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UPDATED BUDGET ESTIMATES

GROWING DEFICITS AND DEBT

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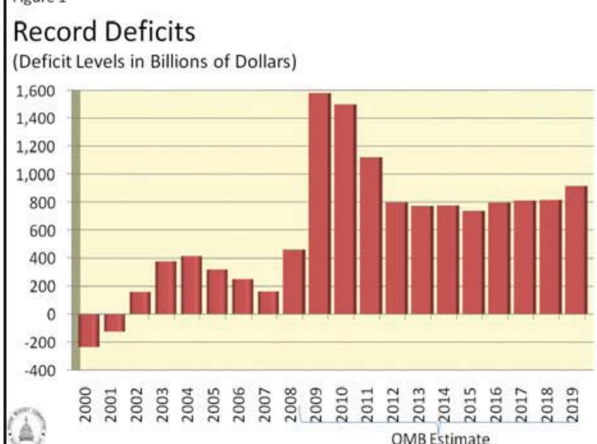
SUMMARY

The Office of Management and Budget [OMB] and the Congressional Budget Office [CBO] today released their updated budget and economic forecasts. The bottom line is as follows:

- **Ten-Year Deficits.** OMB shows a deficit $1.9 trillion higher over the next 10 years; CBO's deficit is $1.6 trillion higher. The largest factor in the deficit increase is the economy, with both OMB and CBO showing a weaker recovery in 2010. CBO shows the unemployment rate averaging 10.2 percent in 2010; OMB shows a 9.8-percent average. Note that because of baseline constraints, CBO extends and inflates enacted fiscal year 2009 war funding (including the supplemental) for the entire 10-year period, which causes its "official" deficit increase to be $2.7 trillion. If this is removed, CBO's deficit increase is $1.6 trillion over 10 years.

  The President's budget deficits are at unprecedented levels, and remain so throughout the decade (see Figure 1).

Figure 1



- **Deficit in 2009.** By both estimates, the fiscal year 2009 deficit will be $1.6 trillion (11.2 percent of gross domestic product [GDP]), more than three times the previous record. OMB's deficit has declined from $1.8 trillion largely due to withdrawing a $250-billion placeholder for additional Troubled Assets Relief Program [TARP] funds (further described below). CBO did not assume the TARP placeholder in its earlier baseline projection, so its deficit decline is smaller; CBO's deficit reduction results from a lower estimate of TARP outlays from the enacted program.

- **Debt.** Under the President's budget, debt held by the public more than doubles in 5 years (to $12.3 trillion) and more than triples in 10 years (to $17.5 trillion), compared to the 2008 levels of $5.8 trillion (see Figure 2).

The following discussion summarizes the projections by the two agencies.

- **Deficits.** Under the OMB estimates, projected deficits have swollen to $9 trillion over the next 10 years – an increase of $2 trillion, or nearly 30 percent, compared with the administration's estimate just 6 months ago. The deficit under the President's budget never falls below $739 billion, and reaches $917 billion in 2019.

- **Debt.** Relative to the 2008 level ($5.8 trillion), debt held by the public under the President's budget more than doubles in 5 years (to $12.3 trillion) and more than triples in 10 years (to $17.5 trillion) (see Figure 2). Relative to the economy, debt rises from 40.8 percent of GDP last year to 76.5 percent of GDP in 2019.

Figure 2

Doubling and Tripling the Debt

(in Billions of Dollars)

- **Spending.** The deficits and debt are driven by higher spending. The President and the Democratic Congress have launched an unprecedented increase in spending, including a $408-billion fiscal year 2009 omnibus appropriations bill with nearly 9,000 earmarks; a $787-billion "stimulus" bill; and a new $1-trillion health care entitlement. As a result, outlays never fall below 22 percent of GDP, and reach 23.2 percent of GDP in 2019.

Table 1: Administration Projections of Spending, Revenues, and Deficits, 2009-19

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2009-19
In Billions of Dollars												
Receipts	2,074	2,264	2,591	2,945	3,161	3,365	3,582	3,791	3,985	4,186	4,389	34,259
Outlays	3,653	3,766	3,715	3,741	3,936	4,143	4,321	4,586	4,795	5,001	5,307	43,309
Deficits	1,580	1,502	1,123	796	775	778	739	795	810	815	917	9,051
Debt Held by Public	7,856	9,575	10,590	11,443	12,281	13,126	13,927	14,782	15,651	16,523	17,493	n/a
As Percentages of Gross Domestic Product												
Receipts	14.7%	15.7%	17.1%	18.4%	18.6%	18.7%	18.8%	19.0%	19.0%	19.1%	19.2%	18.4%
Outlays	25.9%	26.1%	24.6%	23.3%	23.2%	23.0%	22.7%	22.9%	22.9%	22.8%	23.2%	23.5%
Deficits	11.2%	10.4%	7.4%	5.0%	4.6%	4.3%	3.9%	4.0%	3.9%	3.7%	4.0%	5.1%
Debt Held by Public	55.7%	66.3%	70.0%	71.4%	72.3%	72.9%	73.2%	74.0%	74.7%	75.5%	76.5%	n/a

Source: Office of Management and Budget, *Mid-Session Review*.

- **The Illusion of Fiscal Year 2009 Deficit Reduction.** As noted, the administration claims the 2009 deficit has declined by $261 billion. But there are two things to note about this. First, the resulting deficit is still $1.6 trillion, more than three times the record and, at 11.2 percent of GDP, the highest deficit as a share of the economy since World War II. Second, this "reduction" is achieved by removing a $250-billion "placeholder" that was included in the February budget. The

Treasury never requested this funding, and it almost certainly would not have been passed by the Congress. If the $250-billion placeholder is set aside, the *Mid-Session Review* shows the TARP has increased in cost by $60 billion (see Table S-8 in the administration's *Mid-Session Review* document).

The remaining deficit "reduction" comes from a lower estimate of deposit insurance outlays. But the Federal Deposit Insurance Corporation is under tremendous strain: just last Friday, the Guaranty Bank failed at a cost of about $3 billion (it was the third largest bank failure this year and brought the number of bank failures in 2009 to 81).

CONGRESSIONAL BUDGET OFFICE

- **Deficits.** CBO estimates a 2009 deficit of $1.6 trillion, roughly $400 billion more than estimated in January. At 11.2 percent of GDP, it is the largest deficit as a share of the economy since World War II. CBO says the deficit results from a combination of weak revenues and higher spending due to the economic downturn and financial turmoil; and it has been boosted by various spending policies, including economic "stimulus" legislation.

  Over the next 10 years, CBO estimates a deficit increase of $2.7 trillion. But as noted previously, because of baseline constraints, CBO extends and inflates enacted fiscal year 2009 war funding (including the supplemental) for the entire 10-year period. If this is removed, CBO's deficit increase is $1.6 trillion over 10 years.

Table 2: Congressional Budget Office Projections of Spending, Revenues, and Deficits, 2009-19

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2009-19
In Billions of Dollars												
Receipts	2,100	2,264	2,717	3,010	3,221	3,403	3,577	3,737	3,908	4,081	4,260	34,177
Outlays	3,688	3,644	3,638	3,600	3,759	4,961	4,135	4,358	4,534	4,703	4,982	41,314
Deficits	1,587	1,381	921	590	538	558	558	620	626	622	722	7,137
Debt Held by Public	7,612	8,868	9,782	10,382	10,870	11,439	11,986	12,581	13,174	13,611	14,324	n/a
As Percentages of Gross Domestic Product												
Receipts	14.9%	15.7%	18.1%	19.1%	19.4%	19.6%	19.9%	19.9%	20.0%	20.1%	20.2%	19.3%
Outlays	26.1%	25.2%	24.3%	22.8%	22.6%	22.9%	22.9%	23.2%	23.2%	23.2%	23.6%	23.4%
Deficits	11.2%	9.6%	6.1%	3.7%	3.2%	3.2%	3.1%	3.3%	3.2%	3.1%	3.4%	4.0%
Debt Held by Public	53.8%	61.4%	65.2%	65.9%	65.5%	66.0%	66.5%	67.1%	67.5%	67.0%	67.8%	n/a

Source: Congressional Budget Office, *The Budget and Economic Outlook: An Update*, August 2009.

- **Debt.** Debt held by the public rises from 40.8 percent of GDP in 2008 to 67.8 percent in 2019. Again, these figures are lower than those of the administration's mainly because CBO assumes higher revenues.

COMPARISON OF ECONOMIC ASSUMPTIONS

A direct comparison of the economic assumptions of OMB, CBO, and the Blue Chip consensus of private forecasters is reflected in Table 3 below. Some key points are the following:

- **Economic Growth.** Both OMB and CBO are predicting relatively sluggish economic growth next year following this year's sharp contraction. CBO expects real GDP growth of just 1.7 percent in 2010, while the administration sees 2.0-percent growth. The latest private-sector consensus from the Blue Chip calls for a 2.3-percent increase next year.

Table 3: Comparison of Economic Assumptions

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Real GDP (year/year)												
MSR	1.1	-2.8	2.0	3.8	4.3	4.3	4.1	3.6	3.2	2.8	2.6	2.5
February Budget	1.3	-1.2	3.2	4.0	4.6	4.2	2.9	2.6	2.6	2.6	2.6	2.6
CBO	1.1	-2.5	1.7	3.5	5.0	4.5	3.0	2.7	2.5	2.3	2.2	2.2
Blue Chip	1.1	-2.6	2.3	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Consumer Price Index												
MSR	3.8	-0.7	1.4	1.5	1.9	2.0	2.0	2.0	2.1	2.1	2.1	2.1
February Budget	3.8	-0.6	1.6	1.8	2.0	2.1	2.1	2.1	2.1	2.1	2.1	2.1
CBO	3.8	-0.5	1.7	1.3	1.0	1.1	1.5	1.8	2.0	2.0	2.0	2.0
Blue Chip	3.8	-0.5	1.9	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Unemployment Rate												
MSR	5.8	9.3	9.8	8.6	7.7	6.8	5.9	5.6	5.5	5.3	5.3	5.2
February Budget	5.8	8.1	7.9	7.1	6.0	5.2	5.0	5.0	5.0	5.0	5.0	5.0
CBO	5.8	9.3	10.2	9.1	7.2	5.6	4.9	4.8	4.8	4.8	4.8	4.8
Blue Chip	5.8	9.3	9.9	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
91-Day Treasury Bills												
MSR	1.4	0.2	1.3	2.6	3.8	4.0	4.0	4.0	4.0	4.0	4.0	4.0
February Budget	1.4	0.2	1.6	3.4	3.9	4.0	4.0	4.0	4.0	4.0	4.0	4.0
CBO	1.4	0.2	0.6	1.7	3.1	4.1	4.5	4.6	4.7	4.8	4.8	4.8
Blue Chip	1.4	0.2	0.7	NA	NA	NA	NA	NA	NA	NA	NA	NA
10-Year Treasury Notes												
MSR	3.7	3.6	4.5	4.9	5.2	5.2	5.2	5.2	5.2	5.2	5.2	5.2
February Budget	3.7	2.8	4.0	4.8	5.1	5.2	5.2	5.2	5.2	5.2	5.2	5.2
CBO	3.7	3.3	4.1	4.4	4.7	5.0	5.3	5.4	5.5	5.6	5.7	5.7
Blue Chip	3.7	3.4	4.1	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a

Source: Office of Management and Budget, *Mid-Session Review*, and Congressional Budget Office. Note: Blue Chip figures are from the August forecast.

- **Unemployment.** The unemployment rate is expected to linger at high levels over the next few years, even after real GDP growth has returned to a more healthy clip. CBO predicts the unemployment rate will peak at just under 10.5 percent in 2010 (averaging 10.2 percent for the year) and will remain above 9.0 percent in 2011. This is a notable increase from CBO's earlier forecast in March, when the agency was expecting the unemployment rate to fall to 7.7 percent in 2011. OMB sees unemployment peaking above 10 percent, with the average at 9.8 percent in 2010, then declining to 8.6 percent in 2011. This represents a change from the administration's earlier economic forecast, when it argued that the economic "stimulus" package would hold the unemployment rate below 8.0 percent in 2010.

- **Inflation.** CBO is expecting very low rates of inflation well into the next decade. It expects the consumer price index [CPI] to rise by just 1.3 percent in 2011, and by only 1.1 percent in 2012 and 2013. The administration expects slightly higher increases in the CPI over the medium term. CBO's prediction on the inflation front is consistent with a "Phillips Curve" relationship between the unemployment rate and inflation – i.e. the excessive slack in labor markets generated by the sharp recession and a lingering high unemployment rate will tend to hold down the rate of inflation well into the future. But it is important to note that other factors besides the so-called "output gap" could lead to higher-than-predicted rates of inflation over the medium term. With the Federal Reserve's extraordinary actions to pump up liquidity, along with huge budget deficits and a reliance on borrowing from foreign countries, the likelihood is toward higher inflation in the future.

- **Interest Rates.** Both the CBO and OMB have increased the expected rate on the 10-year Treasury note over the next few years relative to their earlier forecasts. Longer-term interest rates have increased from their historic low levels earlier this year. In addition, Treasury is expected to shift more of their borrowing to the longer end of the yield curve (i.e. 3-year, 7-year, and 10-year notes), which is expected to put upward pressure on these longer-term rates. It is worth pointing out that CBO's estimate of debt service costs, which are partly linked to interest rates on Treasury notes, have increased by $300 billion over 10 years from its March forecast.

Additional graphics relevant to this discussion can be found at:
http://www.house.gov/budget_republicans/graphs/20090825msr.pdf