month comes as House Republican leaders prepare for what Speaker John Boehner last month called a "whale of a fight" over the nation's $16.7 trillion debt limit.

The leaders are banking on winning public support for a strategy of pairing their goals of spending cuts, looser environmental regulations and an Obamacare delay with the increase in the debt cap, rather than using the possibility of a government shutdown as leverage to win their objectives.

Quick Agreement

A quick agreement on a continuing resolution might bode well for talks on raising the debt ceiling, said Millan Mulraine, director of U.S. rates research at TD Securities USA LLC in New York.

“The initial cue for markets will come from how easily we are able to resolve the discussion on the government shutdown,” Mulraine said. Treasury Secretary Jacob J. Lew said this week the government probably would exhaust extraordinary measures it has been using to keep under the debt ceiling no later than Oct. 17 and will have about $30 billion cash on hand. That’s down from a projection of $50 billion last month.

The U.S. was stripped of its AAA credit ranking by Standard & Poor’s in August 2011, a move that partly reflected an impasse in Congress over raising the debt ceiling as well as the government’s lack of a plan to rein in its debt load.

While the downgrade didn’t result in investors charging the U.S. more to borrow, as 10-year Treasury yields slipped to record lows in July 2012, the move contributed to a global stock-market rout that erased about $6 trillion in value from July 26 to Aug. 12, 2011.

“A shutdown of non-essential services is inconvenient for a while. If we hit the debt ceiling, we’re in unchartered territory,” Prakken said. “If you miss an interest payment on the national debt, that’s a sovereign default of sorts, and I think it would shake the foundations of the global financial system.”

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