WASATCH
CAPITAL MANAGEMENT OF
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Tempest in a Teapot -Article by Mark Lazar

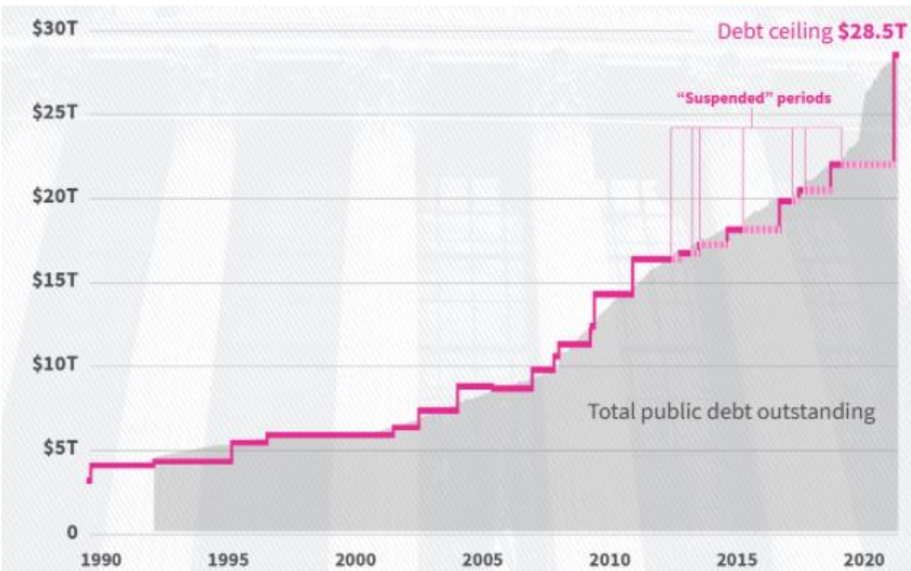
***I wish it were possible to obtain a single amendment to our Constitution—I mean an additional article, taking from the federal government the power of borrowing*. Thomas Jefferson**

September was a busy month. Oil prices jumped 9%, domestic stocks dipped 5%, the US economy expanded at 6.7%, home prices rose 20% YoY, a Chinese real estate company with $300B in debt teetered on the verge of default spooking the credit markets, and Senator Manchin derailed the $3.5 trillion spending bill. Much of the prior month's price volatility, however, could be attributed to the Fed signaling its intention to reduce bond purchases (quantitative easing) as early as November if the economy continues on its current track. Predictably, there was a corresponding selloff in Treasury securities, resulting in the 10-year note jumping from 1.30% to 1.52%, or a 17% increase. The jump in interest rates strengthened the US dollar ~2%, but compressed stock, bond, and commodity prices.

Item	YTD Change
Dow Jones Ind Avg	10.58%
S&P 500 Index	14.68%
EAFE Foreign Index	6.23%
Barclays Agg Bond Index	-2.13%
10-Year Inflation Forecast	2.38%
2021 GDP Growth Forecast	6.7%
Unemployment Rate	5.2%

**Market index data as of 9/30/2021*

The debt ceiling is once again in the spotlight. In a nutshell, the debt ceiling imposes a cap on how much debt the federal government can possess at any given time. The amount is set by law and once reached, the Treasury Department must halt issuance of debt securities and, instead, limit spending to the amount of tax revenues collected. The current cap is $28.5T, and the chart below illustrates three decades of history.



Source: US Treasury

Not surprisingly, the debt ceiling is a political football that allows out-of-power parties to attack the folks holding the reigns as being fiscally irresponsible. In 2006 junior senator Barrack Obama made the following impassioned speech in response to the Republican's request to raise the debt ceiling: "Increasing America's debt weakens us domestically and internationally. Leadership means that 'the buck stops here.' Instead, Washington is shifting the burden of bad choices today onto the backs of our children and grandchildren. America has a debt problem and a failure of leadership. Americans deserve better. I therefore intend to oppose the effort to increase America's debt limit."

But where did the debt ceiling come from and what purpose does it serve? In 1917 the Second Liberty Bond Act created a debt ceiling which empowered Congress to control the federal purse. Furthermore, a limit on federal debt imposes a form a fiscal accountability that compels both Congress and the President to take visible action in order to increase the federal government's ability to borrow/spend more.

What options do policymakers currently have? There are five possible scenarios:

1. Reduce federal spending
2. Increase tax revenues

3. Halt payments of interest and/or principle on government bonds. In other words, default
4. Undertake extraordinary measures; in other words, cash management techniques that delay a technical default for weeks and perhaps even several months, but not indefinitely
5. Raise the debt ceiling

Since 1976 there have been 21 government shutdowns, ranging between 1–34 days, during which government agencies were required to furlough non-essential personnel and stop or limit their activities. And each time the presiding party along with the media issued grave warnings that if the budget wasn't passed Uncle Sam would default, Social Security checks would be halted, interest rates would skyrocket, and the markets would collapse. None of which happened, of course, but both campaign contributions and viewership increased dramatically.

Debt negotiations are always a game of brinksmanship. But at the end of the day, neither party has the political will to die on the hill, which is why shutdowns are generally averted or resolved within a handful of days. Washington bureaucrats and the media know that fear sells, so they both paint an apocalyptic picture of what would happen if non-essential government agency personal are either furloughed, or temporarily work without pay until an agreement is reached.

This isn't to say we shouldn't have an honest, objective, civil discussion about the role of government, what it should and shouldn't do, and how it ought to pay the bills; we should. But government shutdowns have historically been a blip in terms of the markets and the economy. Debt showdowns may make good political fodder, but if history is any indicator, the sky isn't falling, and government shutdowns have been more akin to a tempest in a teapot.

Mark Lazar, MBA
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Wasatch Team Updates

Mark

Mark & Savina golfing in Hayden

Stan

Stan with his family on a fall hike this month

Rees

Rees & Lisa enjoying fall leaves in the Uinta Mountains

John

John and 4 friends on a biking/camping trip in Canyonlands!

Kendall

Kendall and Bracken in Costa Maya

Nicola

Nicola out to breakfast with her grand babies!

Matt

Matt and Sam with friends in Montauk, NY.

Jon

Jon and his family at his birthday dinner this month

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