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**Review of the Final Monthly Treasury
Statement for Fiscal Year 2009
October 20, 2009**

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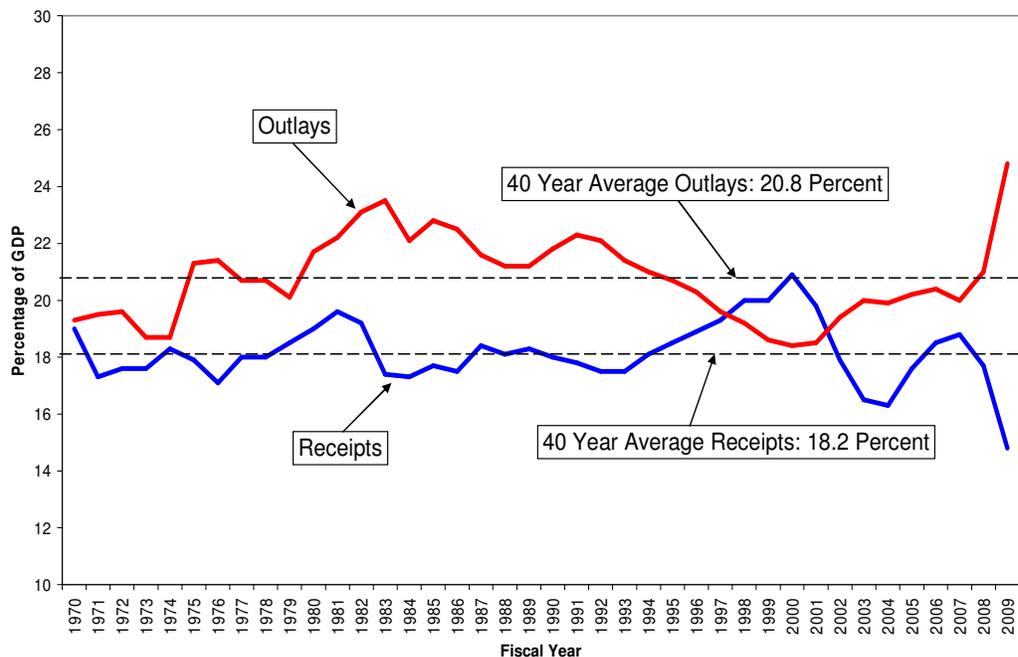
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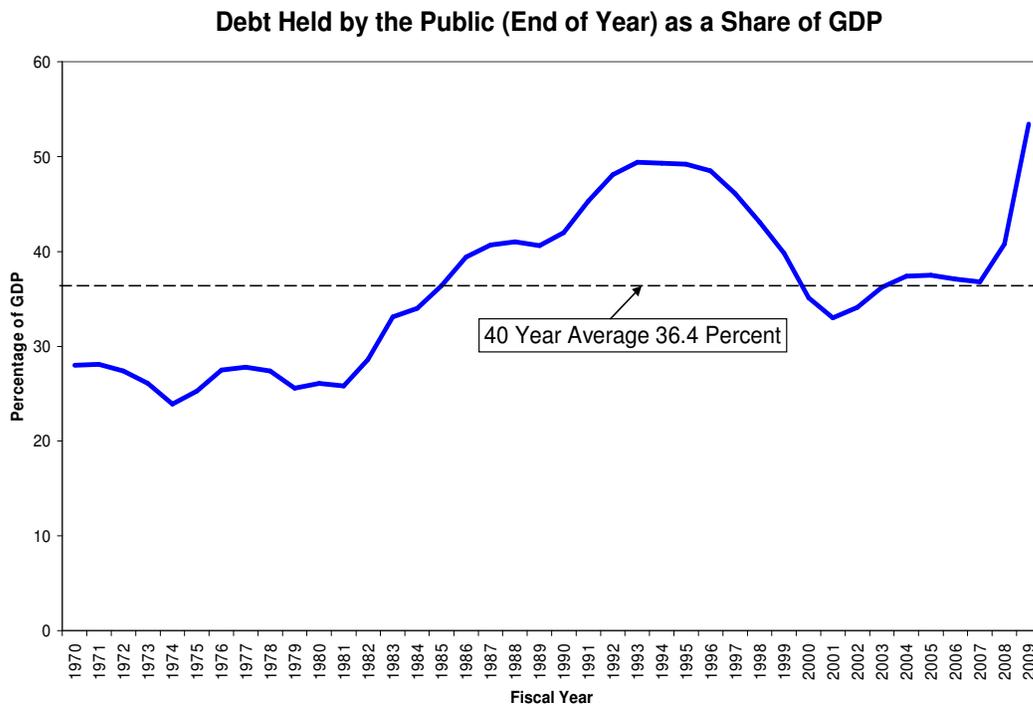
The Treasury Department and Office of Management and Budget released the official budget results for Fiscal Year 2009. Highlights from the release include:

- The deficit was a record \$1.417 trillion, or 10 percent of gross domestic product (GDP). This figure is very close to the Congressional Budget Office's (CBO) August estimate of \$1.409 trillion, but somewhat below the Office of Management and Budget's (OMB) midsession estimate of \$1.580 trillion. Receipts totaled \$2.105 trillion (14.8 percent of GDP) while outlays totaled \$3.522 trillion (24.8 percent of GDP).

Total Receipts and Outlays as a Share of GDP



- The Troubled Asset Relief Program (TARP) and the American Recovery and Reinvestment Act (ARRA) account for 24 percent, or \$340 billion of the deficit total. The stimulus and economic recovery efforts therefore amounted to about 2.4 percent of GDP in the last fiscal year.
- The U.S. Government ran a deficit in every month of fiscal year 2009. This is unprecedented in the 29 years of data available on the Treasury Department website. In most years the government runs surpluses when quarterly payments of estimated taxes or income tax returns are due.
- Total borrowing from the public increased to \$7.544 trillion. As a share of the economy, debt held by the public reached 53.4 percent.
- The debt as a share of GDP increased by 12.6 percentage points in fiscal year 2009. This is the largest annual change in debt as a share of GDP since fiscal year 1945.



Receipts

Total receipts declined year-over-year for the second consecutive year in 2009. Every major source of tax revenues declined in 2009, leading to a total drop in receipts of \$419 billion, or 16.6 percent, relative to fiscal year 2008. Over the past two years, receipts have fallen by \$463 billion, or 18 percent. Collections for the

individual income tax and the corporation income taxes have declined relative to prior year in both 2008 and 2009.

Receipts by Source

(By fiscal year in millions of dollars)

Source	2009	2008	2009 Relative to 2008		2007	2009 Relative to 2007	
			\$ Change	% Change		\$ Change	% Change
Individual Income Tax	915,308	1,145,748	-230,440	-20.1	1,163,472	-248,164	-21.3
Corporation Income Taxes	138,229	304,346	-166,117	-54.6	370,243	-232,014	-62.7
Social Insurance and Retirement	890,918	900,154	-9,236	-1.0	869,607	21,311	2.5
Excise Taxes	62,484	67,334	-4,850	-7.2	65,069	-2,585	-4.0
Estate and Gift Taxes	23,482	28,844	-5,362	-18.6	26,044	-2,562	-9.8
Customs Duties	22,454	27,568	-5,114	-18.6	26,010	-3,556	-13.7
Miscellaneous Receipts	51,738	49,647	2,091	4.2	47,228	4,510	9.5
Total	2,104,613	2,523,641	-419,028	-16.6	2,567,672	-463,059	-18.0

Outlays

Fiscal year 2009 spending was up by \$543 billion year-over-year. Of that amount, \$154 billion stems from the TARP, \$113 billion is associated with spending authorized in ARRA, and \$96 billion provided assistance to the Fannie Mae and Freddie Mac. Federal outlays grew at an annual rate of 18.2 percent, their fastest clip since 1975.

Almost two-thirds of all agencies saw outlays increase by double digits in fiscal year 2009, while only three saw a year-over-year decline. Somewhat surprisingly, the Department of Education was one of those agencies where net outlays were lower—despite the creation of the new State Fiscal Stabilization Fund in ARRA, which spent \$12.4 billion last fiscal year. The lower spending was the result of increased receipts in the student loan programs from changes in the amounts and composition of student loans.

Some of the large increases in agency spending were related to automatic stabilizers as well as efforts to aid the economy. These increases include:

- Unemployment Trust Fund (Labor) up \$70.5 billion or 151.3 percent;
- Food Stamps (Agriculture) up \$16.3 billion or 41.4 percent; and
- Medicaid (Health and Human Services) up \$49.5 billion or 24.6 percent (this is a result of both the recession and the increased match rate provided in ARRA).

Total Outlays by Agency

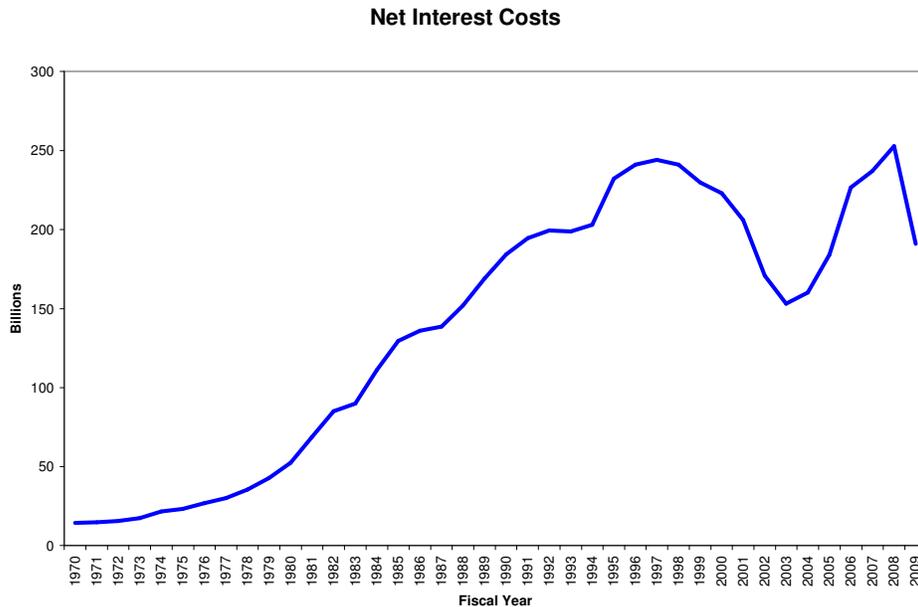
(By fiscal year in millions of dollars)

<u>Agency</u>	<u>2009</u>	<u>2008</u>	<u>\$ Change</u>	<u>% Change</u>
Legislative Branch	4,713	4,429	284	6.4
Judiciary	6,643	6,345	298	4.7
Agriculture	114,436	90,789	23,647	26.0
Commerce	10,721	7,726	2,995	38.8
Defense-Military	636,793	594,680	42,113	7.1
Education	53,387	65,957	-12,570	-19.1
Energy	23,684	21,404	2,280	10.7
Health and Human Services	796,323	700,501	95,822	13.7
Homeland Security	51,721	40,683	11,038	27.1
Housing and Urban Development	61,024	49,086	11,938	24.3
Interior	11,810	9,880	1,930	19.5
Justice	27,713	26,544	1,169	4.4
Labor	138,156	58,840	79,316	134.8
State	21,435	17,506	3,929	22.4
Transportation	73,006	64,945	8,061	12.4
Treasury	703,172	548,819	154,353	28.1
Veterans Affairs	95,490	84,783	10,707	12.6
Corps of Engineers	6,840	5,077	1,763	34.7
Other Defense Civil Programs	57,277	45,784	11,493	25.1
Environmental Protection Agency	8,070	7,938	132	1.7
Executive Office of the President	743	1,172	-429	-36.6
General Services Administration	320	342	-22	-6.4
International Assistance Programs	14,827	11,403	3,424	30.0
NASA	19,168	17,834	1,334	7.5
National Science Foundation	6,005	5,848	157	2.7
Office of Personnel Management	72,302	64,393	7,909	12.3
Small Business Administration	2,246	528	1,718	325.4
Social Security Administration	727,549	657,799	69,750	10.6
Other Independent Agencies	50,361	45,196	5,165	11.4
Undistributed Offsetting Receipts	<u>-274,199</u>	<u>-277,789</u>	<u>3,590</u>	<u>-1.3</u>
Total	3,521,734	2,978,440	543,294	18.2

Debt and Interest

In fiscal year 2009, total borrowing from the public increased by \$1.743 trillion. This amount is \$324 billion larger than the increase in the deficit principally because of the increase in direct loan activity by the federal government in fiscal year 2009. Direct loans are counted in the budget as the present value of the amount estimated not to be repaid. The face value of the loan must be borrowed from the public, however, which drives the debt upward. In 2009, the direct loans for the purchase of mortgage-backed securities added \$171 billion to the debt, and direct loans through the TARP added \$129 billion to the debt.

Even though debt increased by over 30 percent in the past year, net interest on the debt decreased. Outlays for budget function 900 dropped by \$61.9 billion (-24.4 percent) to \$190.9 billion in 2009.



The drop in net interest costs is likely the result of a flight to safety by investors during the 2008 financial crisis; a similar reduction in net interest costs during a time of increasing debt occurred in fiscal years 2002 and 2003 after the 2001 terrorist attacks on the United States. The budget is at risk of higher net interest costs as a result of higher interest rates much as it was earlier in this decade.

This risk is attenuated because a large percentage of the nation's debt is held by people outside of the United States. The Treasury and Federal Reserve Board report that foreign holders owned \$3.449 trillion of Treasury securities as of the end of August 2009 (<http://www.treas.gov/tic/mfh.txt>). That amount is approximately 46 percent of the total borrowing from the public at the end of that month. Foreigners increased their holdings of federal debt by \$649.3 billion in the first 11 months of fiscal year 2009, absorbing 38.8 percent of the total increase in borrowing from the public. The balance of the increase was absorbed from within the United States, including the purchase of Treasury securities by the Federal Reserve.

Foreign holders face both currency risk and interest rate risk in their holdings of Treasury securities. To the extent that they perceive that they might be paid back in dollars that are worth less than the dollars that were used to purchase the

securities, they may demand a higher interest rate. The United States has been fortunate that some of its trading partners—China, the United Kingdom, Hong Kong and Switzerland—have chosen to increase disproportionately their share of total Treasury securities owned by foreigners.

**Change in Holdings of Treasury Securities by Major Foreign Holders
First 11 Months of Fiscal Year 2009**

(Holdings at End of Month, in Billions of Dollars)

<u>Country</u>	<u>August</u> <u>2009</u>	<u>Share</u> <u>of</u> <u>Total</u> <u>(%)</u>	<u>September</u> <u>2008</u>	<u>Share</u> <u>of</u> <u>Total</u> <u>(%)</u>	<u>\$ Increase</u>	<u>Share of</u> <u>Increase</u> <u>%</u>
China	797.1	23.1	618.2	22.1	178.9	27.6
Japan	731.0	21.2	617.5	22.1	113.5	17.5
United Kingdom	225.8	6.5	112.8	4.0	113.0	17.4
Oil Exporters	189.2	5.5	171.2	6.1	18.0	2.8
Caribbean Banking Centers	180.2	5.2	169.3	6.0	10.9	1.7
Brazil	137.2	4.0	148.3	5.3	-11.1	-1.7
Hong Kong	124.7	3.6	65.5	2.3	59.2	9.1
Russia	121.6	3.5	99.6	3.6	22.0	3.4
Luxembourg	94.2	2.7	104.5	3.7	-10.3	-1.6
Taiwan	75.9	2.2	63.0	2.3	12.9	2.0
Switzerland	68.2	2.0	49.7	1.8	18.5	2.8
All Other	<u>703.6</u>	<u>20.4</u>	<u>579.9</u>	<u>20.7</u>	<u>123.7</u>	<u>19.1</u>
Total	3,448.8	100.0	2,799.5	100.0	649.3	100.0

Some of those trading partners have recently voiced concerns about the value of the dollar and the safety of Treasury securities as a store of value. They worry continued large deficits could lead to the monetization of the debt, reducing the value of the dollar and the purchasing power of their investments.

The Fiscal Year 2011 budget process must go beyond merely “considering proposals to put our country back on a firm fiscal footing,” as OMB Director Orszag stated in last Friday’s release. It is important that the President lead on this issue rather than leaving the work to Congress to bring deficits “down to a sustainable level as the economy recovers,” to use Secretary Geithner’s words.

If deficits are not brought under control soon, bondholders will demand higher interest rates. This in turn will raise debt service costs, further increasing deficits and debt, and creating a downward fiscal spiral that will only end with jarring changes in fiscal policy. This might be prevented with timely action. Hopefully the release of the fiscal year 2009 budget results provides the wake-up call that policymakers need to get the Nation’s fiscal house in order.