



REPUBLICAN CAUCUS

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## HOPE FOR THE BEST, PREPARE FOR THE WORST AN ECONOMIC ‘STRESS TEST’ OF THE ADMINISTRATION’S BUDGET

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### SUMMARY

In the 10-year path of the President’s budget, the deficit never falls below \$500 billion, and it rises to \$712 billion by 2019. But even those disturbing figures, reflecting record high deficits, rely on economic assumptions that are significantly more optimistic than those of private forecasters. In fact, assuming the Blue Chip consensus economic forecast, and applying administration methodology, budget deficits would be more than \$750 billion higher than the administration projects over the next 5 years. Assuming a more adverse economic scenario – the same that is being used by federal regulators to “stress test” the nation’s banks – budget deficits would be nearly \$1.2 trillion higher than the administration projects over the 5-year window.

The discussion below explains these findings.

### COMPARISON OF ECONOMIC PROJECTIONS

The administration’s budget relies on economic assumptions that are significantly more optimistic than the private-sector consensus forecast. These assumptions are crucial because future economic performance will be one of the key factors that will shape the trajectory of the Federal budget deficit in the coming years. Slower-than-predicted gross domestic product [GDP], for instance, would lead to lower receipts as a result of lower taxable income in the economy, and higher outlays as a result of more spending on social insurance programs like food stamps and unemployment benefits. The end result would be a higher-than-expected budget deficit.

The difference between the administration’s economic growth projections and the private-sector Blue Chip consensus forecast is quite large. In fact, on average, the administration’s GDP forecast is *1.0 percentage point higher* than the Blue Chip forecast in *each* of the next 5 years. One percentage point may sound small, but in a \$14.3-trillion economy, the difference between 3 percent and 2 percent growth amounts to \$150 billion more output more than just 1 year.

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## ANALYSIS

Given the high degree of uncertainty about the economic outlook, the Budget Committee’s Republican staff conducted a “stress test” to see how the administration’s budget predictions might change with a less optimistic GDP forecast (i.e. the Blue Chip consensus). This analysis uses the rule-of-thumb methodology employed by the Office of Management and Budget [OMB] to gauge the impact on the budget from a GDP path that is 1.0 percentage point lower than expected over the next 5 years.<sup>1</sup>

*These calculations show that budget deficits would be more than \$750 billion higher than expected over the next 5 years if the economic recovery follows the Blue Chip consensus path instead of the administration’s desired recovery path.*

This alternative economic forecast would materially affect the administration’s budget predictions and alter its advertised deficit reduction. For instance, with this less rosy economic forecast, the administration’s deficit as a share of the overall economy would be close to 5.0 percent in 2014, well above its current 3.1 percent prediction for that year (see Table 2 below).

**Table 1**

<i>Billions of dollars</i>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2010-14</u>
Administration's GDP forecast	14,291	14,902	15,728	16,731	17,739	18,588	
February Blue Chip Consensus GDP	14,176	14,676	15,395	16,184	17,009	17,859	
<b>Increase in deficit using Blue Chip forecast*</b> (i.e. sustained 1 percent lower GDP growth)	<b>14</b>	<b>46</b>	<b>87</b>	<b>136</b>	<b>189</b>	<b>246</b>	<b>703</b>
Debt service costs of deficit increase*	--	--	2	7	17	29	55
<b>Total increase in deficit</b> (lower GDP path + higher debt service costs)	<b>14</b>	<b>46</b>	<b>89</b>	<b>143</b>	<b>206</b>	<b>275</b>	<b>758</b>

\* Estimated, House Budget Committee, Republican Staff

**Table 2**

	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>
Administration's deficit forecast	1,752	1,171	912	581	533	570
Administration's deficit as % of GDP	12.3	8.0	5.9	3.5	3.0	3.1
<b>New deficit forecast using Blue Chip GDP*</b>	<b>1766</b>	<b>1217</b>	<b>1001</b>	<b>724</b>	<b>739</b>	<b>845</b>
<b>New deficit as a share of Blue Chip GDP*</b>	<b>12.5</b>	<b>8.3</b>	<b>6.5</b>	<b>4.5</b>	<b>4.3</b>	<b>4.7</b>

\* Includes estimated debt service costs

<sup>1</sup> See OMB Table 12-5, Sensitivity of the Budget to Economic Assumptions:  
<http://www.gpoaccess.gov/usbudget/fy09/pdf/spec.pdf>

Federal regulators are currently “stress testing” the nation’s banks to see if they have sufficient capital to weather a few different economic scenarios. Their “adverse” scenario assumes a GDP decline in 2009 that is sharper than the Blue Chip consensus and growth in 2010 that is much more modest than the consensus. Applying OMB’s methodology to this GDP path shows budget deficits that are nearly \$1.2 trillion higher than the administration’s prediction over the next 5 years. This economic scenario would push the administration’s deficit as a share of the economy to 5.7 percent in 2014, compared to the current 3.1 percent prediction for that year (see Table 3 below).

**Table 3**

	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2010-14</u>
<b>Increase in deficit using "adverse" economic scenario*</b> (i.e. lower GDP growth than Blue Chip in '09 and '10)	<b>22</b>	<b>71</b>	<b>134</b>	<b>211</b>	<b>293</b>	<b>381</b>	<b>1,090</b>
Debt service costs of deficit increase*	--	1	3	11	26	46	86
<b>Total increase in deficit</b> (lower GDP path + higher debt service costs)	<b>22</b>	<b>72</b>	<b>137</b>	<b>222</b>	<b>319</b>	<b>427</b>	<b>1,177</b>
Administration's deficit forecast	1,752	1,171	912	581	533	570	
Administration's deficit as % of GDP	12.3	8.0	5.9	3.5	3.0	3.1	
<b>New deficit forecast using "adverse" GDP*</b>	<b>1,774</b>	<b>1,243</b>	<b>1,049</b>	<b>803</b>	<b>852</b>	<b>997</b>	
<b>New deficit as a share of "adverse" GDP*</b>	<b>12.6</b>	<b>8.7</b>	<b>7.0</b>	<b>5.1</b>	<b>5.1</b>	<b>5.7</b>	

\* Estimated, House Budget Committee, Republican Staff

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This document was prepared by the Republican staff of the Committee on the Budget, U.S. House of Representatives. It has not been approved by the full committee and may not reflect the views of individual committee members.