CHAPTER I. INTRODUCTION

This report presents projections made by the Congressional Budget Office (CBO) of federal revenues, budget authority, outlays, and credit activities for fiscal years 1984 through 1988. The projections take as their starting point taxing, spending, and lending policies for fiscal year 1983, as in effect at the end of the second session of the 97th Congress, and show what would happen if those policies were to continue unchanged for the following five fiscal years. The projections therefore do not represent a forecast of future federal budgets, since those budgets will doubtless include numerous policy changes. They are, however, a baseline or benchmark against which proposed policy changes may be measured and assessed.

Sometimes it is hard to determine what constitutes current government budgetary policies and how they should be projected into the future. Always it is difficult to predict the path of the economy and how it will affect the budget. Various assumptions can be made, and for each possible set of assumptions there will be a different baseline. Assumptions about the nature of current policies and the future of the economy must nevertheless be made if any realistic budget planning is to be done. The report clearly identifies the crucial assumptions and indicates, where appropriate, how an alternative choice would have affected the results.

THE BASELINE CONCEPT

Baseline budget projections are designed to show what would happen to the federal budget if current policies were to be continued into the future. This is not equivalent to assuming that there will be no new Congressional action. Without new legislation, spending programs requiring annual appropriation would quickly wither away because of the lack of funds; many other programs would disappear in later years as their authorizing legislation expired. The baseline projections assume that the Congress will take action as needed to continue the policies embodied in the current legislation, including the maintenance of real resource levels in the face of inflation.

The baseline revenue figures in this report are a projection of federal tax laws existing at the end of calendar year 1982. These tax laws are assumed to continue unchanged, and future tax changes called for under current law are generally assumed to occur as scheduled. This includes the expiration of various temporary tax provisions that have been enacted recently, such as the temporary increases in cigarette and telephone excise taxes enacted in 1982. The only exception to this rule is that airport and airway taxes are assumed to be continued beyond their 1987 expiration date, as they have been continued in the past.

The baseline concept for spending is more complex than that for revenues. Federal spending can be divided essentially into two categories. A large part of federal spending is mandated by existing law. This includes spending for Social Security benefits and other entitlement programs, for permanent appropriations such as interest on the public debt, and for most trust funds and other special funds. The baseline spending projections for these programs are comparable to the baseline revenue projections. It is assumed that existing law at the close of the second session of the 97th Congress will continue unchanged, and that future spending will respond to assumed economic and population changes in the same way that it has responded to such changes in the past.

The remainder of the federal spending budget is subject to annual review through the appropriations process. The baseline projections for these programs are generally based on fiscal year 1983 appropriation funding levels as enacted by the Congress through December 1982, with future increases to keep pace with inflation. For national defense, the baseline figures derive from the fiscal year 1983 budget resolutions, as extrapolated by CBO. Details on the baseline spending assumptions are provided in Appendix D.

This year for the first time, CBO is publishing projections of the federal credit budget--federal government loans and loan guarantees. Some direct loans and loan guarantees are subject to limits enacted in appropriations bills. The base for projecting government direct loans and loan guarantees consists of appropriation limits where enacted and CBO's estimates of obligations and commitments where programs have no appropriation limits or where program levels are below the appropriated limit. Projections of programs with appropriation limits assume credit levels that grow with inflation unless otherwise constrained by a permanent lending ceiling. Projections of programs without appropriation limits are CBO's estimates of activity for these programs, including an adjustment for inflation. For both limited and nonlimited programs, CBO's projections of credit levels are consistent with its unified and off-budget spending estimates.

THE USE OF BASELINE PROJECTIONS

The primary purpose of the CBO budget projections is to provide a neutral baseline against which the Congress can consider potential changes during its deliberations on the annual budget resolutions. A longer-term framework is helpful in making annual budget choices because these decisions frequently have little impact on the budget in the short run but can significantly influence the budget over a period of several years.

In 1982, the CBO baseline, modified somewhat to conform with economic and other assumptions agreed to by representatives of the Congress and the Administration, served as the so-called bipartisan baseline used for negotiations between the Congress and the Administration and for developing the Congressional budget resolution for fiscal year 1983. CBO budget projections also served as the baseline for computing the spending reductions and revenue increases to be achieved in the budget reconciliation process in 1981 and 1982. The reconciliation instructions contained in the First Concurrent Resolutions on the Budget for Fiscal Years 1982 and 1983 required certain Senate and House committees to reduce outlays or increase revenues by specified amounts from baseline levels, but each committee had discretion regarding how these savings were to be achieved.

CBO makes similar use of baseline budget projections in its bill cost estimates for calculating the costs or savings that would result from legislative proposals to change existing law. This is particularly important for calculating the budgetary effects of changes in entitlement programs, such as Social Security, Medicaid, veterans' pensions, and federal employee retirement.

PLAN OF THIS REPORT

Chapter II provides an overview of the baseline projections for revenues, budet authority, and outlays for 1984-1988. It begins with a discussion of the economic assumptions used for the projections and presents the baseline spending and revenue projections. The sensitivity of the budget projections to economic assumptions is demonstrated by showing how the projections would change under alternative high- and low-growth paths.

The third chapter presents detail on the baseline revenue projections, showing the revenues by major source. It also discusses the impact of the Economic Recovery Tax Act (ERTA) of 1981, the Tax Equity and Fiscal Responsibility Act (TEFRA) of 1982, and other recent tax legislation.

Chapter IV provides detail on the baseline spending projections. It is organized by the spending categories used in last year's budget debate--national defense, entitlements and other mandatory spending, nondefense discretionary spending, net interest, and offsetting receipts.

The last chapter consists of baseline projections of the credit budget. Since this is a new part of the baseline projections report, the chapter begins with definitions of terms used in the credit budget. The second part of the chapter contains historical data on federal lending and baseline projections of credit by the major purposes for which it is used.

The appendixes to this report contain a distribution of the baseline spending projections by budget function, major program category, and committee jurisdiction; a translation of the projections into national income and product account terms; and a detailed description of the programmatic assumptions underlying the baseline projections.

CHAPTER II. OVERVIEW OF THE PROJECTIONS

The Congressional Budget Office estimates that in fiscal year 1983 federal government revenues will equal $606 billion, outlays $800 billion, and the unified budget deficit $194 billion, or 6.1 percent of the gross national product (GNP). If current taxing and spending policies are continued unchanged, both revenues and outlays will grow in absolute dollars but will decline as a percentage of GNP. Since revenues and outlays as a percentage of GNP will fall by similar amounts, however, the baseline deficit remains level at 5.6 percent of GNP from 1984 to 1988. In the absence of tax increases or spending reductions, the unified budget deficit will equal $197 billion in 1984, $214 billion in 1985, and $267 billion in 1988.

These baseline projections are clearly not a forecast of what will actually happen. The economy may not perform as assumed for the projections. Future budgets undoubtedly will change present taxing and spending policies to adjust to changes in the economy and in national priorities. The baseline projections show the effect on the budget of continuing current policies under the CBO economic forecast for 1983-1984 and longer-run assumptions for 1985-1988.

ECONOMIC ASSUMPTIONS

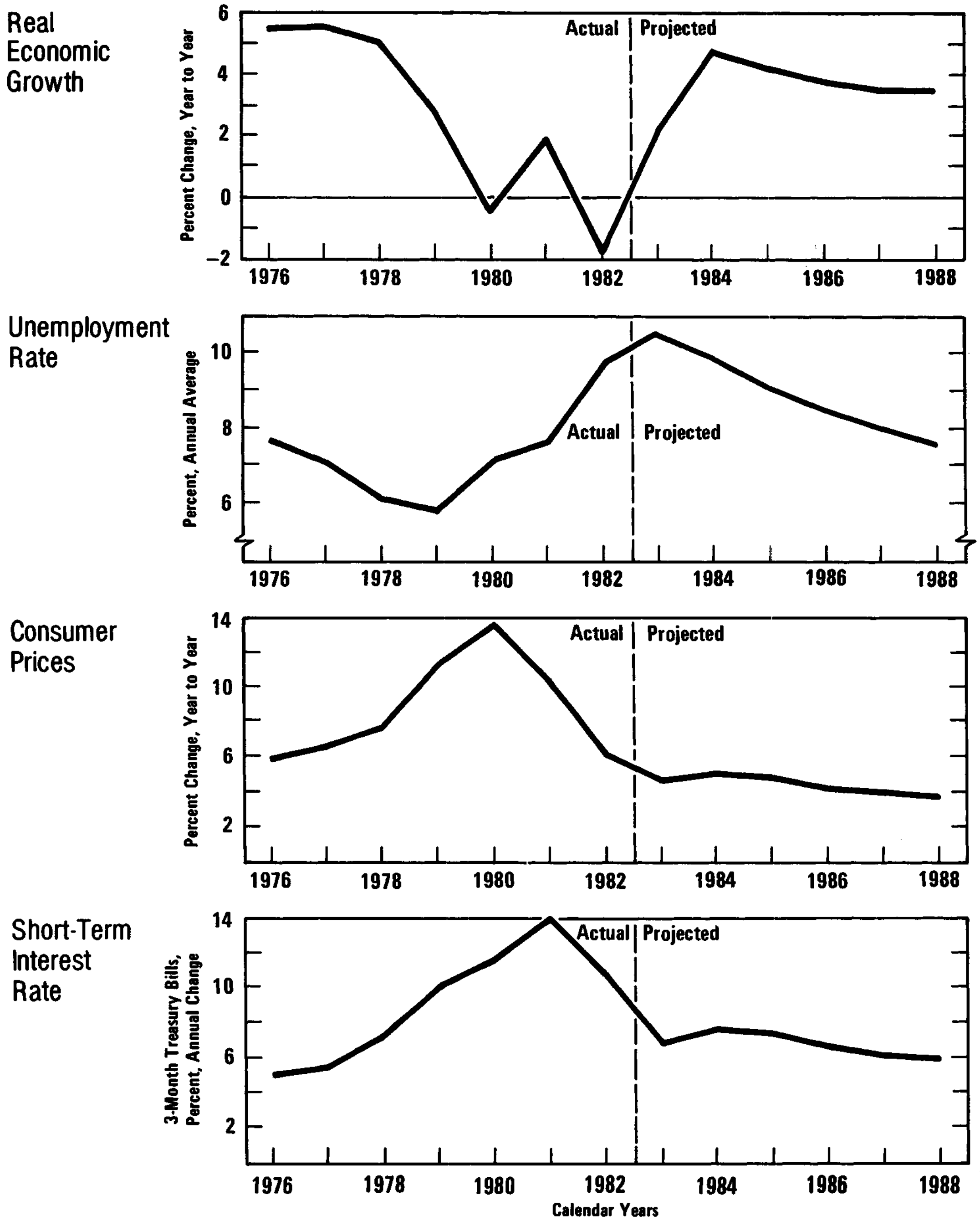
Since economic conditions have major effects on federal budget revenues and outlays, budget projections must be based on explicit assumptions about economic trends over the next several years. Tax receipts depend on taxable incomes, which reflect both real economic growth and inflation. About 30 percent of federal spending is directly indexed for inflation through automatic cost-of-living adjustments. The costs of certain benefit programs, such as unemployment insurance and food stamps, also depend on the level of unemployment in the economy. The costs of interest on the public debt depend on the level of interest rates. In the absence of major budget cuts or program increases, the remainder of the budget typically has kept pace with inflation through specific Congressional actions.

The major economic assumptions underlying the baseline budget projections are shown in Table 1 and displayed in Figure 1. These assump-

TABLE 1. BASELINE ECONOMIC ASSUMPTIONS (By calendar year, dollar amounts in billions)

	1982 Actual	Forecast		Longer-Run Assumptions			
		1983	1984	1985	1986	1987	1988
Gross National Product (GNP)							
Current dollars							
Amount	3,058	3,266	3,580	3,903	4,221	4,540	4,878
Percent change, year to year	4.1	6.8	9.6	9.0	8.1	7.6	7.4
Constant (1972) dollars							
Amount	1,476	1,506	1,577	1,642	1,703	1,762	1,824
Percent change, year to year	-1.8	2.1	4.7	4.1	3.7	3.5	3.5
Prices							
GNP deflator (percent change, year to year)	6.0	4.6	4.7	4.7	4.3	3.9	3.8
Consumer Price Index (percent change, year to year)	6.1	4.5	5.0	4.7	4.1	3.9	3.7
Unemployment Rate (percent, annual average)	9.7	10.6	9.8	9.0	8.4	8.0	7.5
Interest Rate (91-day Treasury bills, percent, annual average)	10.6	6.8	7.4	7.2	6.6	6.1	5.9

Figure 1.
Major Economic Assumptions



tions are explained in detail in a companion volume to this report; they are only summarized here. 1/

CBO projects a modest recovery from the current recession, with real growth rates of 2.1 percent in calendar years 1983 and 4.7 percent in 1984. The unemployment rate is projected to average 10.6 percent in calendar year 1983 and to decline to 9.8 percent in 1984. Inflation is expected not to increase substantially despite the recovery because of food and fuel price increases below the overall rate of inflation and because of lower wage growth owing to the high unemployment. The rate of growth in the GNP deflator, which was 6.0 percent in 1982, is projected to be 4.6 percent in 1983 and 4.7 percent in 1984.

Short-term interest rates are expected to decline somewhat from current levels and to rise slightly in 1984, as the recovery progresses. The three-month Treasury bill rate is projected to average 6.8 percent 1983 and 7.4 percent in 1984. In real terms, interest rates remain high in the forecast, providing a considerable restraint on economic growth.

While all short-run economic forecasts are subject to considerable uncertainty, the range of uncertainty is even greater for economic assumptions more than two years into the future. The economic assumptions for 1985 and beyond are therefore not a forecast but an extrapolation of the forecast for 1983 and 1984. They assume noncyclical moderate economic growth and declining inflation. It is by no means certain, however, that outyear projections are consistent with prospective monetary and fiscal policies, particularly the large federal deficits.

In the CBO long-run assumptions, growth in real GNP is 4.1 percent in 1985 and slows to 3.5 percent by 1988. Unemployment gradually declines to 7.5 percent by 1988. The growth rate of the GNP deflator slows to 3.8 percent by 1988 because of prolonged high unemployment and below-average growth in food and fuel prices. The three-month Treasury bill rate is assumed to decline to 5.9 percent by 1988.

BASELINE BUDGET PROJECTIONS

As a result of the current deep recession and the record level of unemployment, the federal budget deficit is projected to reach another postwar record in fiscal year 1983. While the 1982 deficit was an

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1. See Congressional Budget Office, The Outlook for Recovery, (February 1983).

unprecedented $111 billion, the 1983 deficit is likely to be almost twice as large--$194 billion. This figure would represent 6.1 percent of GNP, a level never before reached in the post-World War II period. The 1984 baseline deficit is projected to be $197 billion--a slight decline to 5.6 percent of GNP. In later years, the deficit grows in dollar terms and remains level as a percentage of GNP (see Table 2).

These large projected deficits will lead to a substantial increase in the federal debt. Debt held by the public will grow from $929 billion at the beginning of 1983 to $2.4 trillion at the end of 1988--an increase of over 150 percent.

TABLE 2. BASELINE BUDGET PROJECTIONS (By fiscal year)

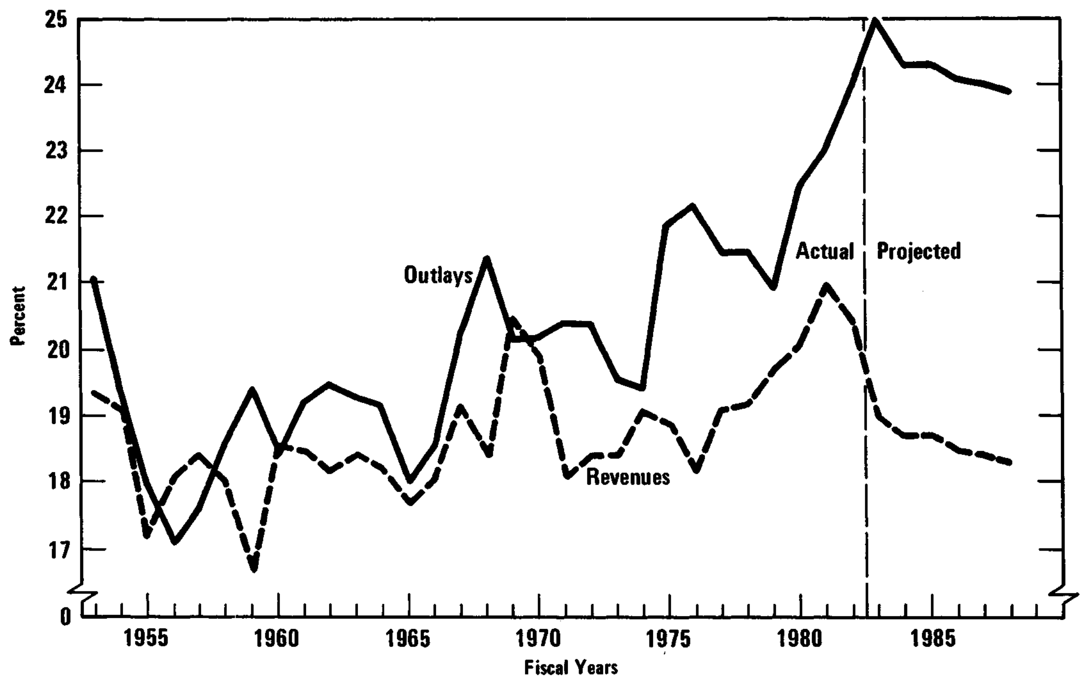
	1982 Actual	1983 Base	Projections				
			1984	1985	1986	1987	1988
	In Billions of Dollars						
Baseline Revenues	618	606	653	715	768	822	878
Baseline Outlays	728	800	850	929	999	1,072	1,145
Baseline Unified Budget Deficit	**111**	**194**	**197**	**214**	**231**	**250**	**267**
Outlays of Off-Budget Federal Entities	17	17	15	16	19	17	17
Total Deficit, Including Off-Budget	128	210	212	231	250	267	284
	As a Percent of GNP						
Baseline Revenues	20.4	19.0	18.7	18.7	18.5	18.4	18.3
Baseline Outlays	24.0	25.0	24.3	24.3	24.1	24.0	23.9
Baseline Unified Budget Deficit	**3.6**	**6.1**	**5.6**	**5.6**	**5.6**	**5.6**	**5.6**
Outlays of Off-Budget Federal Entities	0.6	0.5	0.4	0.4	0.4	0.4	0.4
Total Deficit, Including Off-Budget	4.2	6.6	6.1	6.0	6.0	6.0	5.9

Revenues. Federal revenues in 1983 are projected to be $606 billion-- $12 billion less than the 1982 amount. Because of the recession, taxable personal income will increase by only 4.4 percent, and this increase will not be sufficient to overcome the effects of the lower 1983 personal income tax rates. Corporation income taxes are also projected to fall because of the recession, despite the corporate tax increases enacted in 1982.

Baseline revenues are projected to rise from $606 billion in 1983 to $878 billion in 1988--an increase of 45 percent in five years. This represents an average growth of 7.7 percent a year, compared with an assumed average growth in nominal GNP of 8.4 percent a year. Thus, as displayed in Figure 2, baseline revenues as a proportion of GNP are projected to decline from 20.4 percent in 1982 to 18.3 percent in 1988. The decline is relatively rapid during 1983 and 1984, when staged reductions in individual income taxes take place, but slows thereafter.

Outlays. Federal outlays in 1983 are projected to reach $800 billion-- an increase of $72 billion from 1982. In the later years, baseline outlays are

Figure 2.
Federal Revenues and Outlays as a Percentage of GNP



projected to increase at a slightly slower pace than revenues. Under baseline assumptions, outlays would rise from $800 billion in 1983 to $850 billion in 1984 and over $1.1 trillion by 1988. This represents an average annual growth in outlays of 7.4 percent during the projection period (1983 to 1988), or about one percentage point less than the assumed growth in GNP and 0.3 percentage point less than the projected growth in revenues. Under baseline assumptions, outlays would decline as a share of GNP--from 25.0 percent in 1983 to 23.9 percent in 1988. By 1988, however, the ratio of federal outlays to GNP would still be higher than for all postwar years before 1982.

Unified Budget Deficit. Under baseline assumptions, the unified budget deficit would equal $194 billion (6.1 percent of GNP) in 1983 and $197 billion (5.6 percent of GNP) in 1984.

The 1984 deficit would grow in dollar terms, but would remain roughly constant as a percentage of GNP. By 1988, the deficit would equal $267 billion.

Off-Budget Outlays. The spending of certain federal entities has, by law, been excluded from the unified budget totals. The outlays of these off-budget entities, however, must be added to the budget deficit to derive the total federal deficit that must be financed. Table 2 therefore shows the CBO baseline projection of the outlays of off-budget federal entities and of the total deficit.

Under baseline assumptions, the outlays of the off-budget federal entities are projected to be $17 billion in 1983 and to average the same amount in 1984-1988. Off-budget outlays will equal 0.5 percent of GNP in 1983 and 0.4 percent of GNP in later years. Taking into account off-budget outlays, the total federal deficit is projected to decline from 6.6 percent of GNP in 1983 to 6.1 percent in 1984 and 5.9 percent by 1988.

Federal Debt. At the end of fiscal year 1982, the federal debt subject to statutory limit exceeded $1.1 trillion. Of this amount, slightly over $900 million was held by the public, with the remainder being held by federal government trust and other funds.

The large baseline deficits, both on- and off-budget, would cause debt held by the public to increase by one and one-half times over the next five years. By the end of fiscal year 1988, debt held by the public would swell to $2.4 trillion (see Table 3). Total debt subject to limit, which also rises as government trust funds increase their holdings of federal securities, would reach $2.6 trillion.

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TABLE 3. PROJECTIONS OF FEDERAL GOVERNMENT DEBT
(By fiscal year, dollar amounts in billions)

	1982 Actual	Projections					
		1983	1984	1985	1986	1987	1988
Debt Subject to Limit (beginning of year)	999	1,143	1,344	1,562	1,804	2,068	2,347
Increase in Debt Subject to Limit							
Unified budget deficit	111	194	197	215	231	250	267
Trust fund surplus	6	1	6	11	14	12	9
Off-budget deficit	17	17	15	16	19	17	17
Means of financing (other than borrowing) and other adjustments	11	-11	--	--	--	--	--
Total Increase	144	201	218	242	264	279	293
Debt Subject to Limit (end of year)	1,143	1,344	1,562	1,804	2,068	2,347	2,640
Debt Held by the Public (end of year) a/	929	1,128	1,340	1,571	1,820	2,087	2,372
Debt Held by the Public as a Percent of GNP b/	30.6	35.3	38.3	41.1	43.9	46.8	49.5

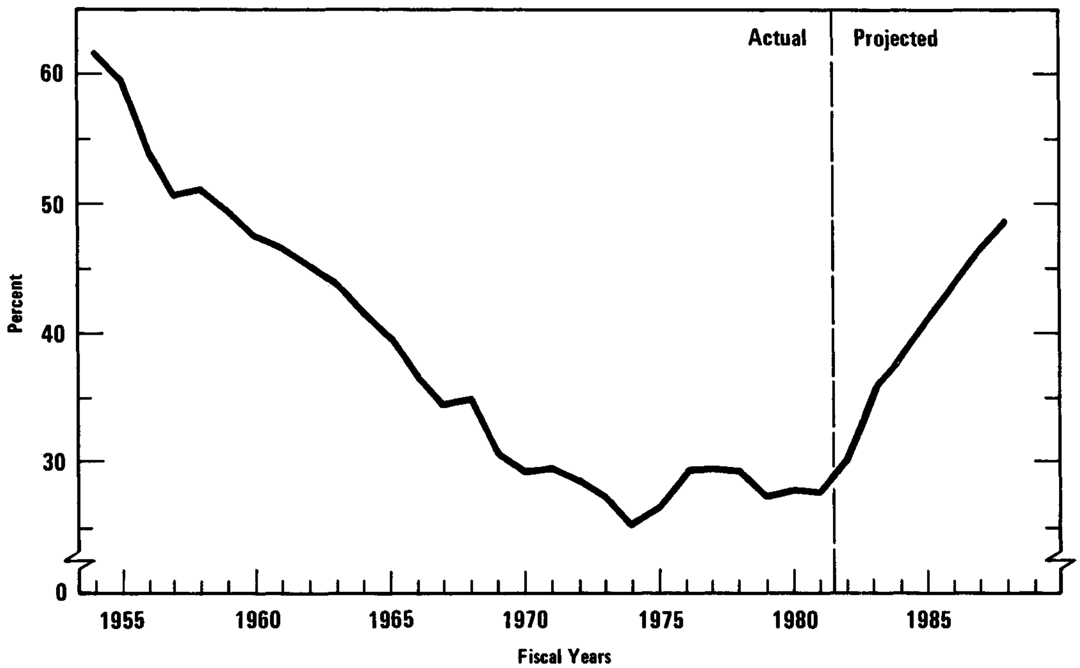
NOTE: Details may not add due to rounding.

a. Includes debt held by the Federal Reserve System.

b. Debt at the end of the year as a percentage of GNP during the year.

Debt increases of this magnitude would also reverse a long-run decline in the ratio of debt held by the public to gross national product. During the 1950s and 1960s, as illustrated in Figure 3, debt held by the public declined substantially in relation to GNP. The ratio then remained roughly level during the 1970s. Under baseline assumptions, however, debt held by the public as a percentage of GNP would, by 1988, reach a level not seen since 1960.

Figure 3.
Federal Debt Held by the Public as a Percentage of GNP



ALTERNATIVE ECONOMIC ASSUMPTIONS

As noted above, budget projections depend greatly on their underlying economic assumptions; changes in economic conditions can have major effects on revenues, outlays, and the deficit. Yet, forecasting economic conditions is subject to great uncertainty. Consequently, this section examines how the baseline budget figures would vary under alternative economic assumptions.

Although the economic assumptions underlying the baseline are those that CBO believes to be most likely, there is a good chance that the economy will perform differently than assumed. To illustrate the possibilities, CBO has prepared two alternative sets of economic assumptions, detailed in Table 4.

The first alternative is a high-growth path, with lower interest rates, lower unemployment, and slightly higher inflation. Real GNP grows at approximately the rate of a normal post-World War II cyclical recovery in the first three years. Thereafter, real growth continues at 4 percent annually. Inflation, as measured by the GNP deflator, averages 4.9 percent a year from 1983 to 1988, and the unemployment rate drops to 6.0 percent by the end of the period.

In the low-growth path, on the other hand, interest rates and unemployment are assumed to be higher and inflation is lower. The growth rate in real GNP is 0.8 percent in 1983 and averages 3.2 percent a year over the 1984-1988 period. Inflation averages 4 percent, and unemployment drops to 9 percent by 1988.

The revenues, outlays, and deficits resulting from these alternative economic assumptions are summarized in Table 5. As would be expected, revenues are higher in the high-growth case and lower in the low-growth case than they are in the baseline. These differences result primarily from differences in assumed rates of real growth, since the ratio of revenues to GNP varies little across the three alternatives. The slight differences among the ratios of revenues to GNP under the different growth assumptions result from complex interactions between changing income shares (corporate income tends to become a larger portion of GNP when growth rates are higher) and changing effective tax rates. The current tax system, with its emphasis on accelerated depreciation, leads to lower effective tax rates on business income when economic growth and investment are higher.

Conversely, outlays in the high-growth alternative are lower than those in the baseline both in dollar terms and as a percentage of GNP. Lower unemployment reduces outlays for unemployment compensation and shrinks the number of low-income persons eligible for Medicaid, food stamps, and assistance payments. Net interest outlays are also lower, both because of lower interest rates and the lower deficits (resulting from the other changes in revenues and outlays) that must be financed. The higher inflation assumption tends to increase outlays, but this effect is more than offset by the impacts of lower unemployment and interest rates. All of these factors operate in reverse in causing outlays in the low-growth alternative to be higher than in the baseline.

TABLE 4. ALTERNATIVE ECONOMIC ASSUMPTIONS (By calendar year)

	1983	1984	1985	1986	1987	1988
Gross National Product (GNP)						
Current dollars (percent change, year to year)						
High-growth alternative	9.0	11.3	9.5	9.1	8.9	8.1
CBO baseline projection	6.8	9.6	9.0	8.1	7.6	7.4
Low-growth alternative	5.4	7.9	7.9	7.2	6.6	6.4
Constant (1972) dollars (percent change, year to year)						
High-growth alternative	4.0	6.0	4.2	4.0	4.0	4.0
CBO baseline projection	2.1	4.7	4.1	3.7	3.5	3.5
Low-growth alternative	0.8	3.3	3.3	3.2	3.0	3.0
Prices						
GNP deflator (percent change, year to year)						
High-growth alternative	4.8	4.9	5.1	4.9	4.8	4.9
CBO baseline projection	4.6	4.7	4.7	4.3	3.9	3.8
Low-growth alternative	4.5	4.4	4.4	3.9	3.5	3.2
Consumer Price Index (percent change, year to year)						
High-growth alternative	4.6	5.3	5.0	4.6	4.6	4.8
CBO baseline projection	4.5	5.0	4.6	4.1	3.9	3.7
Low-growth alternative	4.5	4.9	4.4	3.8	3.4	3.2
Unemployment Rate (percent, annual average)						
High-growth alternative	9.9	8.5	7.7	7.0	6.4	6.0
CBO baseline projection	10.6	9.8	9.0	8.4	8.0	7.5
Low-growth alternative	11.2	10.9	10.3	9.8	9.4	9.0
Interest Rate (91-day Treasury bills, percent, annual average)						
High-growth alternative	4.4	5.4	5.7	5.0	5.0	4.9
CBO baseline projection	6.8	7.4	7.2	6.6	6.1	5.9
Low-growth alternative	8.4	9.9	8.9	7.7	7.2	6.3

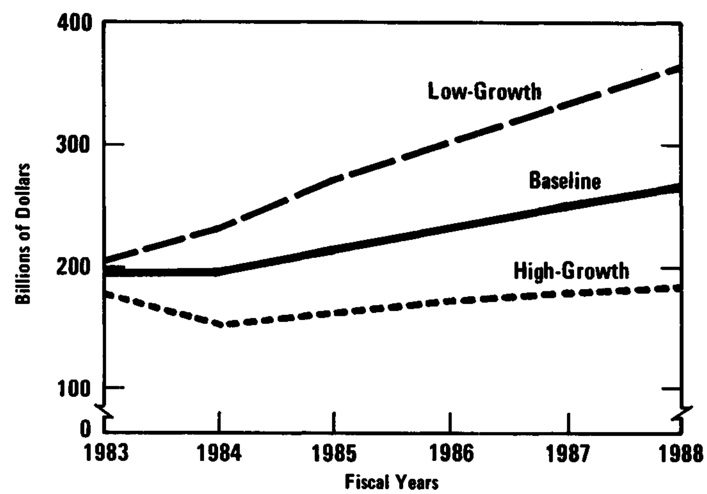
TABLE 5. BASELINE BUDGET PROJECTIONS UNDER ALTERNATIVE ECONOMIC ASSUMPTIONS (By fiscal year)

	1983	1984	1985	1986	1987	1988
		In Billions of Dollars				
Baseline Revenues						
High-growth alternative	615	676	742	798	862	933
CBO baseline projection	606	653	715	768	822	878
Low-growth alternative	599	636	686	730	777	825
Baseline Outlays						
High-growth alternative	793	830	904	971	1,041	1,116
CBO baseline projection	800	850	929	999	1,072	1,145
Low-growth alternative	804	868	958	1,032	1,110	1,187
Baseline Unified Budget Deficit						
High-growth alternative	178	155	162	172	179	183
CBO baseline projection	194	197	214	231	250	267
Low-growth alternative	205	232	272	302	333	363
		As a Percent of GNP				
Baseline Revenues						
High-growth alternative	19.0	18.7	18.7	18.4	18.3	18.1
CBO baseline projection	19.0	18.7	18.7	18.5	18.4	18.3
Low-growth alternative	18.9	18.7	18.6	18.5	18.4	18.4
Baseline Outlays						
High-growth alternative	24.4	23.0	22.8	22.4	22.1	21.7
CBO baseline projection	25.0	24.3	24.3	24.1	24.0	23.9
Low-growth alternative	25.3	25.5	26.0	26.1	26.3	26.5
Baseline Unified Budget Deficit						
High-growth alternative	5.5	4.3	4.1	4.0	3.8	3.6
CBO baseline projection	6.1	5.6	5.6	5.6	5.6	5.6
Low-growth alternative	6.5	6.8	7.4	7.6	7.9	8.1

Under the low-growth baseline, the deficit would rise even more sharply than in the baseline case. It would reach $363 billion by 1988 and would represent 8.1 percent of GNP (see Figure 4). Under the high-growth alternative, on the other hand, the deficit would be relatively flat. It would decline a bit from 1983 to 1984, and would increase modestly thereafter. By 1988, the deficit would be within $5 billion of its 1983 amount, although it would have declined from 5.5 percent to 3.6 percent of GNP. Even with the assumption of a normally strong economic recovery, therefore, the federal budget would still show large deficits for the next several years.

Figure 4.

Federal Deficit Under Alternative Economic Assumptions



COMPARISON OF 1983 AND 1981 BASELINE PROJECTIONS

The 1983 baseline projections differ significantly from the baseline projections produced two years ago. The baseline projections used for the first budget resolution for fiscal year 1982 showed a unified budget deficit of $30 billion in 1982 and growing budget surpluses in 1983-1986. 1/ The actual 1982 deficit was $111 billion, and the latest baseline projections show large budget deficits for 1983-1986. Table 6 compares the two sets of baseline projections and summarizes the basic reasons for the remarkable change in budget outlook.

TABLE 6. DIFFERENCES BETWEEN JULY 1981 AND FEBRUARY 1983 BASELINE DEFICIT PROJECTIONS (By fiscal year, in billions of dollars)

	1982	1983	1984	1985	1986
July 1981 Baseline Surplus or Deficit (-)	-30	28	76	138	209
Differences Due to					
Changed economic outlook	-71	-152	-173	-196	-230
Legislative actions	3	-34	-74	-128	-186
Technical estimating changes	-12	-26	-27	-28	-24
Total Differences	-80	-212	-274	-353	-440
February 1983 Baseline Deficit	-111	-194	-197	-214	-231

In each year from 1982 to 1986, the difference between two baseline paths results primarily from a changed economic outlook. Over the entire five-year period, 60 percent of the change in outlook from budget surpluses to budget deficits can be attributed to the failure of the economy to perform as projected two years ago. The economic assumptions of the July 1981 baseline were those used for the conference agreement on the first budget resolution for fiscal year 1982. They also corresponded closely to the economic projections assumed by the Administration for its fiscal year 1982 budget revisions that were submitted to the Congress in March 1981.

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1. Congressional Budget Office, Baseline Budget Projections: Fiscal Years 1982-1986 (July 1981).

Those assumptions, which are laid out in Table 7, reflected the view of the Administration and the budget resolution conferees that the fiscal and monetary restraint in the President's economic program, together with a general lowering of inflationary expectations, would lead to a steady reduction in inflation and interest rates in an environment of substantial real economic growth. The assumptions did not foresee the recession that developed in 1981 or the low rates of real economic growth that are now anticipated for the next several years. The assumptions also incorporated higher rates of inflation than the current CBO forecast envisions, as shown in Table 7.

TABLE 7. COMPARISON OF JULY 1981 AND FEBRUARY 1983 BASELINE ECONOMIC ASSUMPTIONS (By calendar year)

	1981	1982	1983	1984	1985	1986
Gross National Product (GNP)						
Current dollars (percent change, year to year)						
July 1981 Baseline	12.0	13.0	12.4	10.8	9.8	9.3
February 1983 Baseline a/	11.6	4.1	6.8	9.6	9.0	8.1
Constant (1972) dollars (percent change, year to year)						
July 1981 Baseline	2.0	4.1	5.0	4.5	4.2	4.2
February 1983 Baseline a/	1.9	-1.8	2.1	4.7	4.1	3.7
Prices						
GNP deflator (percent change, year to year)						
July 1981 Baseline	9.7	8.6	7.0	6.0	5.4	4.9
February 1983 Baseline a/	9.4	6.0	4.6	4.7	4.7	4.3
Consumer Price Index (percent change, year to year)						
July 1981 Baseline	11.0	8.3	6.2	5.5	4.7	4.2
February 1983 Baseline a/	10.3	6.1	4.5	5.0	4.6	4.1
Unemployment Rate (percent, annual average)						
July 1981 Baseline	7.5	7.2	6.6	6.4	5.9	5.6
February 1983 Baseline a/	7.6	9.7	10.6	9.8	9.0	8.4
Interest Rate (91-day Treasury bills, percent, annual average)						
July 1981 Baseline	13.5	10.5	9.4	8.2	7.0	6.0
February 1983 Baseline a/	14.0	10.6	6.8	7.4	7.2	6.6

a. Figures for 1981 and 1982 are actual values.

On the outlay side of the budget, the effects of higher unemployment and lower inflation are largely offsetting. Both factors combine, however, to result in substantial revenue losses. These are discussed in more detail in Chapter III.

Legislative actions are the second largest reason for differences between the two baselines, accounting for about 30 percent of the change over the five-year period. The legislative differences can be subdivided into four categories, which are displayed in Table 8. First, changes in the tax law have resulted in net revenue reductions growing from $38 billion in 1982 to $154 billion by 1986. As detailed in Chapter III, these changes include both the tax cuts provided by the Economic Recovery Tax Act of 1981 and the tax increases contained in the Tax Equity and Fiscal Responsibility Act of 1982.

TABLE 8. DIFFERENCES BETWEEN JULY 1981 AND FEBRUARY 1983 BASELINE DEFICIT PROJECTIONS ATTRIBUTABLE TO LEGISLATIVE ACTION (By fiscal year, in billions of dollars)

	1982	1983	1984	1985	1986
Tax Reductions	38	63	93	121	154
Defense Spending Increases	1	15	27	47	65
Nondefense Spending Cuts	-42	-47	-56	-59	-61
Effect of Legislative Actions on Interest Costs	*	3	10	19	28
Total Legislative Actions	-3	34	74	128	186

Defense spending increases added $1 billion to baseline outlays in 1982 and $15 billion in 1983 and are projected to increase 1986 spending by $65 billion. Nondefense spending cuts reduced 1982 baseline outlays by $42 billion, with the savings projected to grow to $61 billion by 1986. By 1986, the defense and nondefense policy changes roughly offset each other, although the nondefense reductions are greater than the defense increases in the earlier years. Since the net effect of these legislative changes is to increase the deficit in 1983 and thereafter, interest costs also rise because of the higher deficits that must be financed.

The final source of differences between the July 1981 and the February 1983 projections is technical estimating changes. These consist primarily of unexpectedly higher outlays for farm price supports and Medicare benefits and lower receipts from offshore oil leases. They account for less than 10 percent of the differences between the two sets of projections.