

RELEASE IN PART B6

From: sbwhoep [redacted]
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Subject: H: Richard Medley has sent this around in his private newsletter. Sid

B6

US Election And The Fed Welcome To The New (Old) World

September 19, 2010

One of the main debates inside senior Fed offices is how much they may have to balance a much more conservative fiscal policy if the Republicans take over. This is the most important question facing officials on both sides of the fence (far more than squiggles and whirls of monthly numbers).

But it's not just spending and taxes, important as they are, it's also implementation of Reg Reform and Health Care Reform. All of that is going to change after November. Here are the details.

Amid the snarkiness about how crazy the Tea Party candidates may be (and, as you know, we LOVE snarkiness) two things should not be lost:

1. The President has lost control of the spending and tax agenda
2. The President has lost control of implementing the Reg Reform and health care legislation Congress pushed through.

All polling from both parties and independent sources point strongly to the Republicans taking over the House. Although they are less likely to take over the Senate, they will be able to gain effective control of spending, taxes and large scale administrative reforms.

Let's start with spending:

The basic fact is that all spending has to be approved by Congress and it starts with the House. As we wrote nearly a week ago, House Republican Leader Boehner and his senior staff have made it clear to us that they would like to freeze spending at 2008 levels with an annual cost savings of \$340 billion. This will be one of the top Republican priorities.

Freezing spending at 2008 levels will not happen. However, even in the unlikely event the Republicans do not take over the House the budget will -- at most -- be frozen at or near FY 2010 levels (i.e. the last time money was formally appropriated).

Since there have been no spending bills approved and the fiscal year starts in October, the Congress has to pass a "continuing resolution" that keeps the government running until specific appropriations are made (the 1995 government shutdown happened because there were no appropriations and no continuing resolution...the government literally runs out of spending authority).

Congress will pass a CR in the next few weeks and it will most likely run through the formation of the new Congress (say February or March) next year. They could only do it through the lame duck session, but that would be cutting it close and too cute.

Because the new Congress -- even if the Republicans fail to take full control of the House -- will be dominated by fiscal conservatives, Boehner's CR idea will have traction. The Senate will make it more moderate, but then it will be up to the President to veto it and thus shut down government or sign it and take the hit.

In turn that does two things: (1) it frees up money for the Bush tax rollovers and (2) it helps the plan to slow or freeze implementation of the reg reform and health care reform bills.

The first part is obvious. The second may be less so. People forget that implementation of these rules requires staff increases, staff reg writing, etc and that's money. By freezing spending at previous levels you freeze the ability to hire new staff and you seriously obstruct the new rule writing process.

Add to that Boehner's commitment to overturn the two major regulatory reforms and you've got a tidal wave of indecision and paralysis (Jesus, talk about mixed metaphors although it would be interesting to see one of those).

The hearings he will announce and simply the chilling effect of him threatening to overturn the laws will accomplish ninety-percent of what he wants to get done, and potentially give the courts time to strike down parts of the health care bill now under appeal.

THE SENATE

While everyone has written off Republican control of the Senate (we haven't), the attention should be on what the Senate will look like even if the consensus of 52-54 Democratic majority prevails.

The point is how the US Senate will function in January 2011 given its new membership. We got a glimpse of what this would look like when moderate Republican Scott Brown was elected and the health care public option was panned and Reg Reform was trimmed around the edges.

The incoming crop of members are much more ardent on government spending, the debt, taxes and regulatory oversight. They will make Boehner's job much easier

Take a quick look at the new members (and the several they will marry up with once they are sworn into office).

While some of these candidates are replacing Republican open seats, all of them are generally considered more conservative than their predecessors:

1. ck (CO) – likely winner
2. Toomey (PA) – likely winner
3. Rubio (FL) – likely winner
4. Ayotte (NH) – likely winner
5. Blunt (MO) – likely winner
6. Portman (OH) – likely winner
7. Coats (IN) – likely winner
8. Paul (KY) – likely winner
9. Miller (AK) – likely winner
10. Lee (UT) – likely winner
11. Boozman (AR) – likely winner
12. Hoeven (ND) – likely winner
13. Kirk (IL) – 50/50 (lean GOP)
14. Angle (NV) – 50/50 tossup

There are several other Democrat-controlled seats that remain in play (CA, WI, WA, and CT). These races continue to develop and we will report more as the picture on Election Day becomes clearer.

These likely new members will join the following traditional budget trouble-makers in the US Senate:

1. DeMint (SC)
2. Coburn (OK)
3. Inhofe (OK)
4. McConnell (KY)
5. Kyl (AZ)
6. McCain (AZ)
7. Thune (SD)

8. Crapo (ID)

9. Vitter (LA)

10. Burr (NC)

One aggressive Senator can slow the body to a snail's pace, and Republicans operated efficiently as a minority party with only 41 votes total. In January, there will be at least 22 new and existing serious road blocks now patrolling the Senate Floor. The Republican pick-ups will make getting to 60 votes for cloture impossible on spending bills.

Welcome to the new reality.