



CBO's Analysis of the President's FY 2012 Budget March 18, 2011

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Today, the Congressional Budget Office (CBO) released its preliminary analysis of President Obama's FY 2012 budget request, which estimates that the President's budget will fall far short of the Administration's own goal of balancing the non-interest budget by 2015 and stabilizing the debt as a share of the economy. Whereas the President's budget had projected deficits would fall to around 3 percent of GDP and debt would stabilize below 77 percent, CBO estimates deficits will reach 4.9 percent of GDP in 2021, and debt will continue to rise to above 87 percent.

This analysis reaffirms our previous concerns that the President's budget does not go far enough to stabilize the debt, and reinforces the fact that doing so will require looking beyond non-security discretionary spending.

Through 2021, CBO estimates deficits of nearly \$9.5 trillion as compared to the \$7.2 trillion estimated by OMB. The difference stems primarily from two sources. First, OMB relies on more optimistic economic and technical assumptions, resulting in nearly \$1.3 trillion less in baseline deficits. Secondly, OMB's estimates incorporate \$777 billion (including interest) in unspecified savings to offset several years of "doc fixes" and finance transportation spending. The remaining difference stems from different estimates of various policies.

Fig. 1: Factors explaining different deficit levels (billions)

	2012-2021
Deficits in President's Budget (OMB)	\$7,202
Different Economic and Technical Assumptions in Baseline*	\$1,272
Exclusions of Unspecified Offsets in Budget	\$777
Different Cost Estimates of Policy Proposals	\$219
Deficits in President's Budget (CBO)	\$9,470

*This also incorporates a small amount of legislative changes in the baseline.

This analysis reinforces the importance of comprehensive reform which addresses not only domestic discretionary spending, but also tackles defense spending, slows the growth in entitlement spending, and reforms the tax code. Failure to address all areas of the budget will make it nearly impossible to bring our medium and long-term fiscal situation under control.

Budget Projections

Under CBO's estimate of the President's budget, deficits would reach \$1.4 trillion (9.5 percent of GDP) in 2011 and \$1.1 trillion (7.4 percent of GDP) in 2012. By 2015, deficits would fall to a low of 4.1 percent of GDP – as the economy recovers, rescue measures wind down, and some of the President's deficit reduction policies phase in – but will rise again thereafter, reaching 4.9 percent of GDP by 2021. These estimates are considerably higher than OMB's, which show deficits holding fairly constant at around 3 percent of GDP for the latter half of the decade.

Spending under CBO's estimates will never fall below 23 percent of GDP, and will exceed 24 percent by the end of the budget window. This is nearly 1 percent of GDP higher than OMB's estimates, and substantially above historical averages of less than 21 percent of GDP. Revenues, meanwhile, are projected to rise from 14.8 percent of GDP this year to 19 percent by 2016 and 19.3 percent by 2021. This would put revenues modestly above historical averages (just over 18 percent of GDP), but somewhat below OMB's estimates of 20 percent of GDP by 2021.

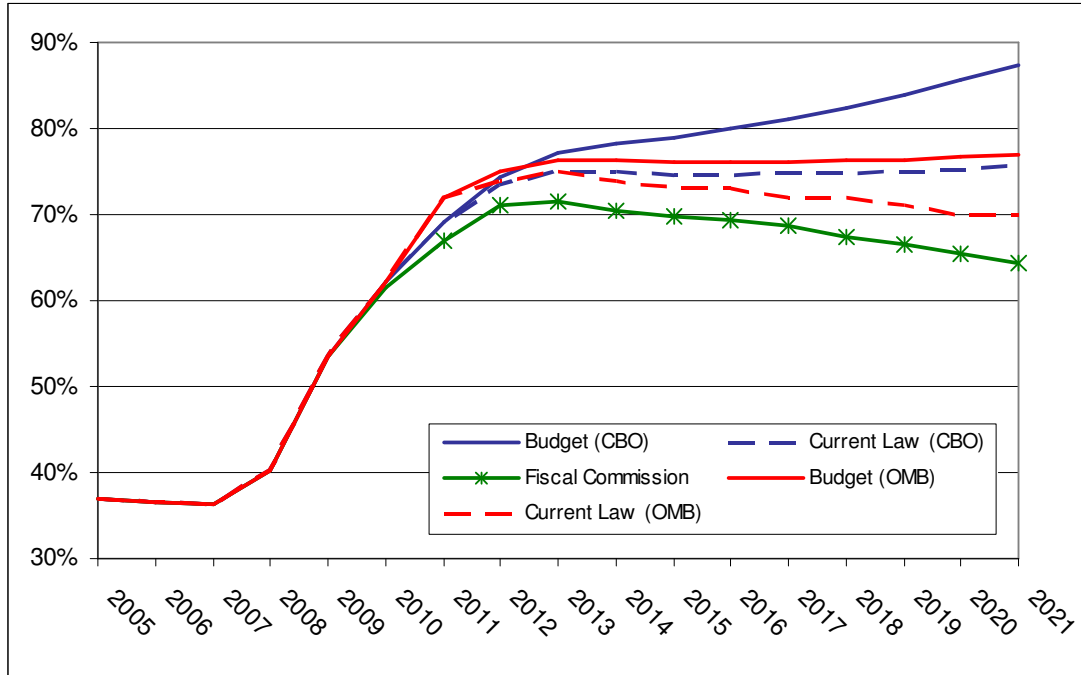
Fig. 2: Differences in Projections for the President's Budget Proposal (Billions)

Fiscal Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2012-2021
REVENUE												
2012 Budget (CBO)	14.8%	16.2%	17.7%	18.6%	18.9%	19.0%	19.1%	19.1%	19.2%	19.2%	19.3%	18.7%
2012 Budget (OMB)	14.4%	16.6%	17.9%	18.7%	19.1%	19.3%	19.5%	19.6%	19.8%	19.9%	20.0%	19.0%
Baseline (CBO)	14.8%	16.3%	18.8%	19.9%	20.1%	20.0%	20.3%	20.4%	20.5%	20.7%	20.8%	19.9%
Baseline (BEA)	14.4%	16.7%	18.7%	20.0%	20.0%	20.1%	20.5%	20.7%	21.0%	21.1%	21.3%	20.0%
OUTLAYS												
2012 Budget (CBO)	24.3%	23.6%	23.2%	23.0%	23.0%	23.4%	23.4%	23.4%	23.8%	24.0%	24.2%	23.5%
2012 Budget (OMB)	25.3%	23.6%	22.5%	22.4%	22.3%	22.6%	22.5%	22.5%	22.8%	23.0%	23.1%	22.7%
Baseline (CBO)	24.7%	23.3%	23.1%	23.0%	23.1%	23.5%	23.4%	23.3%	23.7%	23.9%	24.0%	23.5%
Baseline (BEA)	25.0%	23.3%	22.6%	22.6%	22.6%	22.8%	22.7%	22.7%	22.9%	23.1%	23.3%	22.9%
DEFICITS (Percent of GDP)												
2012 Budget (CBO)	9.5%	7.4%	5.5%	4.4%	4.1%	4.4%	4.3%	4.3%	4.7%	4.8%	4.9%	4.8%
2012 Budget (OMB)	10.9%	7.0%	4.6%	3.6%	3.2%	3.3%	3.0%	2.9%	3.0%	3.1%	3.1%	3.7%
Baseline (CBO)	9.8%	7.0%	4.3%	3.1%	3.0%	3.4%	3.1%	2.9%	3.2%	3.2%	3.2%	3.6%
Baseline (BEA)	10.6%	6.6%	3.8%	2.6%	2.6%	2.8%	2.2%	1.9%	1.9%	2.0%	2.0%	2.8%
Deficits (\$ billions)												
2012 Budget (CBO)	\$1,399	\$1,081	\$692	\$513	\$538	\$635	\$590	\$585	\$665	\$710	\$729	\$6,737
2012 Budget (OMB)	\$1,645	\$1,101	\$768	\$645	\$607	\$649	\$627	\$619	\$681	\$735	\$774	\$7,205
Baseline (CBO)	\$1,480	\$1,100	\$704	\$533	\$551	\$659	\$617	\$610	\$696	\$739	\$763	\$6,971
Baseline (BEA)	\$1,593	\$1,036	\$643	\$463	\$496	\$552	\$460	\$417	\$438	\$472	\$488	\$5,465

With spending at high and growing levels and revenues failing to keep up, the President's budget is expected to cause the national debt to expand substantially. Under CBO's estimate, the debt will grow from about 69 percent of GDP at the end of 2011 (and only 36 percent back in 2007), to nearly 80 percent of GDP in 2016 and over 87 percent by 2021.

These projections are substantially worse than OMB's estimate that debt will stabilize at below 77 percent through the decade, and if allowed to occur would bring the debt to potentially dangerous levels. Stabilizing the debt as a share of the economy should be considered the absolute minimum of what we must do. It would be far more preferable to reduce the debt-to-GDP levels to below 60 percent.

Fig. 3: Debt Held by the Public (Percent of GDP)



Policy Changes

Relative to current law, CBO projects that the President's budget will add \$2.7 trillion to the deficit, compared to \$1.7 trillion estimated by OMB. Among the most costly proposals are an extension of the 2001/03/10 tax cuts for those making under \$250,000 and continued AMT patches (\$3,102 billion over ten years), continued doc fixes (\$298 billion), new spending on transportation (\$213 billion), the continuation of the American Opportunity Tax Credit for college students (\$90 billion), and the permanent extension of the R & E tax credit (\$88 billion).

Among the largest deficit-reducing policies includes a limitation on the size of itemized deductions for higher earners (\$293 billion), reforms to the international tax system (\$133 billion), and a variety of measures to reduce health care spending (\$48 billion). The President's non-security discretionary freeze and the assumption that war spending will cost \$50 billion a year also contribute to deficit reduction, leading to about \$948 billion less in discretionary spending.

Fig. 4: Ten Year Deficit Impact of Policy Changes in the President's Budget

	OMB	CBO
Current Law Deficit	\$5,465	\$6,737
Extend 2001/2003/2010 Tax Cuts for Income below \$250,000 and Continue AMT Patches*	\$3,194	\$3,102
Extend the American Opportunity Tax Credit	\$94	\$90
Extend Research & Experimentation Credit	\$106	\$88
Other Tax Cuts for Individuals and Businesses	\$73	\$89
Limit Itemized Deductions to Pay for 3-year AMT Patch	(\$321)	(\$293)
Financial and Energy Taxes	(\$100)	(\$94)
Reform U.S. international tax system	(\$129)	(\$133)
Reform Unemployment Taxes	(\$61)	(\$47)
Other Tax Changes	(\$161)	(\$82)
Sub-Total, Tax Changes	\$2,695	\$2,720
Spending Proposals		
Enact Doc Fixes	\$370	\$298
Specified Health Spending Reductions	(\$62)	(\$48)
Reduce Fraud and Abuse (Program Integrity Measures)	(\$69)	(\$22)
Discretionary Changes (Includes \$50 Billion War Spending Plug)	(\$1,190)	(\$948)
Increase Transportation Spending~	\$241	\$213
Other Spending Changes	\$86	\$1
Sub-Total, Spending	(\$624)	(\$506)
Unspecified Deficit Reduction		
Unspecified Measures to Offset Doc Fixes	(\$315)	n/a
Unspecified Measures to Fully Finance Transportation Spending	(\$328)	n/a
Sub-Total, Unspecified	(\$643)	Not Counted#
Net Interest Changes	\$311	\$519
Change in Deficit	\$1,739	\$2,733
Deficit under President's Budget	\$7,205	\$9,470

*Includes taxation of capital gains and dividends at a 20% rate on income above \$250,000 a year.

~Includes Pell Grant adjustments and baseline transportation funding.

#CBO does not score these changes since they lack specificity.

The \$1 trillion difference between CBO's and OMB's deficit reduction estimates is largely the result of the so-called "magic asterisks" in the President's budget. The President's budget assumes doc fixes will be fully offset without identifying these offsets beyond the first two years, and that unspecified "bipartisan financing" will be available to pay for existing and new transportation spending. Including interest, we estimate these measures total around \$777 billion. OMB and CBO are also working off of different discretionary baselines, resulting in less "savings" for the President's discretionary path.

In addition, the two scoring agencies have different estimates (and in some cases classifications) for a large number of policy proposals.

Conclusion

Unfortunately – but not unsurprisingly – CBO’s estimate of the President’s budget shows that we are on a dangerous fiscal path, even if we enact the deficit-reducing policies proposed in the budget. This demonstrates, quite clearly, that the debt cannot be stabilized by simply freezing non-security discretionary spending and identifying a few opportunities to raise revenue and reduce spending in a relatively painless way.

Real fiscal reforms will require looking at all areas of the budget – reducing defense spending and cutting tax expenditures, but most importantly addressing the long-term growth of Social Security, Medicare, and Medicaid. Though the President’s budget takes some important steps to reduce spending, it fails to truly tackle any of these areas.

In the coming weeks and months, the President has an opportunity to take on these tough issues in a meaningful way. Today, a bipartisan group of 64 Senators sent President Obama a letter encouraging him to do just that. The President should heed this call and work with Members of both parties to bring the debt under control. The nation’s future depends on it.