

FINANCIAL MARKETS

US GOVERNMENT
SHUTDOWN:
WILL IT AFFECT THE
US ECONOMY?



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ANOTHER POLITICAL IMPASSE

FOREWORD

At the time of writing, we're now 34 days into the partial US government shutdown, which makes it the longest in history.

Recent shutdowns have been a consequence of political jostling between Congress and the White House. Despite that jostling, a compromise was always found.

But this shutdown feels a little different. With a Democrat-led House vehemently opposed to President Trump's request for border wall funding, the markets are now pondering the economic impact of a prolonged shutdown.

Patrick Latchford
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SHUTDOWNS: WHAT YOU NEED TO KNOW

WHAT IS A GOVERNMENT SHUTDOWN?

US government shutdowns occur when the federal government essentially runs out of money to fund its operations and services.

The thought of the US government running out of funds might seem farcical - but in the age of partisan politics, shutdowns are commonplace.

So why do shutdowns happen? Well, it isn't because the funds aren't available to the federal government.

It's actually because Congress, or the sitting President, hasn't approved a bill which stipulates how funds should be spent. These are known as "appropriation bills". Sometimes, something called "continuing resolutions" are passed to keep the government open on a short-term basis.

Without an "appropriations bill" or "continuing resolution", the US

federal government is required to close non-essential operations and services. It's why shutdowns are sometimes called "partial government shutdowns".

But for some Americans, the impact of a shutdown is very real. Firstly, many US government employees that work for non-essential services are furloughed. This means they cannot return to work, or receive pay until the government re-opens. Meanwhile, government employees that work for essential services are required to work without pay until the government re-opens.

WHY DO SHUTDOWNS HAPPEN?

With almost 800,000 US government workers receiving no pay, many ask why shutdowns happen at all.

The answer is simple: partisan politics. Shutdowns usually happen when the two main political parties, the Democrats and Republicans, each have control in two branches government (the legislative and executives branches).

The pattern has become predictable in recent years. During President Obama's administration, the Republican-controlled House of Representatives opposed plans for the Affordable Care Act (ACA), leading to a budget deadlock with the Democrat-controlled Senate and President Obama.

Fast-forward to 2019 and the roles have reversed. President Trump and the Republican-controlled Senate are now at an impasse with the Democrat-controlled House of Representatives. The standoff centres on funding to construct a wall on the border

between the US and Mexico.

HOW LONG WILL THE 2019 SHUTDOWN LAST?

In recent years, shutdowns have been resolved by both sides being willing to compromise. However, with regards to the current shutdown, a compromise between President Trump and Democrats (at this moment in time) doesn't look likely.

The nature of the dispute is relatively simple. After rejecting an appropriations bill that had been passed by the House and Senate, President Trump has requested additional funds totalling \$5.7 billion to construct a wall on the southern border between the US and Mexico. The Democrats have so far refused.

Remember - building a border wall to curb illegal immigration was central to then-candidate Trump's election campaign. During the election campaign, the Republican nominee also claimed that he would get Mexico to pay for the construction of the wall.

Clearly, Mexico is not directly funding the border wall. But the Trump administration claims Mexico will pay for construction through the new USMCA trade deal it has negotiated.

While some private US companies could benefit from this trade deal, many economists dispute the claim that the profits from those companies will fund construction through taxation. It's one reason why Democrats oppose the request for additional funding.

The other reason is based in practicality. Many Democrats believe a border wall is an ineffective means of securing the southern

border. Instead, they favour investing in new technology - such as drones.

Provision for enhanced security was included in the initial appropriations bill both the House and Senate passed in December 2018 - but the effectiveness of these proposals compared to a wall has been questioned by some border patrol agents.

Progress has become more difficult since the turn of the New Year. After winning a majority of House seats in the midterm elections, the Democrats and their newly elected Speaker, Nancy Pelosi, took control of the chamber.

Throughout December there have been multiple bills proposed to reopen the government, albeit without funding for the border wall. But these bills have been declined by the Republican Senate and President Trump.

We're now 34 days (at the time of writing) into a government shutdown - and seemingly, no breakthrough is in sight.

However, President Trump may have another option to secure funding for a border wall. In public remarks, the president has said he would consider declaring a national emergency at the southern border, which the administration believes would give him authority to spend approximately \$7 billion on a border wall.

Such a move would likely prompt a legal challenge.

WILL THE SHUTDOWN AFFECT THE US ECONOMY?

An extended shutdown certainly has the potential to drag on US economic growth. The Bureau of Economic Analysis estimates that 2013's shutdown - which lasted 17 days - saw GDP growth fall by 0.3%.

Some analysts believe the current shutdown could see US GDP fall to approximately 1.2% for the first quarter of 2019.

Predicting the exact impact is difficult - but with nine federal agencies closed and 800,000 federal government employees receiving no pay, both tourism and levels of consumer spending are likely to be affected.

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