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before the

Subcommittee on Taxation

and Debt Management

Senate Finance Committee

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Mr. Chairman and Members of the Committee, I am pleased to appear before you today to testify on the Treasury's request for an increase in the statutory debt limit. My statement will cover three principal topics:

- The budget estimates for the current fiscal year;
- The implications for the statutory debt limit in the next fiscal year if the 1981 budget is balanced; and
- The effect of off-budget federal lending on the public debt.

Budget Estimates for Fiscal Year 1980

The second concurrent resolution for fiscal year 1980 approved by the Congress last November specified revenues of $517.8 billion, outlays of $547.6 billion, and a deficit of $29.8 billion. The appropriate level of the public debt for the fiscal year was estimated to be $886.4 billion.

Since then it has become apparent--on the basis of our latest economic forecast, actual spending through February, and the Administration's March budget estimates--that 1980 outlays will be significantly higher than specified in the second resolution. On March 3, CBO informed the Chairman of the Senate Budget Committee that our current estimates of outlays from actions already completed by the Congress would exceed the second resolution outlay ceiling by $10 billion. The effect of these new spending estimates has been essentially to halt Congressional action on various supplemental appropriations requested by the Administration until the second resolution spending ceilings can be revised.

The increased estimates of outlays did not result from Congressional action. They stem from such causes as higher interest costs, higher rates of inflation, higher farm price supports resulting largely from the grain embargo announced in January, lower asset sales of federally held mortgages and loans, and faster spending rates for defense procurement and several federal grant programs.

On March 5, at the request of the Budget Committees, CBO issued a revised economic forecast for 1980 and 1981 to take account of the recent acceleration in inflation and other developments. The new forecast for 1980 projected higher inflation, attributable partly to higher interest rates, and slightly lower unemployment rates than our January forecast. The details of this revised forecast are described in my testimony before the Senate Budget Committee, which is attached to my statement for your information. On the basis of this revised economic forecast, we estimate that outlays in 1980 that would result from actions already completed by the Congress would total $560.8 billion, or $13 billion above the second resolution ceiling. The principal reason for the $3 billion further increase in estimated outlays since March 3 is higher interest costs.

The Administration has proposed a number of supplemental appropriations for fiscal year 1980, the largest of which are for defense, food stamps, and energy programs. The Administration's latest estimate for 1980 outlays, as of March 31, is $568.9 billion. The House Budget Committee has recommended that the second resolution outlay ceiling be raised to $567 billion. The Senate Budget Committee has recommended a revised ceiling of $566.4 billion. Actual spending through February, was $234 billion, or almost 16 percent above the level of outlays for the first five months of fiscal year 1979. If this rate were to continue for the remainder of this fiscal year, 1980 outlays could be as high as $571 billion. Thus, the likely level for 1980 outlays at this point appears to be in the range of $566 to $571 billion.

Revenues for 1980 are also expected to be higher than the second resolution estimate, largely due to the higher forecast for inflation and the new oil import fee imposed this month by the President. Our current estimate of 1980 revenues, including those from the windfall profits tax, is $529 billion. This implies a 1980 deficit of $37 to $42 billion, which is $7 to $12 billion above the second resolution level.

The Debt Ceiling for 1980

The temporary limit on the public debt, scheduled to expire on May 31, 1980, is $879 billion. The House Budget Committee recommends that the temporary limit be raised to $897 billion for fiscal year 1980, an increase of $18 billion. The Senate Budget Committee's recommendation is $895 billion. The Budget Committee's recommended limits for 1980 are somewhat higher than that proposed by the Administration, largely because of different assumptions about end-of-year cash balances, means of financing, and other adjustments.

The Budget Outlook for 1981

The Administration and the Congress are in agreement that the 1981 budget should be balanced in order to help curb inflationary pressures. The President submitted a revised budget to the Congress on March 31 that shows a surplus of $16.5 billion. The House Budget Committee has reported a first budget resolution for 1981 that shows a $2 billion surplus. On March 25, the Senate passed S. Res. 380, expressing the sense of the Senate that the Committee on the Budget should report a balanced budget for the first resolution, and reserve any surplus for a tax reduction. The Senate Budget Committee has complied with this policy in its 1981 budget recommendations.

Balancing the budget in 1981 will not be easy. It will require taking a number of difficult steps to restrain the growth in federal spending. Many of these steps will demand changes in basic law relating to benefit payments, and grants to state and local governments. The Appropriations Committees will not be able to accomplish the necessary spending reductions by themselves; other committees will have to play a major role in achieving budgetary savings.

The Debt Ceiling for 1981

Even if the budget is balanced in 1981, the temporary limit on the public debt will have to be increased again by at least $30 billion. This will be necessary in order to accommodate the investment of trust fund surpluses in federal securities and the deficit of off-budget federal entities.

We currently estimate that the trust fund surpluses in 1981 will be on the order of $13 to $14 billion. The largest surpluses will be for the civil service retirement and disability trust fund ($9.3 billion), the federal health insurance trust funds ($6.9 billion), and the federal disability insurance trust fund ($3.1 billion). The old-age and survivors insurance trust fund is projected to have a deficit of about $10 billion in 1981.

The deficit of off-budget entities is estimated at about $18 to $19 billion in 1981. Most of this deficit--90 percent, in fact--is attributable to the credit activities of the Federal Financing Bank (FFB). CBO has recommended that the budget activities of all off-budget entities be brought into the budget so that the unified budget will fully reflect federal government spending. We also favor changing the budgetary recording of agency transactions with the Federal Financing Bank so that those transactions are reflected in the agency budgets.

Federal Credit Activities

The Administration has undertaken to provide an explicit program budget for federal credit activities. Its proposed credit program control system, contained in the January budget, is an important first step toward greater control over the growth of federal credit activities.

Federal credit programs have been controlled to some extent through the normal budget process. For example, the budget authority and outlays for most direct loans of the federal government are included in the unified budget, net of loan repayments. Also, limitations of various kinds have been placed on some loan guarantee programs.

But the volume of new direct loans by off-budget federal entities such as the FFB grew by 70 percent between 1976 and 1979, or twice the rate of growth in total budget outlays. New loan guarantees grew even faster during the same period--by 108 percent. Loan guarantees can often be used as a substitute for on-budget direct lending to escape normal budget controls. In fact, many federally guaranteed loans are converted to off-budget direct loans when they are financed through the FFB. In the January budget, the Administration estimated that $10.9 billion of guaranteed loans will be converted in this manner in 1981.

The Congress currently exercises no control over the timing or amount of off-budget financing by the FFB. But the Congress cannot escape the consequences of it. The ceiling on the public debt must be increased dollar-for-dollar for FFB's net lending. Even if the Congress balances the unified budget for 1981, the public debt ceiling will continue to increase if the FFB continues to act as an off-budget lender. Moreover, Congressional efforts at increased budgetary restraint, including possible spending limitations, could have the effect of encouraging more off-budget transactions, particularly loan guarantees, as a way of escaping limitations on direct spending.

The Budget Committees have made a first step toward exercising greater control over federal credit activities by including targets for new obligations for direct loans and new commitments for loan guarantees in the first budget resolution for 1981. Further actions will probably have to be taken to tighten Congressional control over both the spending budget and the credit budget; two possibilities are changing the budgetary treatment of FFB activities so that they are reflected in agency budgets, and bringing off-budget entities into the unified budget.

By taking these steps, the Congress can begin to control in advance the increase in the public debt limitation required to cover the credit activities of off-budget entities. Otherwise, it is in the position of simply ratifying these credit activities through the debt limit process. We believe the Congress should determine explicitly through a credit budget and other means how much of the nation's credit resources are to be allocated through federal credit programs, and how the relative shares of federal credit are to be distributed among competing needs.