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Fitch: Effects of US Fed Govt Shutdown Would Be Limited for Public Finance

Fitch Ratings-New York-29 September 2021: A US federal government shutdown as a result of the failure to pass legislation to extend government funding would unlikely affect most US public finance credits in the near term, Fitch Ratings says. However, a prolonged shutdown without a clear path or timeline for resolution could lead to disruption in federal payments to public and private entities and limited economic effects in areas with larger concentrations of federal employment. Moreover, political deadlock complicates policymaking, which may have longer-term implications for entities relying on federal funding. Government funding expires at midnight on October 1.

It is unclear what agencies and services would be affected in a shutdown, as President Joseph Biden has discretion about what would be considered essential functions of the government and would, therefore, continue through any shutdown. This shutdown may have more extensive reach than prior ones, as Congress has not yet passed any funding bills that would maintain ongoing operations for certain agencies.

Payments to states and local governments under the American Rescue Plan Act should not be affected, as remaining allocations are not due until 2022. Medicaid, which is the largest federal government transfer to states, and Medicare are expected to continue as both are considered mandatory spending programs. It is unclear if the funding and operations of public health agencies, such as the Centers for Disease Control and Prevention and US Food and Drug Administration, would be disrupted.

Most federal employees, including Defense and the US Postal Service, which together make up almost half of the total of employees, would not see changes to their employment or pay status. Other employees could be furloughed or required to work without pay. Localities with the highest proportion of federal employment are unlikely to see long-lasting effects on economically-sensitive tax revenues as the Government Employment Fair Treatment Act (GEFTA) of 2019 ensures payment of federal salaries deferred during a shutdown. The District of Columbia's operations are protected by the fiscal 2021 D.C. Appropriations bill, which excepts the district government from a shutdown in fiscal 2022.

Universities and non-profit entities may experience temporary pressures if federal research grants are not processed and disbursed. A short-term shutdown would have little effect but those that rely most heavily on federal grants or contracts would suffer in a longer shutdown. Student financial aid will likely be unaffected, as most disbursements for fall have occurred already.

Federal Housing Administration (FHA) loan applications may be stalled for new single-family FHA mortgages and multifamily properties with FHA risk share loans. This will delay the addition of new mortgage assets to Housing Finance Agency (HFA) programs, which could potentially cause a turnaround in the aggregate increases in total assets that HFAs experienced over the last five fiscal years.

Infrastructure projects backed by federal dollars may be affected in a prolonged shutdown. Federal highway transportation funding to states and local governments through the Highway Trust Fund is authorized outside of the annual budget process through multi-year legislation. The current authorization expires on October 1 as well, with reauthorization included in the Infrastructure and Investment Act (HR 3684) scheduled for a final House vote on Thursday. The Senate already cleared HR 3684 and the President plans to sign it if passed by the House.

Extending federal government funding seems to have support across the aisle, which may ease passage of a bill this week. These discussions are related to, but separate from, the deadlock over the debt limit. The Senate recently voted against a measure that combined the two issues, with all Republicans voting against it. The debt limit could be suspended or raised by other means before the limit is reached, estimated to be mid-October.

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