

January 1995

THE ECONOMIC AND BUDGET OUTLOOK: FISCAL YEARS 1996-2000

No fundamental change in the economic or budget situation has occurred since last summer, according to the Congressional Budget Office's report *The Economic and Budget Outlook: Fiscal Years 1996-2000*. The economy may be a bit more robust in 1995 than had been anticipated at that time, but a likely slowdown in growth in 1996 leaves the long-term economic outlook little different from that described by CBO in August 1994. CBO projects that the deficit will decline for the third straight year--to \$176 billion in 1995--but will start growing again in 1996 (see table on the reverse side). The deficits projected for 1995 through 1999 are \$25 billion higher on average than CBO estimated last August. After 2002, however, the deficits in the new extended projections are a little lower than the deficits projected in the summer.

CBO expects that the high level of investment and consumer purchases that spurred the economy to a 4 percent real rate of growth in 1994 will continue into the first part of 1995. Because the economy is already operating close to its potential, that growth is expected to result in somewhat higher rates of inflation and interest. In turn, those higher interest rates are likely to slow growth by the end of 1995--cutting it to 3.1 percent in 1995 and 1.8 percent in 1996 and dampening inflationary pressures. In CBO's longer-term projections, average annual growth after 1996 is close to the 2.4 percent rate of growth estimated for potential gross domestic product (GDP). Over the 1997-2000 period covered by those projections, inflation averages 3.4 percent and interest rates drift down.

CBO projects that the deficit will decline from the \$203 billion registered in 1994 to \$176 billion in 1995, the lowest level since 1989 and the lowest as a percentage of GDP (2.5 percent) since 1979. After reaching a trough in 1995, the deficit will rise to \$207 billion in 1996 (2.8 percent of GDP), grow again in 1997, and then level off in 1998. Those projections assume no change in current policies governing taxes and mandatory spending; they also assume compliance with the limits on discretionary appropriations that are in place through 1998. Under the assumption that spending for discretionary programs increases at the rate of inflation after 1998, deficits will grow to \$284 billion (3.1 percent of GDP) in 2000, the last year of CBO's regular projections. Under an alternative baseline that assumes that discretionary spending remains frozen at the dollar level of the 1998 caps, deficits increase only to \$243 billion (2.7 percent of GDP) in 2000.

CBO's less detailed extended projections (with discretionary spending adjusted for inflation after 1998) show a deficit of \$322 billion in 2002, the first year that a proposed constitutional amendment requiring a balanced budget could go into effect. To illustrate the magnitude of the task of complying with the balanced budget requirement, CBO has constructed an illustrative path leading to a balanced budget in 2002 that entails deficit reduction of \$1.2 trillion over the 1996-2002 period. Major changes in current policies would be required to achieve deficit reduction on that scale.

Questions concerning the budget projections should be directed to CBO's Budget Analysis Division (202-226-2880) and inquiries about the economic forecast to the Macroeconomic Analysis Division (226-2750). The Office of Intergovernmental Relations is CBO's Congressional liaison office and can be reached at 226-2600. For additional copies of the report, please call the Publications Office at 226-2809.



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Budget Projections and Underlying Assumptions

	1994	1995	1996	1997	1998	1999	2000
Budget Projections (By fiscal year)							
<i>In Billions of Dollars</i>							
Baseline Total Deficit^a							
With discretionary inflation after 1998	203	176	207	224	222	253	284
Without discretionary inflation after 1998	203	176	207	224	222	234	243
Standardized-Employment Deficit^b							
With discretionary inflation after 1998	187	200	216	223	221	247	273
Without discretionary inflation after 1998	187	200	216	223	221	228	233
<i>As a Percentage of GDP</i>							
Baseline Total Deficit							
With discretionary inflation after 1998	3.1	2.5	2.8	2.9	2.7	3.0	3.1
Without discretionary inflation after 1998	3.1	2.5	2.8	2.9	2.7	2.7	2.7
Standardized-Employment Deficit^c							
With discretionary inflation after 1998	2.8	2.8	2.9	2.9	2.7	2.9	3.0
Without discretionary inflation after 1998	2.8	2.8	2.9	2.9	2.7	2.6	2.6
Economic Assumptions (By calendar year)							
Nominal GDP (Billions of dollars) ^d	6,737	7,127	7,456	7,847	8,256	8,680	9,128
Real GDP (Percentage change)	4.0	3.1	1.8	2.4	2.3	2.3	2.3
CPI-U (Percentage change) ^e	2.6	3.1	3.4	3.4	3.4	3.4	3.4
Unemployment Rate (Percent)	6.1	5.5	5.7	5.8	5.9	6.0	6.0
Three-Month Treasury Bill Rate (Percent)	4.2	6.2	5.7	5.3	5.1	5.1	5.1
Ten-Year Treasury Note Rate (Percent)	7.1	7.7	7.0	6.7	6.7	6.7	6.7

SOURCE: Congressional Budget Office.

- a. Caps on discretionary spending are set by law through 1998. Measures of the deficit "with discretionary inflation" assume that discretionary spending grows at the rate of inflation after 1998. Measures of the deficit "without discretionary inflation" assume that discretionary spending remains frozen in dollar terms at the level of the 1998 caps.
 - b. Excludes the cyclical deficit and spending for deposit insurance.
 - c. Shown as a percentage of potential gross domestic product.
 - d. Gross domestic product in 1994 reflects data published by the Bureau of Economic Analysis on January 27, 1995.
 - e. CPI-U is the consumer price index for all urban consumers.
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