GAO Highlights

Highlights of GAO-25-107089, a report to congressional committees.

Why GAO Did This Study

To meet the federal government's borrowing needs, Treasury issues debt in the form of bills, notes, and bonds. These securities play a vital role in U.S. and global financial markets. Congress imposes a legal limit on federal borrowing, known as the debt limit. In recent years, when outstanding debt has reached the limit, extended congressional negotiations have frequently brought the federal government close to being unable to continue paying its obligations. If Treasury exhausts its borrowing authority and runs out of cash to continue paying government obligations, a default will occur.

GAO prepared this report as part of its continuing efforts to assist Congress in addressing challenges related to the debt limit. This report examines (1) factors related to the debt limit that expose the U.S. to a potential default, (2) immediate consequences of a U.S. default for the U.S. financial system, and (3) longer-term consequences of a U.S. default for the economy. GAO reviewed academic literature and agency documents and interviewed agency officials, economists, and market participants from banks, money market funds, and rating agencies, among others.

What GAO Recommends

GAO previously outlined alternatives to the current debt limit process and recommends that Congress consider immediately replacing it with an approach that links debt decisions to spending and revenue decisions at the time they are made.

View GAO-25-107089. For more information, contact Michael E. Clements at (202) 512-8678 or clementsm@gao.gov.

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DEBT LIMIT

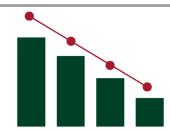
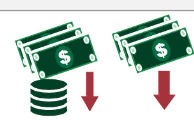
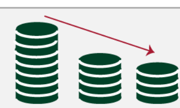
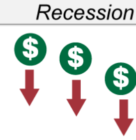
Statutory Changes Could Avert the Risk of a Government Default and Its Potentially Severe Consequences

What GAO Found

The current debt limit process separates decisions on revenue and spending from decisions on debt. As a result, the government periodically runs out of borrowing authority needed to pay existing, legally committed obligations. The Department of the Treasury has used extraordinary measures, which can temporarily free up existing borrowing authority, and cash on hand to continue making payments. However, these resources are limited and eventually run out. Predictions about when the government will no longer be able to pay all of its obligations—the "X-date"—are inherently imprecise due to the unpredictable size and timing of federal cash flows. Consequently, last-minute negotiations on the debt limit can increase the risk of a default. Further, these negotiations do not directly tackle structural spending and revenue levels that contribute to the growing debt.

A default would disrupt financial markets, with immediate, potentially severe consequences for businesses and households. A default could also inflict long-lasting damage to the U.S. and global economies (see figure).

Potential Effects of a U.S. Default on Financial Markets and the U.S. and Global Economies

Market disruption	 *Market crash*	Treasury securities would likely lose value or become unacceptable as collateral, leading to disruptions in critical short-term funding markets. This could cause a loss of liquidity in the financial system, increase risk of insolvency for financial institutions, and trigger potential runs on banks and money market funds.
Challenges protecting bank customers	 *Bank stress*	The Federal Deposit Insurance Corporation's deposit insurance funds are invested in Treasury securities. In the event of a bank failure, the agency may not be able to obtain these funds from the Department of the Treasury to protect bank customers in a timely manner under the constraint of a default.
Reduced credit	 *Credit reduction*	Default could trigger financial market distress, causing financial institutions to preserve their cash. This could lead to reduced lending to businesses and households, making it more difficult and expensive to obtain credit. For example, banks would likely pause new loans and reduce existing home equity lines and credit card limits.
Deep and lasting recession	 *Recession*	If default caused significant financial turmoil, it could trigger a severe and potentially long-lasting recession in the U.S. that potentially spreads to other countries. This could lead to lower business investment, notable job losses, and a decline in household wealth.
Global shift from the dollar	 *Dollar status diminished*	A default could reduce demand for Treasury securities and would contribute to a gradual shift away from the U.S. dollar. If the dollar became less dominant in international trade and financial transactions, U.S. businesses would become more exposed to exchange rate fluctuations, making operating costs less predictable.
Worsening fiscal path	 *Worsening U.S. fiscal path*	The negative effects of growing federal debt could intensify over time, as federal tax revenues would fall during a recession and investors may seek higher interest rates on Treasury securities in the longer term. Higher costs of borrowing for the U.S. would worsen its already unsustainable long-term fiscal path, posing serious economic, security, and social challenges.

Source: GAO (icons). | GAO-25-107089