COMMITTEE FOR A RESPONSIBLE FEDERAL BUDGET

CBO's Long-Term Budget Outlook
June 22, 2011

Today, the Congressional Budget Office (CBO) released its Long-Term Budget Outlook, which yet again illustrates this country's unsustainable fiscal trajectory. Under the Extended-Baseline Scenario, CBO projects debt to rise from 69 percent of GDP today to 75 percent by 2020 and 84 percent by 2035. Under the Alternative Fiscal Scenario, which makes more realistic assumptions about which policies lawmakers might extend, CBO projects debt to grow to 97 percent by 2020, 187 percent by 2035, and then to spiral out of control thereafter.

Compared to last year, both projections have worsened somewhat through 2035, but the debt situation has improved over the longer-term due in part to lower projections of health care spending. The levels of debt projected in the alternative scenario are completely unsustainable, and the projections under current law will almost certainly prove to be wildly optimistic. Both highlight the need for a comprehensive deficit reduction plan that not only stabilizes and reduces the debt over the medium-term, but reforms the way we tax and spend and addresses the long-term drivers of debt – health care and retirement spending.

The Committee for a Responsible Federal Budget believes that these chilling projections should be a cold shower on any plans to delay enacting a comprehensive plan to address the debt. And this wakeup call should erase any thoughts of waiting until after the election—or worse, until markets force our hand—to make the needed changes to the budget.

Fig. 1: Fiscal Projections under CBO's Two Scenarios (Percent of GDP)

	2000	2011	2020	2035	2050
Extended Baseline					
Spending	18.2%	24.1%	23.7%	27.4%	29.4%
Revenue	20.6%	14.8%	20.6%	23.2%	26.1%
Deficit	-2.4%	9.3%	3.1%	4.2%	3.3%
Debt	35%	69%	75%	84%	85%
Alternative Fiscal Scenario					
Spending	18.2%	24.1%	25.5%	33.9%	42.8%
Revenue	20.6%	14.8%	18.3%	18.4%	18.4%
Deficit	-2.4%	9.3%	7.2%	15.5%	24.4%
Debt	35%	69%	97%	187%	330%*

*CRFB Estimate

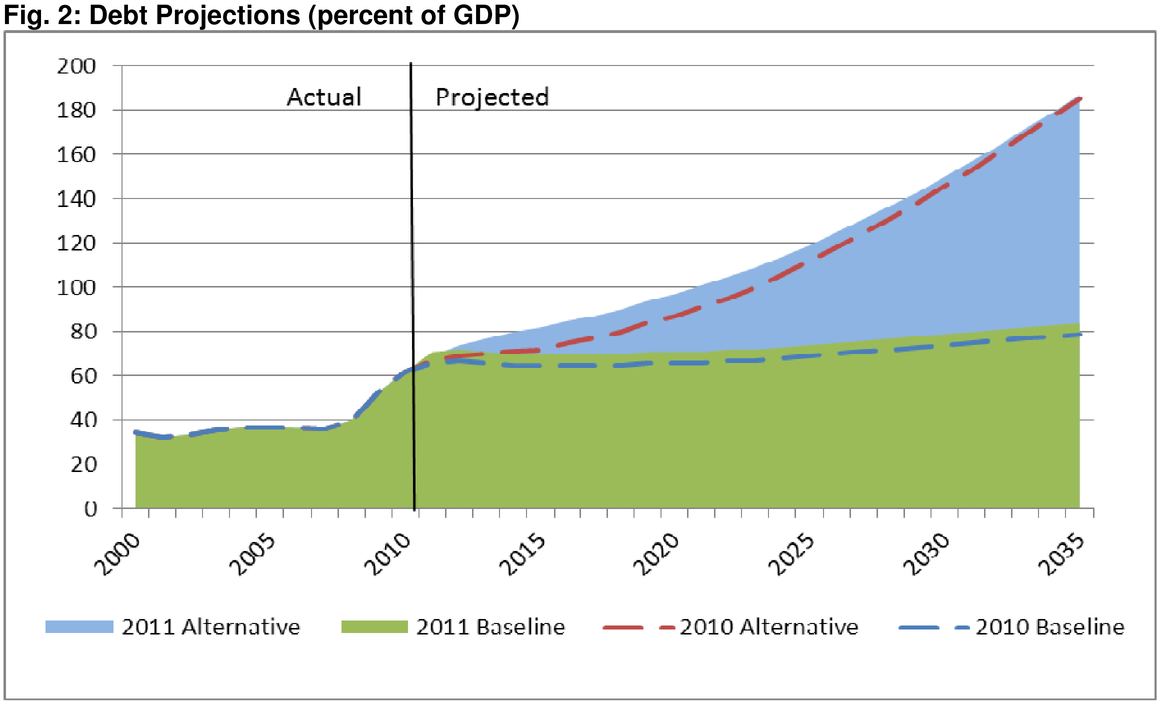
The Long-Term Debt Outlook

In its Long-Term Outlook, CBO makes two separate sets of projections. Under its Extended-Baseline Scenario, CBO assumes the permanent continuation of current law, including the expiration of all the 2001/2003/2010 tax cuts, a 30 percent cut in physician payments as a result of not passing "doc fixes," and the discontinuation of "AMT patches". In this scenario, CBO also assumes that the health reform law (PPACA) is quite successful in controlling costs beyond 2021, despite questions over the sustainability of some of its policies.

The Alternative Fiscal Scenario makes more realistic policy assumptions in the short-run – instead assuming that nearly all of the 2001/2003/2010 tax cuts are continued and AMT patches and "doc fixes" continue to be enacted as they have been in the past. Under this scenario, CBO also assumes discretionary spending will grow at the rate of the economy, revenues will be steady at 18.4 percent of GDP after 2021, and the cost controls under PPACA will be less successful in controlling cost growth beyond 2021.

Both scenarios show the U.S. to be on a troubling fiscal path. Under the baseline scenario, debt would grow to nearly 90 percent of the economy and would only come down over the long-run as a result of assumed unrealistically high levels of taxation. Under the Alternative Fiscal Scenario, debt would breach 100 percent of the economy in 2021, exceed 200 percent by 2037, and continue growing thereafter–ultimately becoming so high that CBO stops making debt projections beyond 2036.

Fig. 2: Debt Projections (percent of GDP)



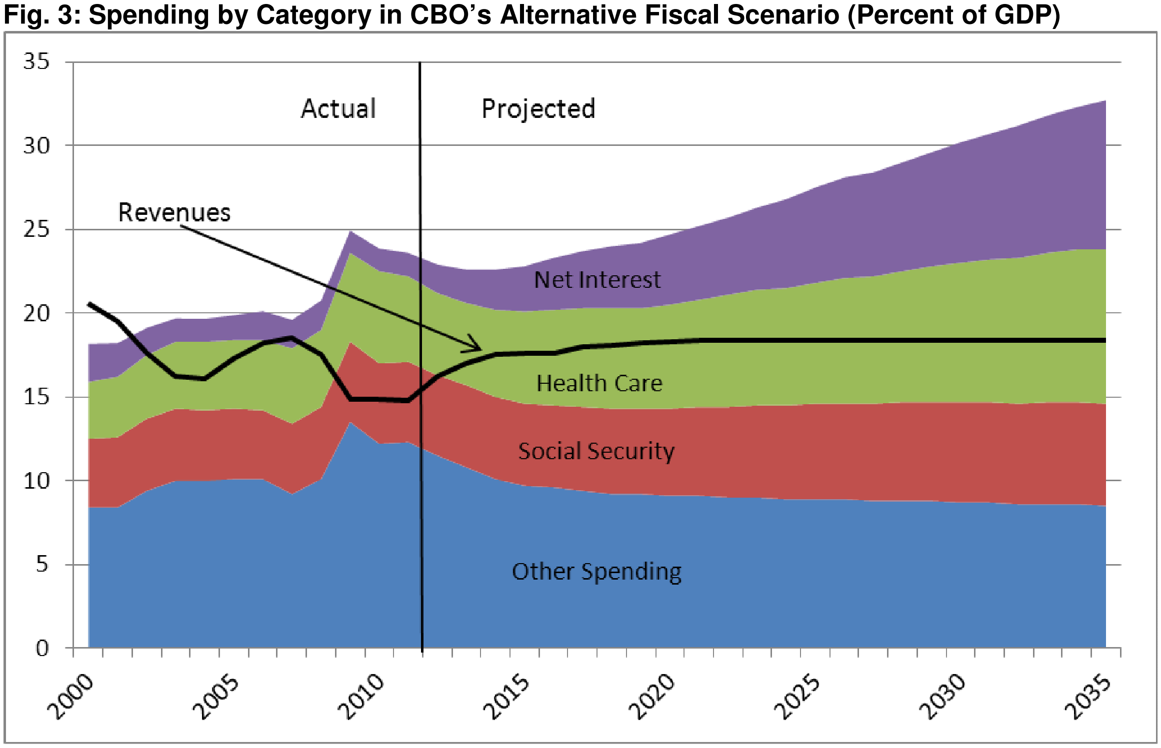
Deficits, Spending, and Revenues

Driving the mounting federal debt between now and 2035 is a growing projected imbalance between spending and revenues. Under the Alternative Fiscal Scenario, CBO projects deficits to bottom out at 5.6 percent of GDP in 2014 before rising to 7.2 percent in 2020 and to 15.5 percent by 2035.

This growing imbalance is primarily fueled by growing levels of spending, which under both scenarios will far exceed their historical averages of below 21 percent of GDP – reaching 23.2 percent and 33.9 percent of GDP by 2035 in the Extended-Baseline Scenario and Alternative Fiscal Scenario, respectively.

This growth will come primarily from increases in entitlement spending—notably Medicare, Medicaid, the exchange subsidies, and Social Security – as well as from higher interest costs resulting from growing levels of debt. Under the Alternative Fiscal Scenario, health spending (net of premiums) will grow from 5.1 percent of GDP today to 6.2 percent in 2020 and 9.2 percent in 2035. Social Security will grow from 4.8 percent of GDP this year to 6.1 in 2035. Interest costs, meanwhile, will rise to 8.9 percent of GDP by 2035, up from only 1.4 percent this year.

Fig. 3: Spending by Category in CBO's Alternative Fiscal Scenario (Percent of GDP)



As with the Alternative Fiscal Scenario, entitlement spending grows substantially under the Extended-Baseline Scenario. Social Security still grows to 6.1 percent of GDP in 2035, and health care spending grows to 8.5 percent of GDP – not as big as the 9.2 percent under the Alternative Fiscal Scenario, but still much higher than the 5.1 percent we are currently spending.

Unlike the Alternative Fiscal Scenario, however, the Extended-Baseline Scenario holds deficits down to the 3 to 4 percent of GDP range, largely due to rapidly growing revenue levels. Not only does this scenario assume that all the 2001/2003/2010 tax cuts expire – something neither political party supports – but it also assumes we discontinue the practice of "patching" the AMT, which means that it will hit about half of all households by 2035, as opposed to 2.6 percent today. As a result, under that scenario, total revenues will eclipse their average of 18.1 percent of GDP by 2013 and their post-war historical record of 20.6 percent of GDP by 2020; revenues will reach 23 percent of GDP by 2035, and actually continue to grow to 30 percent by 2080.

Even under this scenario – where revenues reach unheard of levels – deficits persist, health care spending continues to grow, and the budget does not reach balance.

Conclusion

The country's long-term fiscal health is in danger. Debt is projected to surpass the size of the economy in only 10 years, under reasonable assumptions, and be twice the size of the economy by 2037. No reasonable person can view this scenario as sustainable, and CBO certainly does not.

Currently, policymakers are working together to enact a large deficit reduction package – and this report should help to show just how big the final package must be. In total, policymakers must aim to reduce the deficit by at least $4 to $5 trillion over the next decade in order to put the debt on a downward path. This package should look at all areas of the budget, including defense, domestic discretionary spending, and the tax code. More importantly, however, they must make meaningful reforms to slow the growth of entitlement spending over the medium and long-run. Dealing with these programs is the only way to truly bring our fiscal situation under control.