COMMITTEE FOR A RESPONSIBLE FEDERAL BUDGET

CBO's Analysis of the President's FY 2016 Budget

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Today, the Congressional Budget Office (CBO) released its re-estimate of the President's FY 2016 budget, using its own economic and technical assumptions. While CBO generally shows lower debt in the near term than the Office of Management and Budget (OMB) did, it also shows debt on a slight upward path as a share of GDP after 2020. Thus, it is less likely that the budget would stabilize debt over the long term, as OMB's projections showed.

According to CBO, debt held by the public in the President's budget would reach 73.1 percent of GDP by 2025, 1 percentage point lower than in 2014 (and about what OMB estimated), but 1 percentage point higher than in 2020. In dollars, debt would rise from about $13.1 trillion today to $20.1 trillion by 2025.

CBO projects debt under the President's budget would be $1.1 trillion lower than in CBO's current law baseline in 2025. Those savings can be mostly attributed to two factors: increased revenue and reductions in war spending that are largely already expected to occur.

CBO projects annual deficits would fall from $486 billion (2.7 percent of GDP) in 2015 to $380 billion (2.0 percent of GDP) in 2016 before rising in every subsequent year to over $800 billion (2.9 percent of GDP) by 2025. Both spending and revenue will be growing as a share of GDP over this period, but spending will increase slightly faster, from 20.5 percent in 2015 to 22.1 percent in 2025, while revenue will rise from 17.8 percent to 19.2 percent. These increases are the result of both current law trends and policy changes proposed in the President's budget.

CBO estimates deficits through 2025 will be $206 billion higher under the President's budget than OMB estimates, with more than the entire difference ($345 billion) coming from differences in economic projections. In the other direction, $139 billion of technical differences reduced deficits relative to what OMB estimated. In addition, using CBO's GDP instead of OMB's results in the 2025 debt-to-GDP ratio being one percentage point higher.

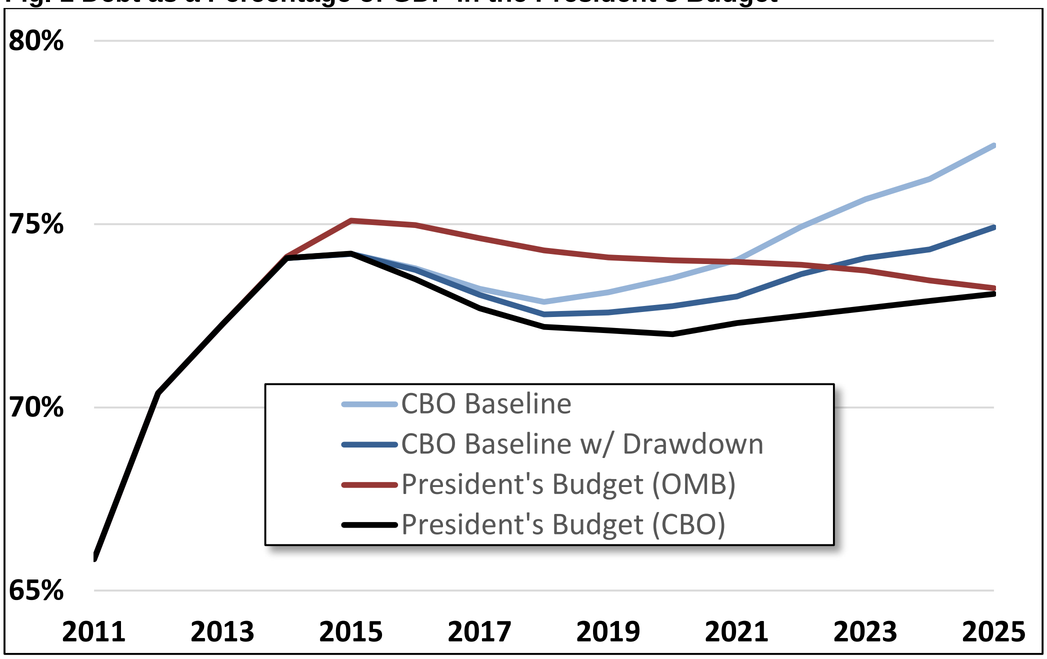
Ultimately, CBO shows that while the President's budget responsibly offsets its new spending, it does not go far enough in reducing the debt to ensure fiscal sustainability over the long term.

Budget Projections

CBO estimates that the President's budget would result in debt falling modestly from 74.1 percent of GDP in 2014 to 72.0 percent by 2020 before rising to 73.1 percent by 2025. In dollar terms, debt would rise from $13.1 trillion today to $20.1 trillion by 2025, a $7 trillion increase.

These numbers are similar in magnitude (but different in their path) to OMB's estimate, which shows debt rising to $13.5 trillion in 2015 to $20.4 trillion, or 73.3 percent of GDP, by 2025. They also represent an improvement over CBO's current law baseline, which has debt rising to $21.2 trillion or 77.1 percent by 2025. Unfortunately, debt would remain on a slightly upward path after 2020, rather than a very slight downward path as OMB projects.

Fig. 1 Debt as a Percentage of GDP in the President's Budget



Source: CBO, OMB, CRFB calculations
Note: "CBO Baseline w/ Drawdown" includes the budgetary effects of the President's war drawdown

This rising path occurs because deficits would increase faster than the growth of the economy in the later years of the projection window. After declining to a low of 2.0 percent of GDP in 2016, deficits would rise continuously to 2.9 percent by 2025. These deficits are an improvement over CBO's current law deficit in 2025 of 3.8 percent, but higher than OMB's estimated deficit of 2.5 percent of GDP.

Spending and revenue would both rise over time under the President's budget, although spending would increase somewhat faster. It would rise from 20.5 percent of GDP in 2015 to 22.1 percent of GDP by 2025, while revenue would rise from 17.8 percent in 2015 to 19.2 percent by 2025. The 2016-2025 ten-year averages for each are 21.6 percent and 19.0 percent, respectively, compared to 21.3 percent and 18.2 percent in CBO's baseline and 21.7 percent and 19.3 percent in

OMB's estimate of the budget. Over the past fifty years, spending has averaged 20.1 percent of GDP, and revenue has averaged 17.4 percent.

Fig. 2 Budget Metrics in CBO's Analysis of the President's Budget

	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2016-2025
Revenue											
2016 Budget (CBO)	19.0%	19.0%	19.0%	19.0%	19.0%	18.8%	18.8%	18.9%	19.0%	19.2%	19.0%
2016 Budget (OMB)	18.7%	19.1%	19.1%	19.2%	19.3%	19.3%	19.4%	19.5%	19.6%	19.7%	19.3%
CBO Baseline	18.4%	18.3%	18.1%	18.1%	18.1%	18.1%	18.1%	18.2%	18.2%	18.3%	18.2%
Outlays											
2016 Budget (CBO)	21.0%	21.0%	21.1%	21.4%	21.5%	21.6%	21.7%	21.9%	22.0%	22.1%	21.6%
2016 Budget (OMB)	21.3%	21.4%	21.5%	21.6%	21.7%	21.9%	21.9%	22.0%	22.0%	22.2%	21.7%
CBO Baseline	20.8%	20.6%	20.5%	20.9%	21.2%	21.4%	21.8%	21.8%	21.7%	22.1%	21.3%
Deficits											
2016 Budget (CBO)	-2.0%	-2.0%	-2.1%	-2.4%	-2.6%	-2.9%	-2.9%	-2.9%	-2.9%	-2.9%	-2.6%
2016 Budget (OMB)	-2.5%	-2.3%	-2.3%	-2.4%	-2.5%	-2.6%	-2.6%	-2.5%	-2.4%	-2.5%	-2.5%
CBO Baseline	-2.4%	-2.3%	-2.4%	-2.8%	-3.1%	-3.3%	-3.7%	-3.6%	-3.4%	-3.8%	-3.1%
Debt											
2016 Budget (CBO)	73.5%	72.7%	72.2%	72.1%	72.0%	72.3%	72.5%	72.7%	72.9%	73.1%	N/A
2016 Budget (OMB)	75.0%	74.6%	74.3%	74.1%	74.0%	74.0%	73.9%	73.7%	73.5%	73.3%	N/A
CBO Baseline	73.8%	73.2%	72.9%	73.1%	73.5%	74.0%	74.9%	75.7%	76.2%	77.1%	N/A

Source: CBO, OMB

Policy Changes

Excluding the drawdown of war spending, which mainly represents a policy already in place, the President's budget contains a total of $615 billion net deficit reduction through 2025. This is the net result of about $2.22 trillion of new revenue and spending cuts, $1.67 trillion of new tax breaks and spending increases, and $70 billion of interest savings. Total savings are somewhat lower than the $930 billion that OMB estimates for the same policies.

We described the changes proposed in the President's budget in some detail in our initial analysis of the budget in February (read the analysis in full here). Under CBO's estimates, the budget through 2025 includes about $475 billion of new spending initiatives, $490 billion of sequester relief, $465 billion of tax cuts, $1.55 trillion of tax increases, $195 billion of net health care savings, $65 billion of other mandatory savings, and $175 billion of net savings from immigration reform. These net primary savings also generate $70 billion in lower interest spending on the debt.

Fig. 3 Policy Changes Through 2025 as Estimated by CBO and OMB

	CBO Numbers	OMB Numbers
New Spending Initiatives	**$475 billion**	**$530 billion**
Fund universal pre-K, other children's initiatives	$90 billion	$90 billion
Expand access to child care	$75 billion	$80 billion
Offer free community college, increase higher ed spending	$105 billion	$100 billion
Increase surface transportation spending	$95 billion	$115 billion
Other spending increases`	$110 billion	$145 billion
Sequester Relief	**$490 billion**	**$590 billion**
Reduce discretionary sequester cuts	$370 billion	$405 billion
Repeal mandatory spending sequester	$120 billion	$185 billion
New Tax Breaks	**$465 billion**	**$475 billion**
Extend expiring child tax credit expansion	$90 billion	$80 billion
Extend and expand EITC	$95 billion	$90 billion
Reform, extend, and expand education tax breaks	$120 billion	$105 billion
Expand child care incentives, provide second-earner credit	$125 billion	$140 billion
Enact other tax breaks	$35 billion	$60 billion
Revenue Increases	**-$1,550 billion**	**-$1,845 billion**
Limit value of tax preferences for high earners	-$570 billion	-$640 billion
Use one-time tax on foreign income for highway shortfall	-$215 billion	-$270 billion
Reform and increase estate tax	-$155 billion	-$215 billion
Increase and reform capital gains taxes	-$235 billion	-$210 billion
Impose a financial fee	-$110 billion	-$110 billion
Reduce the tax gap	-$80 billion	-$85 billion
Reform and increase unemployment taxes	-$20 billion	-$60 billion
Increase tobacco taxes and index to inflation	-$85 billion	-$95 billion
Other revenue	-$80 billion	-$160 billion
Health Care Reforms	**-$195 billion**	**-$290 billion**
Reform Sustainable Growth Rate (SGR)	$175 billion	$155 billion
Reduce spending on prescription drugs	-$165 billion	-$160 billion
Reduce spending on post-acute care	-$80 billion	-$105 billion
Raise Medicare means-tested premiums and cost-sharing	-$95 billion	-$80 billion
Enact delivery system reforms, strengthen IPAB	-$30 billion	-$65 billion
Reduce bad debts, GME, and MA spending	-$65 billion	-$95 billion
Make health care investments and other health changes	$65 billion	$60 billion
Other Mandatory Savings	**-$65 billion**	**-$120 billion**
Reduce farm subsidies	-$10 billion	-$15 billion
Increase PBGC premiums	-$15 billion	-$20 billion
Other savings`	-$40 billion	-$80 billion
Additional Cuts and Reforms	**-$170 billion**	**-$155 billion**
Enact immigration reform	-$175 billion	-$160 billion
Other adjustments`	$5 billion	$5 billion
Net Interest	**-$70 billion**	**-$120 billion**
Total Deficit Reduction	**-$615 billion**	**-$930 billion**
Reduce Overseas Contingency spending from baseline	-$615 billion	-$640 billion
Total Change in Deficit from CBO Baseline	**-$1,230 billion**	**-$1,570 billion**

Source: CBO, OMB, CRFB calculations
` Partially estimated based on OMB scores

Differences Between CBO and OMB Estimates

In total, CBO estimates deficits under the President's budget (2015-2025) will be $206 higher through 2025 than OMB estimates. There are at least three ways to look at these differences, described below.

One way to understand the difference between CBO and OMB estimates is to show how much is attributable to differing estimates in *policy changes* versus how much is attributable to differences in *baseline* projections prior to policy action. On a like basis (using our "PAYGO baseline"), CBO estimates $315 billion less of savings than OMB does. This means that more than all of the difference can be attributed to different policy scores as opposed to different baseline projections. Some of the biggest differences in savings estimates include the 28 percent limit on tax breaks ($80 billion less), the increases in the estate tax ($60 billion less), delivery system and IPAB changes ($35 billion less), and post-acute care payment reductions ($25 billion less).

Another way to understand the differences is to look at them by source. In total, CBO estimates $1.1 trillion of lower revenue, $710 billion of lower primary spending, and $195 billion lower of interest costs than OMB estimates. In other words, lower revenue estimates really drive CBO's higher deficit estimates, with lower spending mostly but not fully offsetting that effect.

Finally, one can look at the *cause* of the differences. CBO's more pessimistic economic projections – including GDP that is 1 percent lower in 2025 – explain $345 billion of higher deficits. By contrast, technical differences – which include things like demographics, income distribution, average tax rates, average benefits, and behavioral responses to policy changes – lower CBO's deficits below what OMB estimated by $139 billion. Importantly, some of this could be due to different conventions, such as OMB projecting what the economy will look like *with* the President's policies in place and CBO not taking them into account.

Fig. 4: Breaking Down the 2015-2025 Deficit Differences Between CBO and OMB

Differences in…	Estimates
What is Being Estimated	**$206 billion**
Baseline Assumptions	-$109 billion
Policy Scores	$315 billion
Sides of the Ledger	**$206 billion**
Revenue	$1,100 billion
Spending	-$720 billion
Interest	-$195 billion
Estimation Methodology	**$206 billion**
Economic Forecasts	$345 billion
Technical Factors	-$139 billion

Positive numbers indicate CBO scores the FY 2016 Budget as increasing the deficit compared to OMB's estimate, negative numbers reduce it. Numbers are rounded and may not add to total.

Conclusion

Although it differs somewhat, CBO's analysis of the President's budget verifies OMB's finding that the President's budget would commendably pay for all of the initiatives it proposes with real savings.

Unfortunately, it also verifies that the budget includes too little net savings to put the debt on a clear downward path relative to the economy. And unlike OMB's estimates, CBO finds the President's budget would result in a small but continuous rise in the debt after 2020.

To ensure the debt is on a sustainable path, policymakers should focus first on the savings in the President's budget, enacting only the new spending and tax breaks that pass a cost-benefit analysis when weighed against the need for further deficit reduction. Furthermore, policymakers should go beyond the President's budget to pursue serious structural entitlement reform. This means not only identifying further health care reforms, but putting in place a plan to make Social Security sustainably solvent for the next 75 years and beyond.

In additional to tax reform and spending cuts, such entitlement reform will be necessary to put the county on a sustainable fiscal course for this and future generations.

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