

---

# U.S. TREASURIES: CAUTION, LOW CEILINGS

**Kevin Flanagan — Head of Fixed Income Strategy**  
**07/26/2017**

With most of the focus in Washington, D.C., being centered on the repeal and replacement of the Affordable Care Act, a topic that had garnered a great deal of attention in the past seems to be flying under the radar: the debt ceiling. This disparity in media coverage will more than likely continue, but in the weeks ahead, the debt ceiling debate definitely will be heating up.

## What Is It?

The debt ceiling, also known as the debt limit, is the total amount of money the U.S. government is allowed to borrow to meet its legal obligations. According to the Treasury Department, since 1960, Congress has acted 78 times to permanently raise, temporarily extend or revise the definition of the debt limit. For the record, adjustments have been made 49 times and 29 times under Republican and Democratic presidents, respectively.

## Recent Episodes

Two of the more noteworthy episodes in the recurring debt ceiling saga occurred relatively recently. The first, and perhaps the most infamous, occurred in 2011. As you may recall, politics was in full play as President Obama and the House Republicans each vied to hold sway, but unfortunately, a budget impasse ensued, with raising the debt ceiling being held hostage in the process. Ultimately, the two aisles came together and produced the Budget Control Act (BCA) of 2011, which not only dealt with budgetary issues but also ended up increasing the debt limit in three steps by a total of \$2.1 trillion, to \$16.4 trillion.

However, the BCA was too little, too late, as Standard & Poor's still decided to downgrade the U.S. credit rating a notch to [AA+](#) on August 5, 2011, only days after the legislation was signed into law. The move reflected S&P's opinion that the BCA "falls short of what...would be necessary to stabilize the government's medium-term debt dynamics." In addition, the S&P also cited "political brinksmanship" making "America's governance and policymaking becoming less stable, less effective and less predictable."

The BCA increase in the debt ceiling lasted until the fall of 2013, creating the second newsworthy episode. This time around, the debt ceiling debate was coupled with the October 2013 government shutdown, which lasted approximately 16 days. It is important to note that while linked, these two events are not the same thing and often get confused. That being said, a resolution was once again found, as the debt limit was suspended until February 2014 and laid the groundwork for our present-day scenario.

## Fast Forward to Now

After a variety of suspensions and resets, the current debt ceiling of \$19.8 trillion was put in place on March 15 this year. Since then, "extraordinary measures" have been used to create room for Treasury borrowing to continue to occur. This approach has been utilized many times in the past, but at some point, these measures become exhausted, and action

needs to take place. Without Congressional action, this is the position in which Treasury soon will find itself. Consensus analysis tends to place the drop-dead date in early October, but there is a risk it could be pushed up to early September, depending upon budget cash flows.

### What if the Unthinkable Happens?

Interestingly, during the 2011 episode, the [Treasury](#) and the [Federal Reserve \(Fed\)](#) produced a plan of sorts in case the debt ceiling was not raised in time. With respect to the financial markets, the most important part of this plan stated that principal and interest on Treasuries would be made on time. For maturing principal, Treasury would have “auctions that would roll over those maturing securities into new issues” and for timely interest payments, it would be “holding back other government payments” and use accumulated “sufficient cash balances in its Fed account.” Needless to say, prioritization is a politically charged concept, as it means the risk of payment delays and/or partial payments for other government obligations.

This topic can't fit into just one blog post, so I'll follow up with another debt ceiling-related post soon. Stay tuned...

***Unless otherwise noted, data source is the Federal Reserve, as of July 20, 2017.***

#### Important Risks Related to this Article

Fixed income investments are subject to interest rate risk; their value will normally decline as interest rates rise. In addition, when interest rates fall, income may decline. Fixed income investments are also subject to credit risk, the risk that the issuer of a bond will fail to pay interest and principal in a timely manner or that negative perceptions of the issuer's ability to make such payments will cause the price of that bond to decline.

For standardized performance and the most recent month-end performance click [here](#) NOTE, this material is intended for electronic use only. Individuals who intend to print and physically deliver to an investor must print the monthly performance report to accompany this blog.

For more investing insights, check out our [Economic & Market Outlook](#)

View the online version of this article [here](#).

## **IMPORTANT INFORMATION**

**U.S. investors only: Click [here](#) to obtain a WisdomTree ETF prospectus which contains investment objectives, risks, charges, expenses, and other information; read and consider carefully before investing.**

There are risks involved with investing, including possible loss of principal. Foreign investing involves currency, political and economic risk. Funds focusing on a single country, sector and/or funds that emphasize investments in smaller companies may experience greater price volatility. Investments in emerging markets, currency, fixed income and alternative investments include additional risks. Please see prospectus for discussion of risks.

Past performance is not indicative of future results. This material contains the opinions of the author, which are subject to change, and should not to be considered or interpreted as a recommendation to participate in any particular trading strategy, or deemed to be an offer or sale of any investment product and it should not be relied on as such. There is no guarantee that any strategies discussed will work under all market conditions. This material represents an assessment of the market environment at a specific time and is not intended to be a forecast of future events or a guarantee of future results. This material should not be relied upon as research or investment advice regarding any security in particular. The user of this information assumes the entire risk of any use made of the information provided herein. Neither WisdomTree nor its affiliates, nor Foreside Fund Services, LLC, or its affiliates provide tax or legal advice. Investors seeking tax or legal advice should consult their tax or legal advisor. Unless expressly stated otherwise the opinions, interpretations or findings expressed herein do not necessarily represent the views of WisdomTree or any of its affiliates.

The MSCI information may only be used for your internal use, may not be reproduced or re-disseminated in any form and may not be used as a basis for or component of any financial instruments or products or indexes. None of the MSCI information is intended to constitute investment advice or a recommendation to make (or refrain from making) any kind of investment decision and may not be relied on as such. Historical data and analysis should not be taken as an indication or guarantee of any future performance analysis, forecast or prediction. The MSCI information is provided on an "as is" basis and the user of this information assumes the entire risk of any use made of this information. MSCI, each of its affiliates and each entity involved in compiling, computing or creating any MSCI information (collectively, the "MSCI Parties") expressly disclaims all warranties. With respect to this information, in no event shall any MSCI Party have any liability for any direct, indirect, special, incidental, punitive, consequential (including loss profits) or any other damages ([www.msci.com](http://www.msci.com))

Jonathan Steinberg, Jeremy Schwartz, Rick Harper, Christopher Gannatti, Bradley Krom, Tripp Zimmerman, Michael Barrer, Anita Rausch, Kevin Flanagan, Brendan Loftus, Joseph Tenaglia, Jeff Weniger, Matt Wagner, Alejandro Saltiel, Ryan Krystopowicz, Kara Marciscano, Jianing Wu, Brian Manby and Scott Welch are registered representatives of Foreside Fund Services, LLC.

WisdomTree Funds are distributed by Foreside Fund Services, LLC, in the U.S. only.

You cannot invest directly in an index.

## **DEFINITIONS**

**Treasury** : Debt obligation issued by the U.S. government with payments of principal and interest backed by the full faith and credit of the U.S. government.

**Federal Reserve** : The Federal Reserve System is the central banking system of the United States.