



Congressional Budget Office

**Presentation to the
National Association for Business Economics**

Four Observations about the Federal Budget

March 7, 2011

**Douglas W. Elmendorf
Director**



Four Observations about the Federal Budget

1. The gap between spending and revenues is likely to remain very large even after we return to normal economic conditions.
2. Fiscal policy cannot be put on a sustainable path just by eliminating waste and inefficiency; the policy changes that are needed will significantly affect popular programs or people's tax payments or both.
3. Policymakers face difficult tradeoffs in deciding how quickly to implement policy changes that would reduce future budget deficits.
4. There is more focus in Washington on federal budget problems today than there has been since the late 1990s, and that focus has led to a range of proposals for tackling the problems.

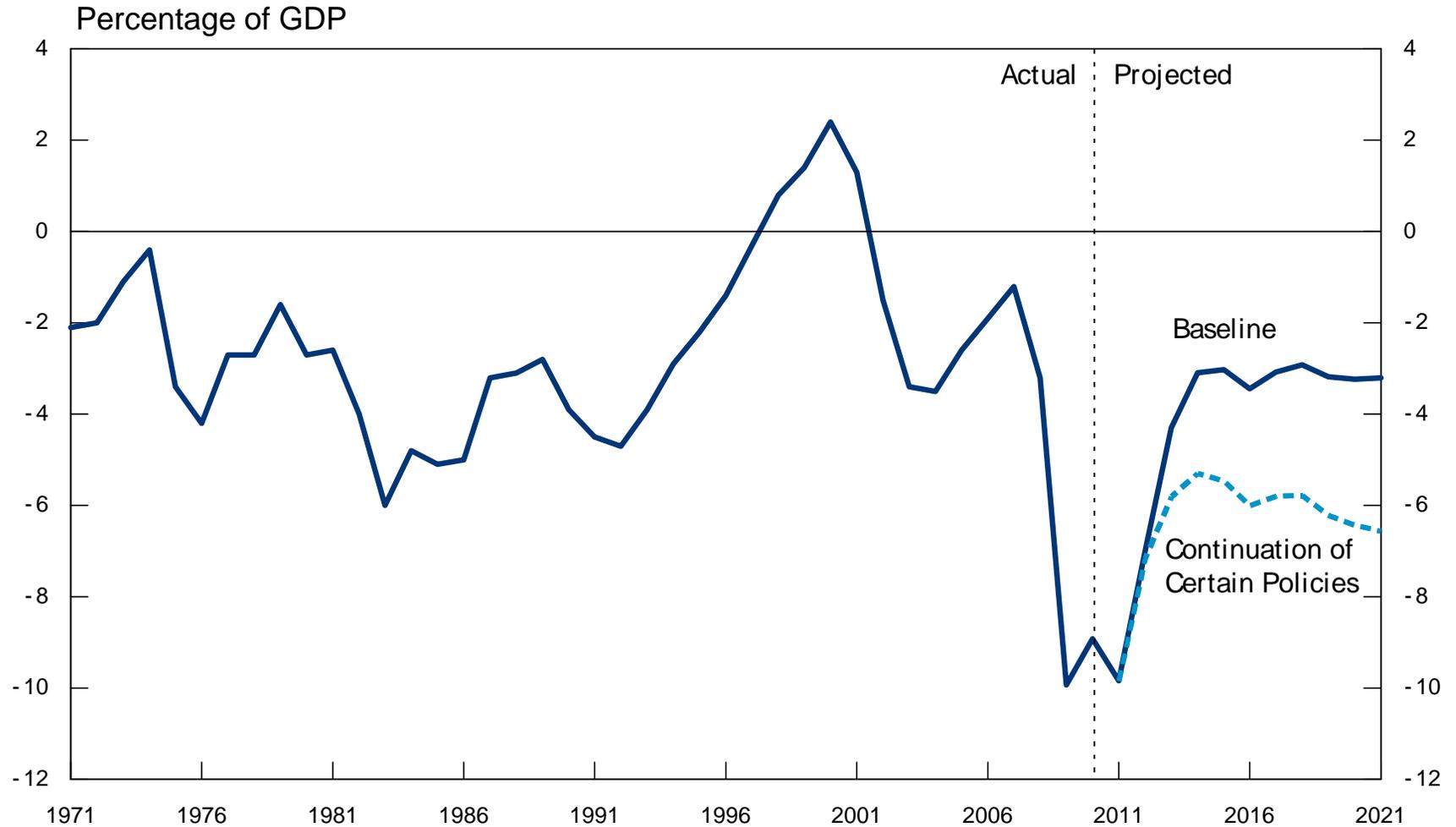


Observation #1

The gap between spending and revenues is likely to remain very large even after we return to normal economic conditions.

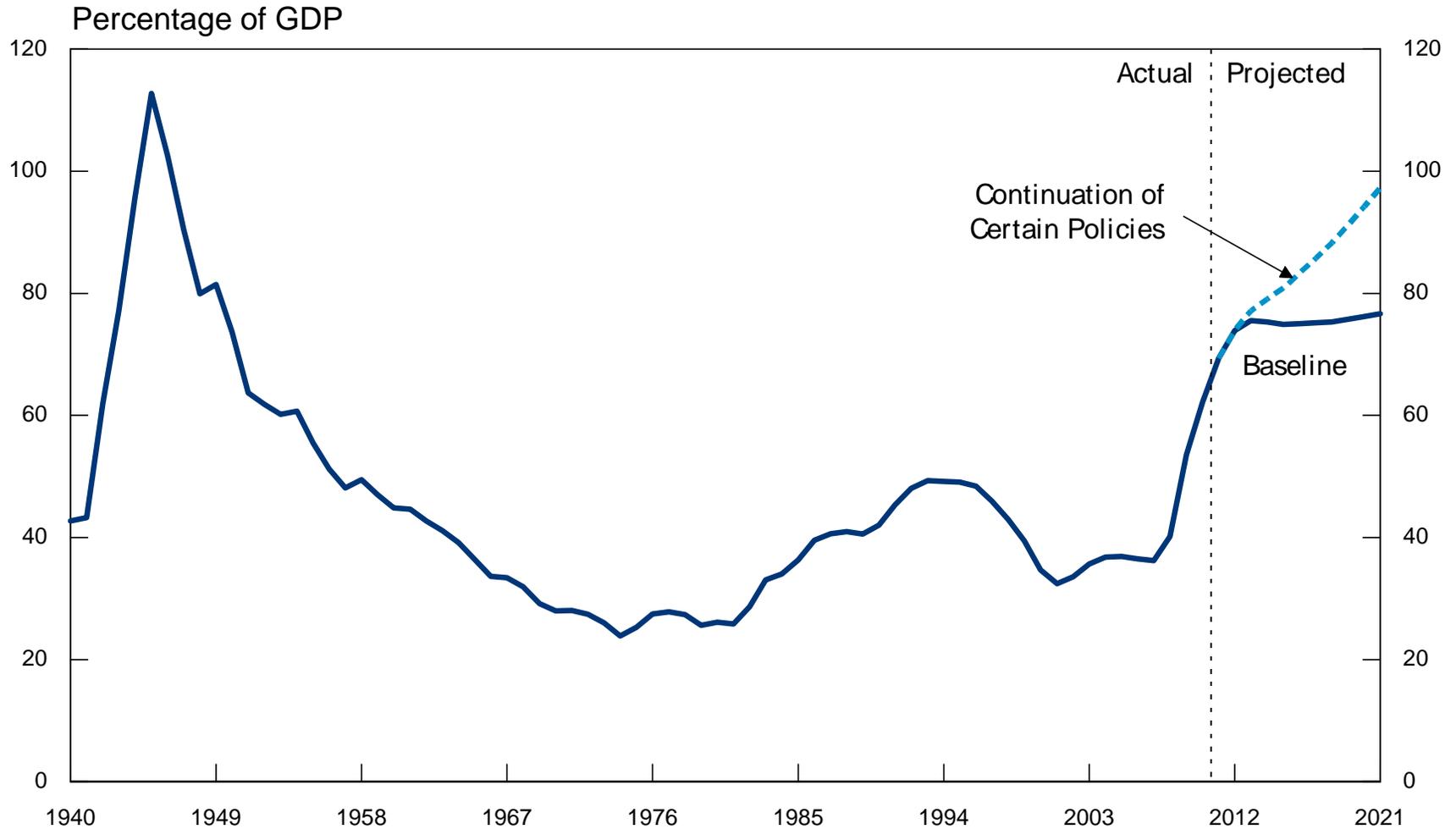


Deficits Under CBO's Baseline or with a Continuation of Certain Policies, Compared with Past Deficits and Surpluses



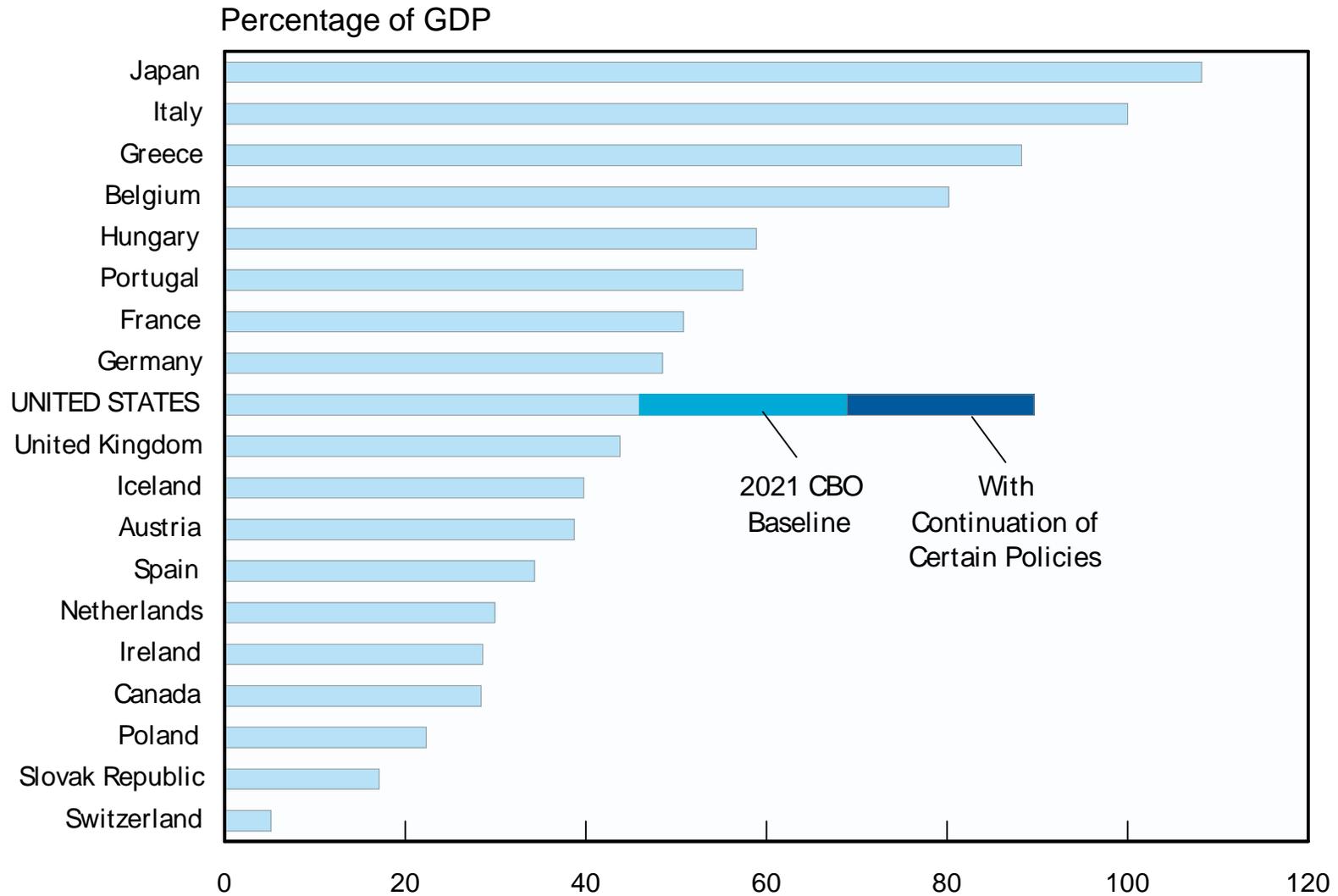


Federal Debt Held by the Public Under CBO's Baseline or with a Continuation of Certain Policies, Compared with Past Debt





Debt Burden Across Countries in 2009



Source: For the United States, debt held by the public net of financial assets. For other countries, general government debt net of financial liabilities as reported by the Organisation for Economic Co-operation and Development.



Observation #2

Fiscal policy cannot be put on a sustainable path just by eliminating waste and inefficiency; the policy changes that are needed will significantly affect popular programs or people's tax payments or both.



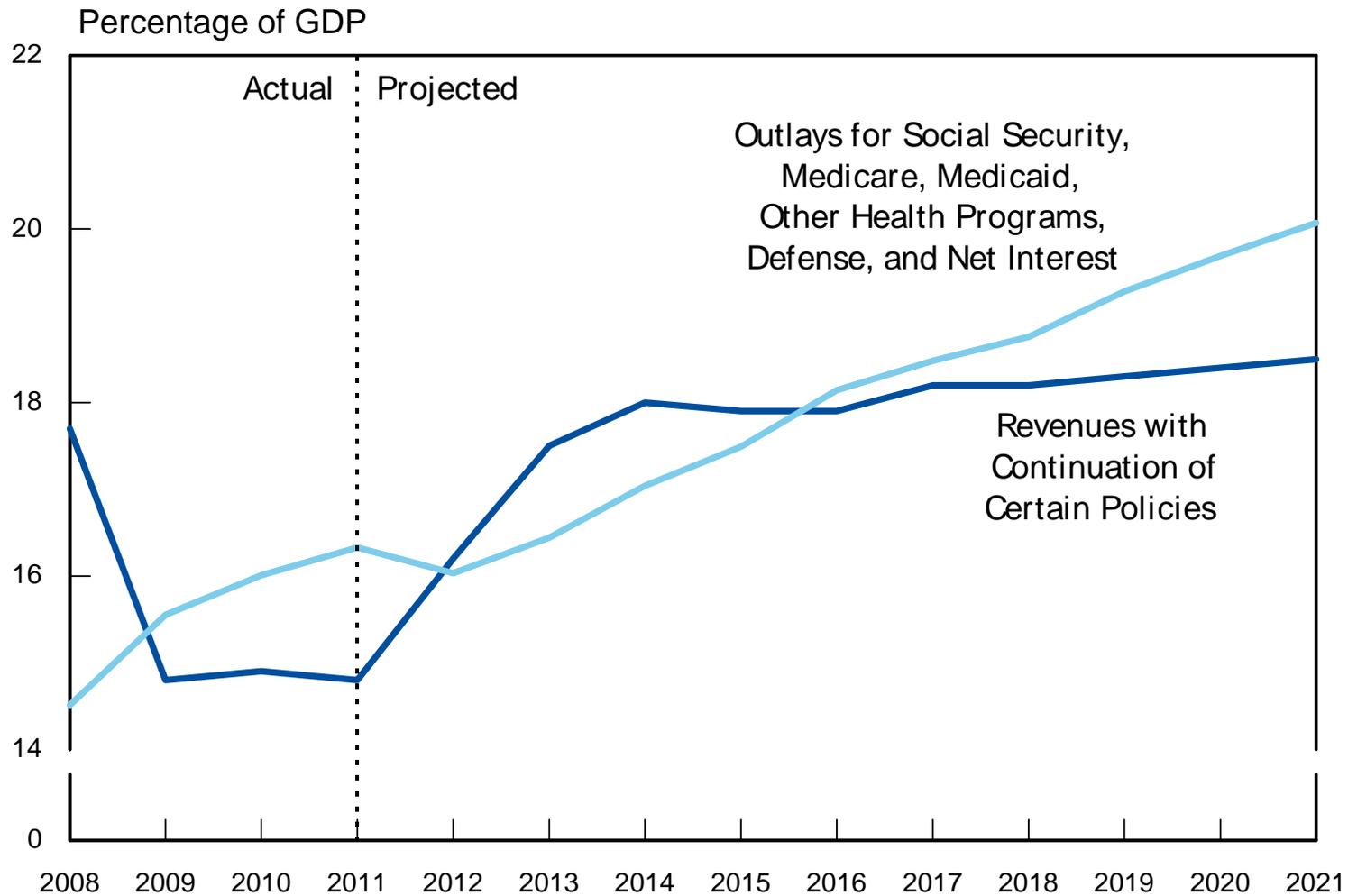
Shares of Federal Spending in 2010

	Percent
Transfer payments to people in the United States	47
Grants to state and local governments	14
Purchases of goods and services for defense	19
Purchases of goods and services for nondefense	9
Interest	8
Other (includes transfers to people outside the U.S.)	4

Source: National Income and Product Accounts.

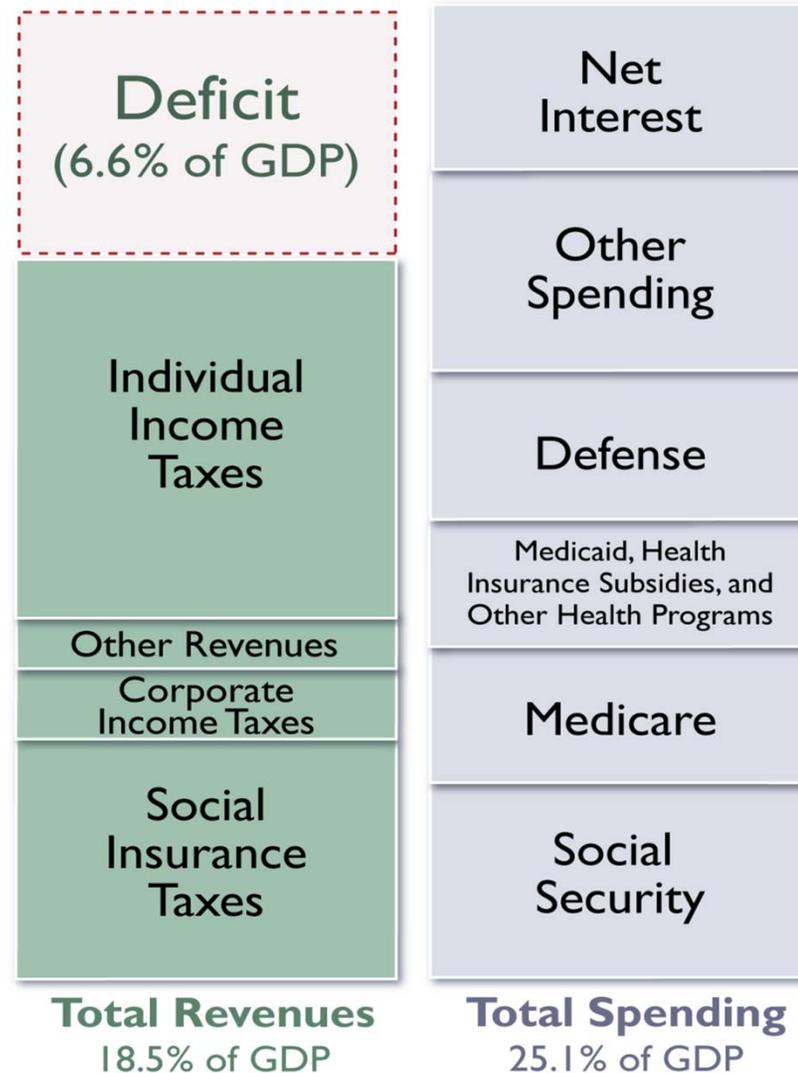


Outlays for Some Major Federal Programs Compared with Total Federal Revenues





Projected Federal Revenues and Spending in 2021 with a Continuation of Certain Policies





Components of the Federal Budget

	1970	2007	2021 January Baseline
	Percentage of GDP		
Revenues	19.0	18.5	20.8
Outlays	19.3	19.6	24.0
<i>Social Security, Medicare, Medicaid, health insurance subsidies, and other health programs</i>	3.8	8.2	12.0
<i>Defense</i>	8.1	3.9	3.6
<i>Other mandatory spending and nondefense discretionary spending</i>	6.0	5.8	5.0
<i>Net interest</i>	1.4	1.7	3.3
Deficit	0.3	1.2	3.2

Note: Figures are shown net of offsetting receipts where relevant.



Observation #3

Policymakers face difficult tradeoffs in deciding how quickly to implement policy changes that would reduce future budget deficits.



Disadvantages of Reducing Deficits Gradually Rather than Quickly

- Reduces the amount of U.S. savings devoted to productive capital investment.
- Requires greater federal spending on interest payments.
- Gives policymakers less flexibility to respond to unexpected problems.
- Increases the likelihood of a fiscal crisis.



Advantages of Implementing Major Budgetary Changes Gradually

- Possibly helps older generations.
- Minimizes the drag of spending cuts or tax increases on the economic expansion.
- Gives families, business, and state and local governments time to plan and adjust.



Making Decisions Soon About How to Put Fiscal Policy on a Sustainable Path Would Be Beneficial

- Enacting policy changes soon:
 - Would allow for gradual implementation while still limiting further increases in federal debt; and
 - Would probably provide some boost to economic activity by reducing uncertainty and holding down interest rates.



Observation #4

There is more focus in Washington on federal budget problems today than there has been since the late 1990s, and that focus has led to a range of proposals for tackling the problems.



Plans to Narrow the Budget Gap

- The plans are *diverse*: They reflect widely varying priorities, with some emphasizing spending cuts and others emphasizing tax increases.
- Yet, they are *similar* in some significant ways. The plans propose policy changes that:
 - Are large in magnitude;
 - Are fairly well-specified; and
 - Would fundamentally alter the tax code and some of the activities of government.