The Daily Dish

A New Fed Chair Nominee

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The Washington Post reports this morning that the President has made his decision about a new chair for the Federal Reserve. “President Obama on Wednesday will nominate Federal Reserve Vice Chair Janet Yellen to lead the U.S. central bank, officials said, selecting a renowned economist focused on combating unemployment for one of the most powerful positions in the world. Yellen would become the first female chief of the nation’s central bank — or any major central bank.”

This major announcement comes at a time when the nation inches closer towards breaching the debt ceiling and the government continues to be shut down. The Wall Street Journal reports this morning on the ongoing negotiations and comments from the President and Speaker of the House. “The exchange left the stalemate no closer to resolution, with the parties dug in even on terms over which they would conduct negotiations. Many federal agencies have been partially closed since Oct. 1, and the Treasury predicts it will run out of cash to pay its bills if the debt ceiling isn't raised this month.” The situation remains fluid but tensions seem to be rising as the October 17th date continues to get closer.

Eakinomics: Guest Authored this Morning by AAF Fiscal Policy Director Gordon Gray

Since May of this year, the Treasury department has been employing what it calls “extraordinary measures” to avoid breaching the debt ceiling. Essentially accounting gimmicks, they allow the Treasury, for a finite period, to continue to fund the government past the date they run up against the debt limit. Treasury has said it will exhaust these tools on October 17th.

When implementing these authorities, the Treasury usually keeps the amount of debt subject to the limit just $25 million under the ceiling. Looking at past Treasury reports we can see that the Treasury kept the debt just below the limit for 78 days during the 2011 crisis. Longer still was the spell preceding the 1996 budget fight, which lasted 135 days and, until recently, was the longest in recent record.

While 135 days is a long time to hover so close to apparent default, the Treasury has since surpassed this streak. Since the debt limit was reinstated in May, the Treasury has continuously maintained the debt at $25 million below the limit, and on October 1st surpassed the 1996 record and began its 136th day of maintaining its small margin.

As risky as it sounds, the implications of utilizing extraordinary measures for this long is unclear. While the accounting tricks the Treasury undertakes sometimes create additional costs, the monetary consequences are relatively small. However, as long as the United States continues to run large external deficits and require continued financing of its existing debt portfolio, it remains subject to the scrutiny of capital markets. Continued reliance on "extraordinary measures" may well contribute to skepticism from market participants that will inevitably result if the United States fails to get its fiscal house in order. An even greater threat remains once "extraordinary measures" are exhausted and the U.S. risks potential default.