First Trust
Monday Morning OUTLOOK

Brian S. Wesbury – *Chief Economist*
Robert Stein, CFA – *Dep. Chief Economist*
Strider Elass – *Senior Economist*
Andrew Opdyke, CFA – *Senior Economist*
Bryce Gill – *Economist*
Nate Gerze – *Economic Analyst*

630-517-7756 • www.ftportfolios.com

March 4, 2024

Is a Debt Spiral Already Here?

Washington DC continues to spend much more than it gets in revenue. In the Calendar Year of 2023, the federal government spent $6.3 trillion, but only collected $4.5 trillion in taxes. This $1.8 trillion gap drove the national debt to $34 trillion in December 2023. And it is only going higher.

One problem with these budget numbers is that government accountants, rightly or wrongly, lowered spending in 2023 by about $300 billion after the Supreme Court struck down a large part of President Biden's proposal to forgive student loans. That legal decision didn't change the government's cash flow last year in any significant way, but it did let the Department of Education "write up" the value of its loan portfolio by about $300 billion. This, they counted as "negative spending," which then reduced the official budget deficit. So, while the reported deficit in 2023 was $1.8 trillion, the Treasury needed to borrow more than $2 trillion to make ends meet.

The high levels of borrowing are causing some investors to fear some sort of imminent and unprecedented snowballing of federal debt. Continual borrowing will lead to skyrocketing interest rates (and higher interest payments), which will lead to severe problems in the financial system.

In particular, they note that since June 2023, when the debt ceiling was suspended, total Treasury debt outstanding has gone up by nearly $3 trillion. That includes a total of $874 billion in the second quarter of 2023, $835 billion in the third quarter, and $834 billion in the fourth quarter. Other than 2020-21, during COVID lockdowns, the debt has never gone up this rapidly, not even in 2008-2009.

But it's important to remember that the debt does not go up at a steady rate during the course of the year. In 2023, during March and April, the federal government received a surge in tax receipts, which temporarily reduced the amount of debt outstanding. We think this will happen again this year, particularly because the S&P 500 went up 24% last year and the federal government is therefore likely to reap lots of non-withheld revenue.

As a result, the Congressional Budget Office estimates that individual income tax payments will be up 13.4% this year and the budget deficit will come in at roughly $1.5 trillion versus $1.7 trillion in Fiscal Year 2023. On that score, we are not as optimistic. Even as we write this, Congress is debating foreign aid measures that, whether you like the underlying policy or not, will, by themselves, boost the deficit.

And while the cost of servicing the debt is going up, the interest measure that matters is the net interest on the debt relative to GDP. In other words, what matters is how much of our national income is needed to service the debt. That measure, while climbing and a problem, is still below the average of roughly 3% of GDP it was back in the 1980s-90s.

However, because we think interest rates will remain higher than government accountants think, the carrying cost of our debt will move higher.

The bottom line is that federal government spending is way too high and most politicians do not seem to care. There are those who look at these numbers and assume some kind of imminent crisis, when what we see is a slow, but unavoidable decay in our underlying potential to grow. New technologies are raising productivity, but a huge government acts like a ball and chain on those benefits.

For now, the markets are ignoring this, and assume a soft landing with lower interest rates. But the more economic growth is undermined, the less likely this outcome.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
3-5 / 9:00 am	ISM Non Mfg Index – Feb	53.0	**53.3**		53.4
9:00 am	Factory Orders – Jan	-2.9%	**-2.8%**		+0.2%
3-7 / 7:30 am	Initial Claims – Mar 2	215K	**215K**		215K
7:30 am	Int'l Trade Balance – Jan	-$63.5 Bil	**-$63.9 Bil**		-$62.2 Bil
2:00 pm	Consumer Credit– Jan	$10.0 Bil	**$6.4 Bil**		$1.6 Bil
3-8 / 7:30 am	Non-Farm Payrolls – Feb	200K	**170K**		353K
7:30 am	Private Payrolls – Feb	163K	**140K**		317K
7:30 am	Manufacturing Payrolls – Feb	10K	**5K**		23K
7:30 am	Unemployment Rate – Feb	3.7%	**3.8%**		3.7%
7:30 am	Average Hourly Earnings – Feb	+0.2%	**+0.3%**		+0.6%
7:30 am	Average Weekly Hours – Feb	34.3	**34.2**		34.1

Consensus forecasts come from Bloomberg. This report was prepared by First Trust Advisors L. P., and reflects the current opinion of the authors. It is based upon sources and data believed to be accurate and reliable. Opinions and forward looking statements expressed are subject to change without notice. This information does not constitute a solicitation or an offer to buy or sell any security.