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Economics Group

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Capitol Hill Update: Funding Extended Until September 30

This week, Congress finalized an omnibus funding bill that divvies up the top line funding agreed to last month. Congress will need to enact at least one more funding bill before the mid-term election in November.

I Thought There Was Already a Budget Deal?

Last month, Congress agreed to a two-year deal that lifts the spending caps that were put in place by the Budget Control Act of 2011. The caps were lifted by $296 billion over the next two years and devoted about 55 percent of that increase to defense spending. The deal also suspended the debt ceiling until March 2019 and included an $89 billion supplemental funding bill for disaster relief.

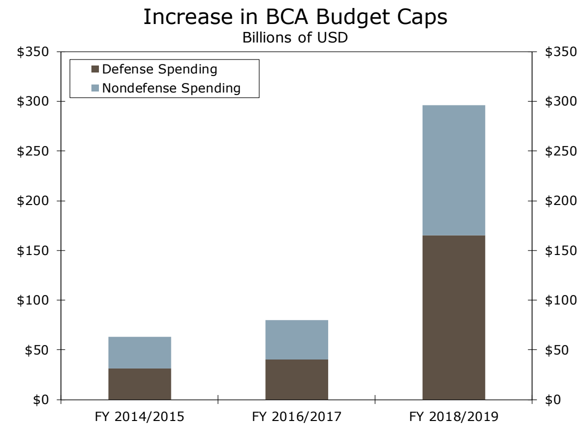
We wrote at the time that to avoid a government shutdown Congress would need to appropriate the new funding agreed to in the deal. This week, those appropriations were passed into law, which allows us to get a better sense of the macroeconomic impact of these fiscal policy changes. Federal discretionary outlays are expected to total $1.3 trillion for fiscal year 2018. Not all of the increase in spending will directly translate into real government spending. For example, some of the $89 billion in disaster spending will be recorded as a transfer across GDP accounts rather than having a direct impact on federal consumption and investment.

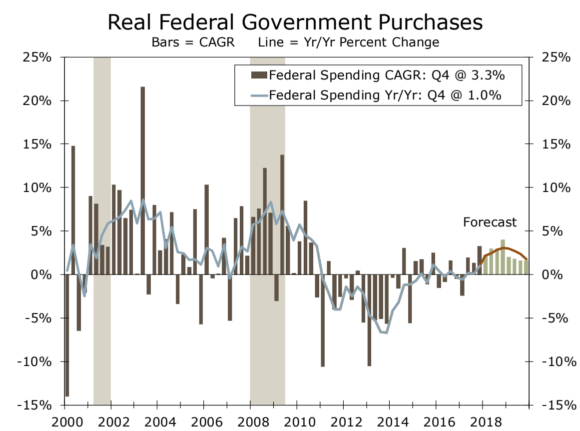
A Positive Short-Run Economic Impact

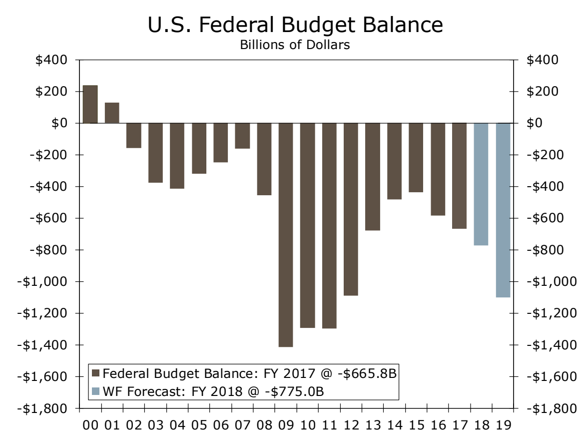
In terms of the economic impact, we are forecasting 2.6 percent year-over-year growth in real federal consumption and investment for 2018. For 2019, we are expecting 2.4 percent real government spending but admit that there is likely upside risk to this outlook. In total, the spending package would add 0.2 percentage points to headline GDP in 2018 under these assumptions and likely closer to 0.4 percentage points for 2019. These boosts to GDP growth are in addition to the tax package, which added 0.2 and 0.3 percentage points respectively to our 2018 and 2019 GDP growth forecasts. Our view remains that the rapid pace of fiscal expansion at this stage of the business cycle is likely to result in greater inflationary pressures this year and next year. We see the headline PCE Deflator reaching 2.1 percent by the end of this year with core inflation gradually moving toward 2.0 percent by Q4-2018.

Previewing the CBO's Budget Outlook

On April 9, the CBO is expected to publish its annual Budget and Economic Outlook. We anticipate that the CBO will increase its deficit forecasts as a result of the fiscal policy changes enacted over the past year. As of its last update in June 2017, the CBO projected a deficit of $563 billion in FY 2018 and $689 billion in FY 2019. We estimate that the deficit will top out at $775 billion this fiscal year and $1.1 trillion for FY 2019. We expect the quarterly deficit numbers and corresponding net Treasury issuance to ramp up toward the end of this calendar year, as there will be some delay before the new budget authority translates into actual outlays.







Source: Congressional Budget Office, U.S. Dept. of Commerce, U.S. Dept. of the Treasury and Wells Fargo Securities

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