MARKET SNAPSHOT

GLENMEDE
INVESTMENT MANAGEMENT

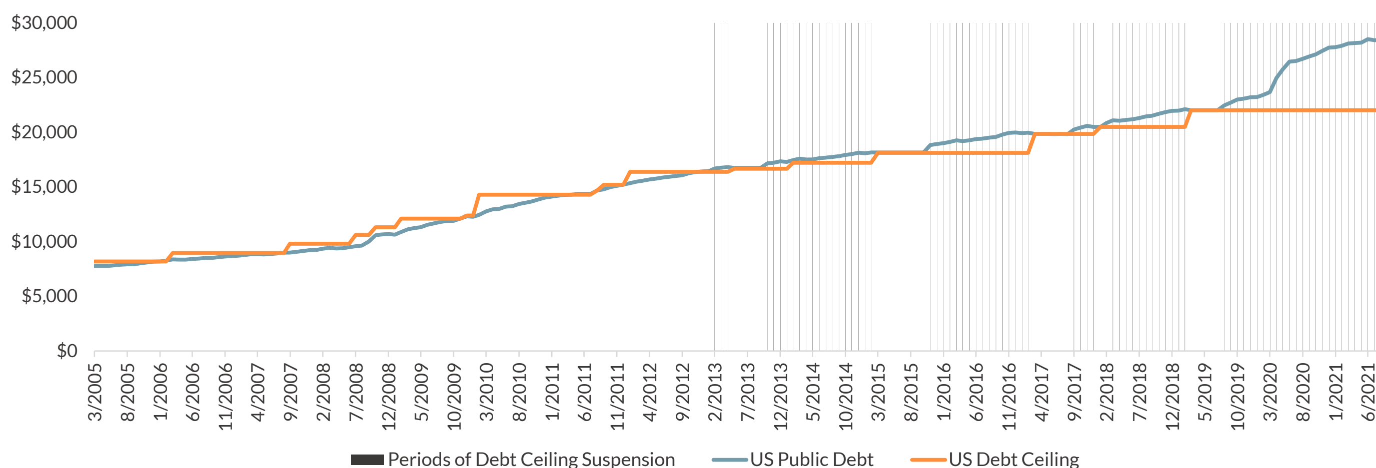
MARKET RISKS OF THE DEBT CEILING

- The U.S. Treasury has taken "extraordinary measures" to extend its borrowing authority since the statutory debt limit suspension implemented in 2019 ended July 31, 2021. Without Congress passing an increase to the debt ceiling or an extension of the suspension, Treasury Secretary Janet Yellen warns these maintenance tools will be exhausted by October 18 and the U.S. could default on its debt.

- History would suggest a default is unlikely because Congress has forestalled such events previously, as noted in the chart. However, these contentious debates are not without other risks, as experienced in 2011 when Standard & Poor's downgraded the U.S. credit rating for the first time in history from AAA to AA+, where it stands today. Additionally, an unprecedented risk to this debate is that the current U.S. public debt tally of $28.6 trillion is over 100% of GDP for the first time since World War II, according to the Congressional Budget Office. This compares to the average ratio of U.S. public debt/GDP over the past decade's debates of ~72%, making a flippant decision to raise the debt ceiling more difficult.

- Ahead of the more contentious debt ceiling debates in 2011 and 2013, short-term U.S. Treasury bill yields spiked higher and U.S. corporate credit spreads widened as the "ex-date" approached, suggesting we could experience similar risk adjustments over the coming weeks (Treasury bills moved about 10 bps, which is large for them, while corporates moved 10 bps the day after the limit was raised and 60 bps a month later due to the downgrade from S&P). While we believe the market implied probability of a catastrophic default on U.S. debt is low, options on the S&P 500 suggest a recognition of this risk, as well as other short-term concerns. According to Bloomberg, the ratio of volatility of the one-month 5% out-of-the-money protective puts relative to the 5% out-of-the-money upside participation calls is over 2, which is above the decade average of 1.6 and the levels seen in the 2011 and 2013 debates.

U.S. Debt



Sources: Bloomberg, Glenmede Investment Management
Past results are not indicative of future performance

Data as of 9/23/2021

The views expressed represent the opinions of certain GIM portfolio managers as of September 29, 2021 and are not intended as a recommendation of any security, sector or product, and any security identified herein may or may not have been bought, held and/or sold by GIM-managed portfolios. Any opinions or projections herein are based on information available at the time of publication and may change thereafter. Information obtained from third-party sources is assumed to be reliable, but accuracy is not guaranteed. Future developments (including performance) may differ materially from expectations and projections noted herein due to various risks and uncertainties and changes in underlying assumptions. For institutional and professional investors only; not for retail clients.