From Widening Deficits to Paying Down the Debt: Benefits for the American People

August 4, 1999

Office of Economic Policy
U.S. Department of Treasury

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Executive Summary

- President Clinton and Vice President Gore, working with the Congress, set the nation on a new course of fiscal responsibility. This program has reversed the pattern of deficit spending. In fiscal year 1999, a surplus of $99 billion, or 1.1 percent of GDP is expected. This would be the largest surplus relative to GDP since 1951. We have ended 28 consecutive years of deficit spending and recorded the first back-to-back surpluses since 1956-57.

- In early 1993, the Federal budget was projected to be in deficit by $429 billion in 1999. Instead, we now expect a surplus of $99 billion. This amounts to a saving of almost $530 billion for 1999 alone.

- Deficits over the years 1994 through 1999 were projected to total $2.1 trillion. Instead, shrinking deficits and a surplus in the two most recent years have slashed that figure by $1.7 trillion, or more than 80 percent. Over the next decade, unified budget surpluses are projected to build, reaching $473 billion, or 3.4 percent of GDP, by 2009.

- Because of this deficit reduction, we have reduced publicly held debt approximately $87 billion this fiscal year– the largest on record after adjusting for inflation. In the last two years, we have paid down $142 billion in debt. Since its peak of $3.830 trillion in March of 1997, we will pay down the debt to $3.638 trillion this quarter.

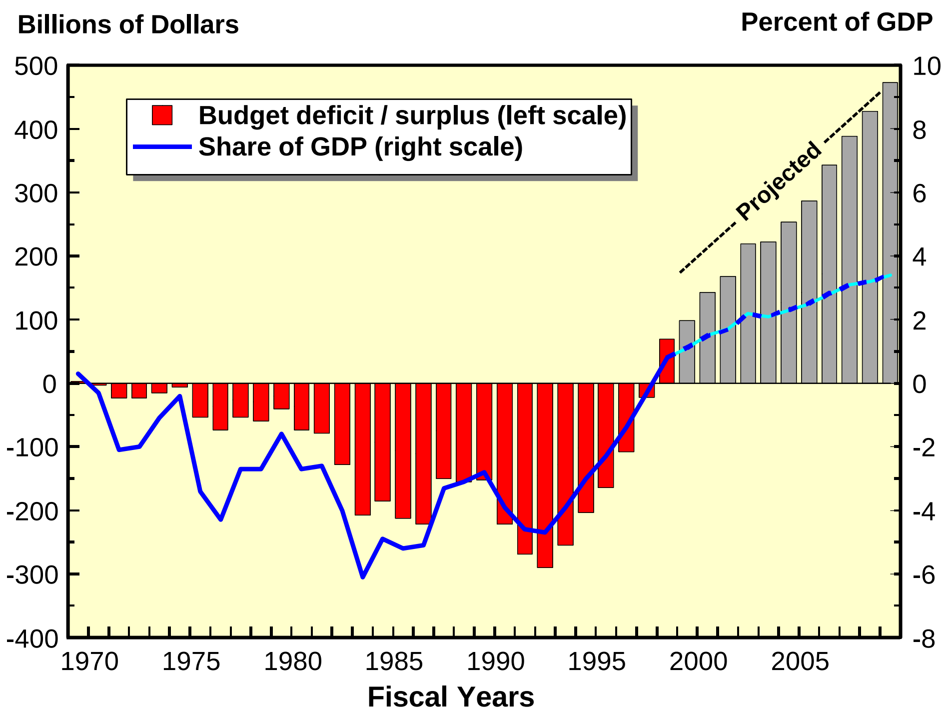
- The reduction in the deficit and lower interest rates have meant much lower interest costs than had been projected. Over the past seven years, a total of $189 billion in interest has been saved.

- In the absence of deficit reduction, interest payments on the ballooning federal debt would have swelled even more in the years ahead. It is estimated that lower interest payments on the federal debt from 1993 through 2003 will save taxpayers a total of almost $840 billion.

- Deficit reduction has helped reduce mortgage interest costs for American families. A typical American family with a mortgage of $100,000 might expect to save about $2,000 annually in mortgage costs.

- Deficit reduction has made more funds available for the private sector, helping to spur investment. Private business investment has surged. Investment in producers durable equipment has grown at double digit rates for six years in a row for the first time on record.

FIRST FEDERAL BUDGET SURPLUS SINCE 1969



Source: OMB, Mid-Session Review FY-2000 Budget

- Deficit spending had been the norm for the U.S. budget throughout most of the post-World War II period. Surpluses were recorded in only three years of the 1950s and in only two years of the 1960s. Our last surplus was in 1969, and it amounted to only 0.3 percent of GDP.

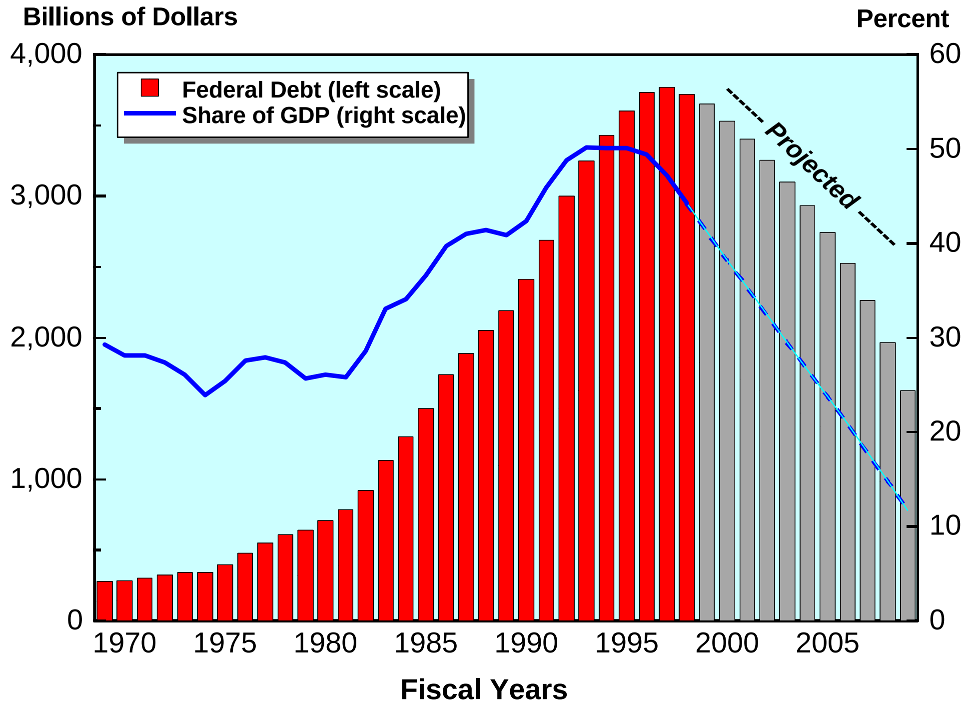
- ***During the 1980s, deficits widened dramatically, reaching 6.1 percent of GDP in 1983.*** The recessions of 1980-1982 contributed to the size of the deficit. But even after six years of economic expansion, 1989's deficit was still 2.8 percent of GDP.

- The deficit widened again in the early 1990s and reached a record in dollar terms of $290 billion, or 4.7 percent of GDP. Since then, ***President Clinton's program has reversed the pattern of deficit spending. In fiscal year 1999, a surplus of $99 billion, or 1.1 percent of GDP, is expected. This would be the largest surplus relative to GDP since 1951.***

- ***Over the next decade, unified budget surpluses are projected to build, reaching $473 billion, or 3.4 percent of GDP, by 2009.***

- Even excluding Social Security funds, the cumulative "on-budget" surplus is projected to exceed $1 trillion over the next ten years.

FEDERAL DEBT ON A DOWNWARD PATH



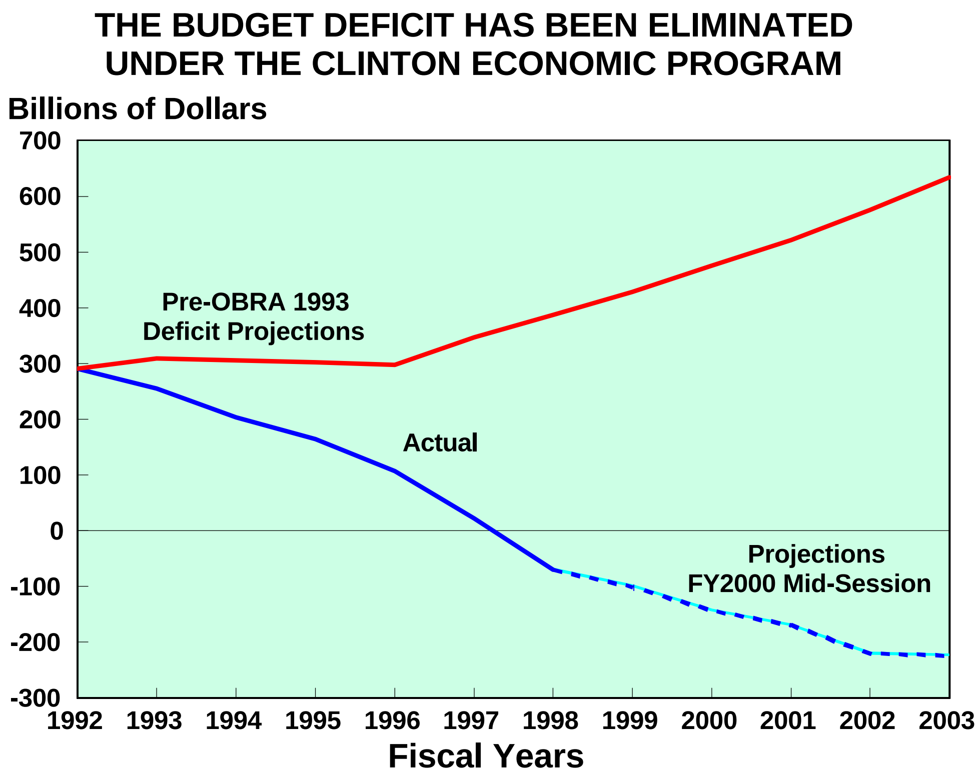
Source: OMB, Mid-Session Review FY-2000 Budget

- ***The legacy of deficit spending was a huge piling up of Federal debt***.

- ***Between 1980 and 1993, the amount of Federal debt held by the public more than quadrupled*** from $710 billion to $3.2 trillion. During this time, publicly held debt surged from 26 percent to 50 percent of GDP.

- Deficits, although declining, continued to add to the Federal debt through 1997, when the amount reached $3.8 trillion. Because deficits were cut over the 1993-1997 period, the debt relative to GDP eased to 47 percent.

- ***Fiscal year 1999 is the second year in a row in which we have been able to pay down some of the outstanding debt***. As a result, the ratio of debt to GDP is being slashed this year to about 41 percent. Under the Administration's proposals, the amount of Federal debt outstanding is projected to fall further to $1.6 trillion, or only 12 percent of GDP, by the year 2009, and is expected to disappear entirely by 2015. This means fewer taxpayer dollars will be needed to pay interest on the public debt between now and 2015.



Source: OMB, Mid-Session Review FY-2000 Budget

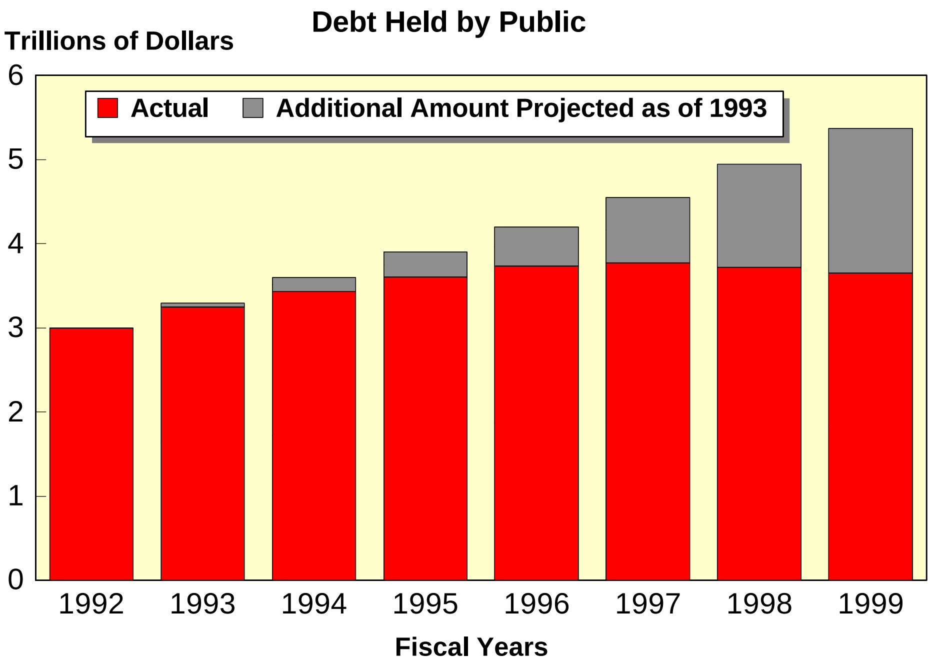
- The path to closing the Federal deficit began with the Administration's efforts in 1993 to reverse the previous decade's trend toward ever-widening deficits. The ***Omnibus Budget Resolution Act of 1993 (OBRA 1993)*** was a critical step toward achieving fiscal soundness.

- The ***1997 Balanced Budget Act*** provided another important push for fiscal discipline.

- ***Due to responsible fiscal policy and the noninflationary growth that it made possible, the Federal budget is now on a path of rising surpluses. We are on track to achieve a surplus approaching $100 billion in fiscal year 1999 instead of the $429 billion deficit that was projected for this year in early 1993. This amounts to a savings of almost $530 billion for 1999 alone.***

- Deficits over the years 1994 through 1999 were projected to total $2.1 trillion. Instead, shrinking deficits and a surplus in the most recent two years have slashed that figure by ***$1.7 trillion, or more than 80 percent***.

DEBT BURDEN CUT BY ONE-THIRD FROM PRE-OBRA PROJECTION



Source: OMB, Mid-Session Review FY-2000 Budget

X Had the deficit grown as projected in 1993, the Federal debt held by the public would have ballooned to $5.4 trillion by 1999, representing 61 percent of GDP, rather than the actual current $3.7 trillion, or 41 percent of GDP.

X As a result, ***the Federal government's debt is $1.7 trillion lower than it was projected to be***. The average American family's share of the Federal debt burden is therefore more than $24,000 smaller.

- This $1.7 trillion represents roughly 19 percent of nominal GDP, and is money that has been freed up for investment in American businesses and homes.

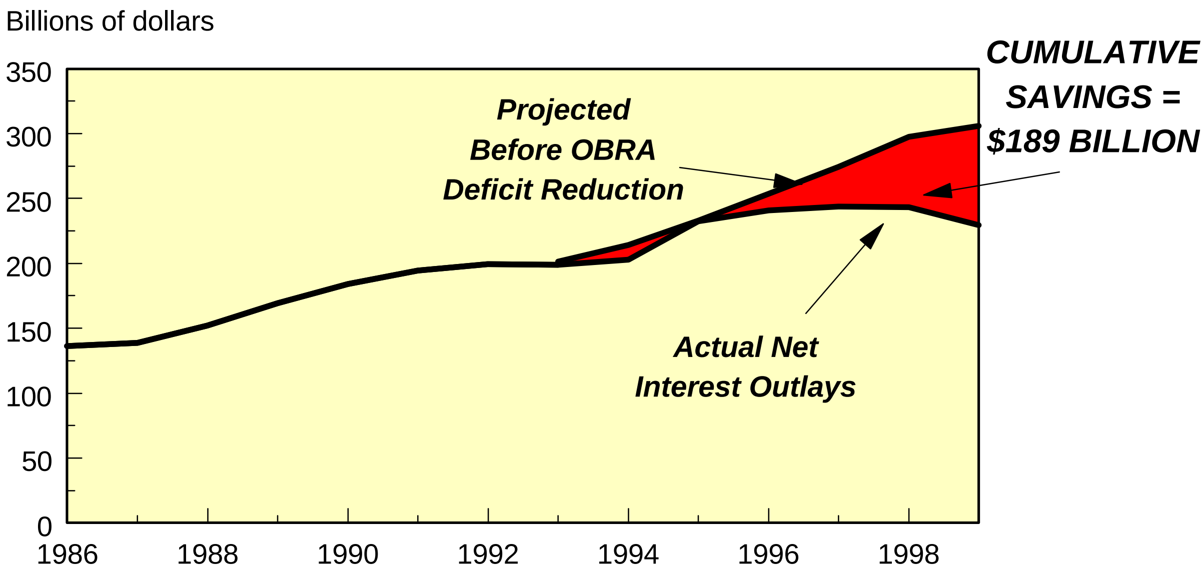
- The attached table illustrates how that $1.7 trillion reduction in the debt burden might be shared by each state, based on relative amounts of personal income.

STATE SHARE OF REDUCTION IN DEBT BURDEN
Billions of Dollars

1.	California	$213.9
2.	New York	137.3
3.	Texas	117.4
4.	Florida	91.8
5.	Illinois	82.8
6.	Pennsylvania	76.6
7.	Ohio	67.1
8.	New Jersey	65.6
9.	Michigan	60.4
10.	Massachusetts	48.0
11.	Georgia	45.5
12.	Virginia	44.3
13.	North Carolina	43.2
14.	Washington	37.9
15.	Maryland	36.6
16.	Indiana	34.0
17.	Missouri	31.6
18.	Wisconsin	31.2
19.	Minnesota	31.0
20.	Tennessee	30.5
21.	Connecticut	29.3
22.	Colorado	27.1
23.	Arizona	25.6
24.	Alabama	22.2
25.	Louisiana	22.2
26.	Kentucky	20.2
27.	South Carolina	19.5
28.	Oregon	19.4
29.	Oklahoma	16.8
30.	Iowa	16.3
31.	Kansas	15.6
32.	Mississippi	12.4
33.	Arkansas	12.3
34.	Nevada	11.3
35.	Utah	10.5
36.	Nebraska	9.8
37.	West Virginia	8.4
38.	New Mexico	8.2
39.	New Hampshire	8.2
40.	Hawaii	7.4
41.	Maine	6.8
42.	Rhode Island	6.3
43.	Idaho	6.2
44.	Delaware	5.3
45.	District of Columbia	4.6
46.	Montana	4.2
47.	South Dakota	3.9
48.	Alaska	3.8
49.	Vermont	3.4
50.	North Dakota	3.3
51.	Wyoming	2.7
	Total United States	$1,700.0

Note: Allocated according to State personal income.
Source: OMB and U.S Bureau of Economic Analysis.

FEDERAL INTEREST EXPENSES HAVE BEEN SHARPLY REDUCED



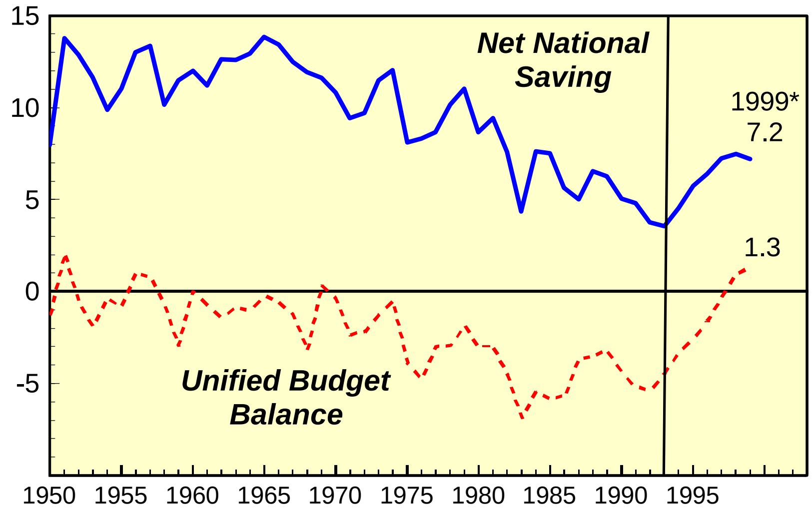
Source: OMB, Mid-Session Review of FY-2000 Budget

- The reduction in the deficit and lower interest rates have meant much lower costs than had been projected prior to the passage of OBRA. ***Over the past seven years, a total of $189 billion in interest has been saved***, as illustrated in the chart above. ***That amounts to roughly $2,700 for every American family***.

- In the absence of deficit reduction, interest payments on the ballooning federal debt would have swelled even more in the years ahead. ***It is estimated that lower interest payments on the federal debt from 1993 through 2003 will save taxpayers a total of almost $840 billion***.

TURNAROUND IN FEDERAL BUDGET BOOSTS NATIONAL SAVING

Percent of Net National Product - Fiscal Years



* FY-1999 estimated.
Source: BEA, National Income and Product Accounts; OMB, Mid-Session Review FY-2000 Budget.

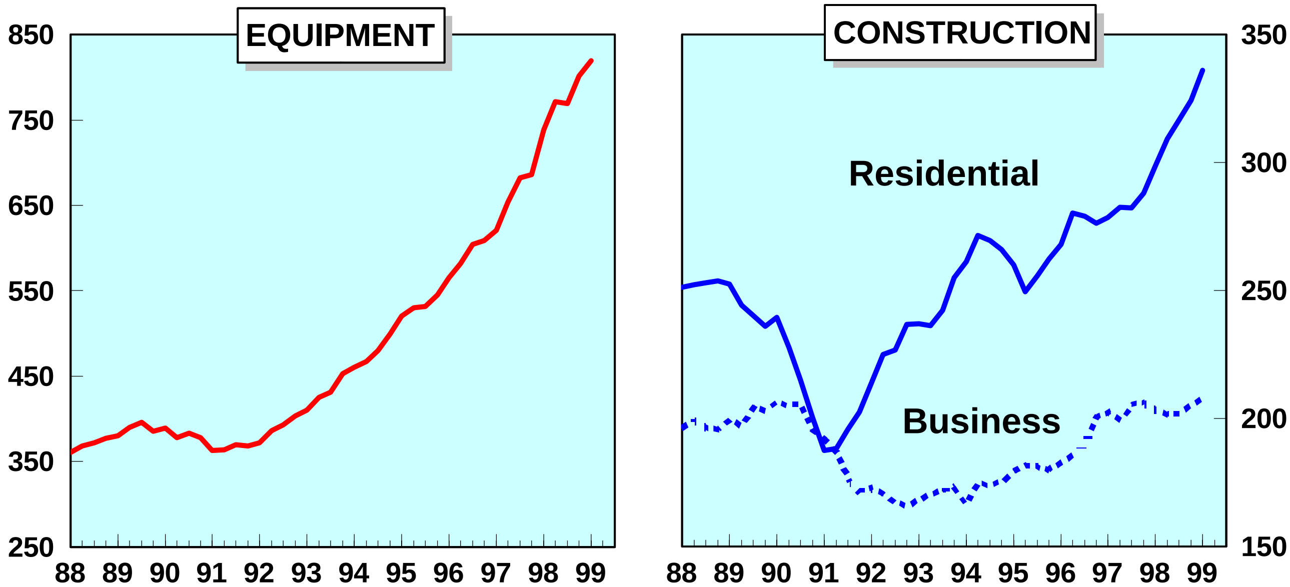
- ***The swing in the Federal budget from steep deficit to surplus has resulted in a doubling of the net national saving rate*** from a post-World War II low of only 3.5 percent of net national product (NNP) in fiscal year 1993 to an estimated 7.2 percent this year. This 3.7 percentage point rise in net national saving was more than accounted for by a 5.7 percentage point swing in the Federal budget, from a deficit of 4.4 percent of NNP in FY-1993 to a surplus estimated at 1.3 percent of NNP this year.

- ***Growing Federal deficits had been a severe drain on national saving.*** In borrowing from the private sector to finance the unified deficit, the Federal government reduced the amount of national saving available for more productive use in the private sector.

- ***As a result of the swing from deficit to surplus, more funds are available for private sector uses, helping to spur investment.***

PRIVATE INVESTMENT HAS SURGED

Billions of 1992 Dollars



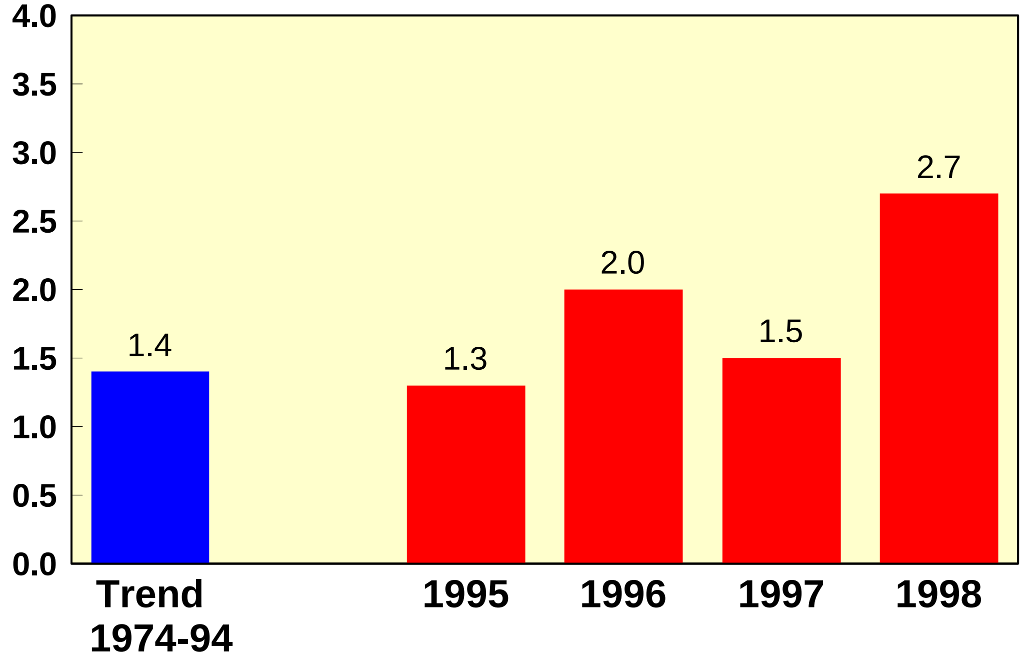
Source: BEA, National Income and Product Accounts.

- ***Private business investment has surged*. *As a share of GDP, real investment has risen to a record high of more than 12 percent*.**

- ***Purchases of producers' durable equipment have been particularly strong.*** For the first time on record, annual growth rates were in double digits for six years running. This component of investment, which includes computers, may be especially closely related to productivity growth.

- ***Investment in new business structures has also benefited from the low interest rate environment.*** The nonresidential market has been recharged since 1993.

STRONG PRODUCTIVITY GROWTH
Percent at an Annual Rate



Source: Bureau of Labor Statistics and U.S. Treasury estimates.

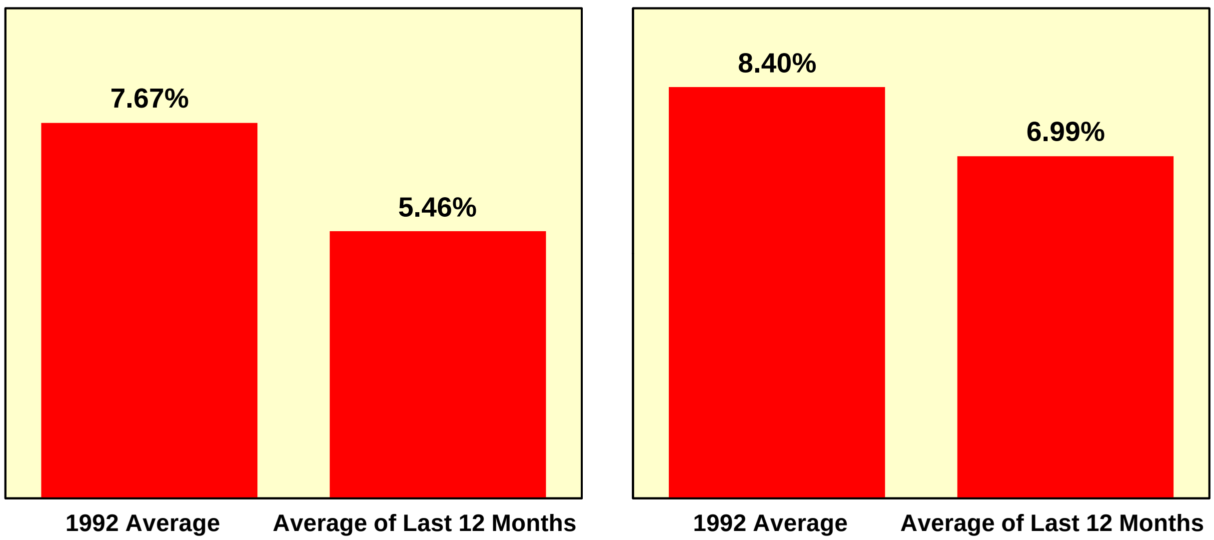
- Rising investment, especially in equipment incorporating the latest advances in technology, has contributed to a ***pickup in workers' productivity.*** Output per hour in the nonfarm business sector has grown at a 2.0 percent annual average rate from the end of 1994 through the first quarter of this year, a substantial acceleration from the trend rate of growth of 1.4 percent (calculated on a methodologically consistent basis) that prevailed from the 1970s through the early 1990s.

- ***Higher productivity leads to higher standards of living.*** Real average hourly earnings of nonfarm production and other nonsupervisory workers have recently posted the strongest increases since the early 1970s. Despite the rapid gain in real wages, unit labor costs have actually decelerated because of strong productivity growth, reducing the pressures on inflation.

- ***Rising investment has also resulted in a rapid expansion of capacity, contributing to an environment of noninflationary growth.***

DEBT REDUCTION MEANS LOWER INTEREST RATES
Monthly in Percent

LONG-TERM TREASURY BOND **30-YEAR CONVENTIONAL MORTGAGE**



Source: Federal Reserve

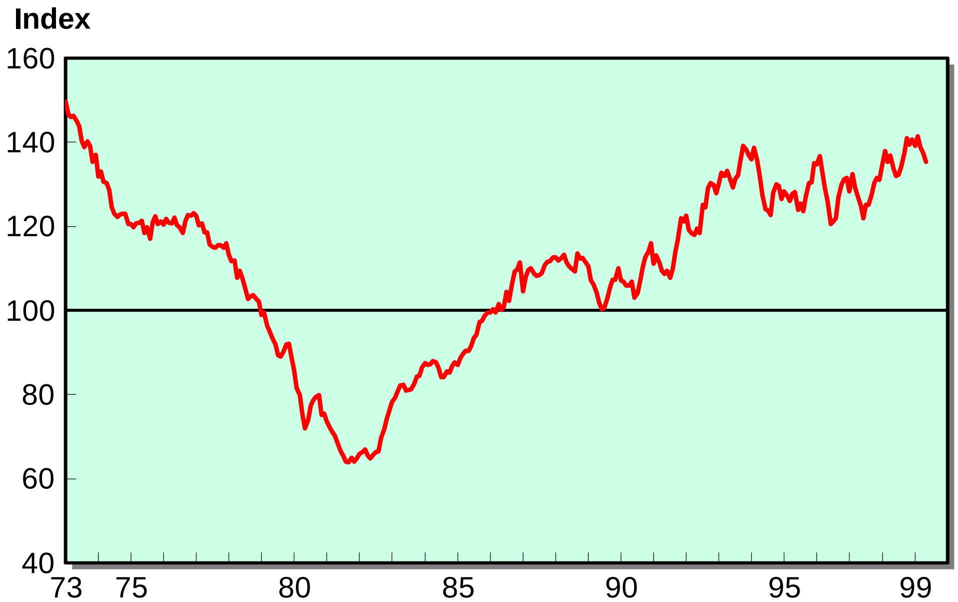
- The impact of deficit reduction on interest rates, especially long-term interest rates, has been significant. On average, interest rates have risen by about 1 percentage point during previous economic expansions. Instead, ***long-term rates have fallen during this expansion.***

- Market interest rates fluctuate and have risen recently but the average ***yield on the 30-year Treasury bond over the last twelve months was less than 5-1/2 percent, down from an average of 7.67 percent in 1992.*** The Blue Chip consensus of private forecasters predicts continued low interest rates.

- Interest rates on conventional home mortgages averaged just under 7 percent over the past twelve months – almost 1-1/2 percentage points below the average in 1992.

- ***Assuming an impact of deficit reduction on interest rates of 2 to 3 percentage points – a range that seems reasonable given the decline in rates during this expansion and the rise in rates during previous expansions – a typical American family with a mortgage of $100,000 would save around $2,000 a year on mortgage payments.*** Like a tax cut, lower mortgage payments would place more money in a family's pockets.

HOUSING AFFORDABILITY SINCE 1993 HAS BEEN THE BEST SINCE THE EARLY 1970'S



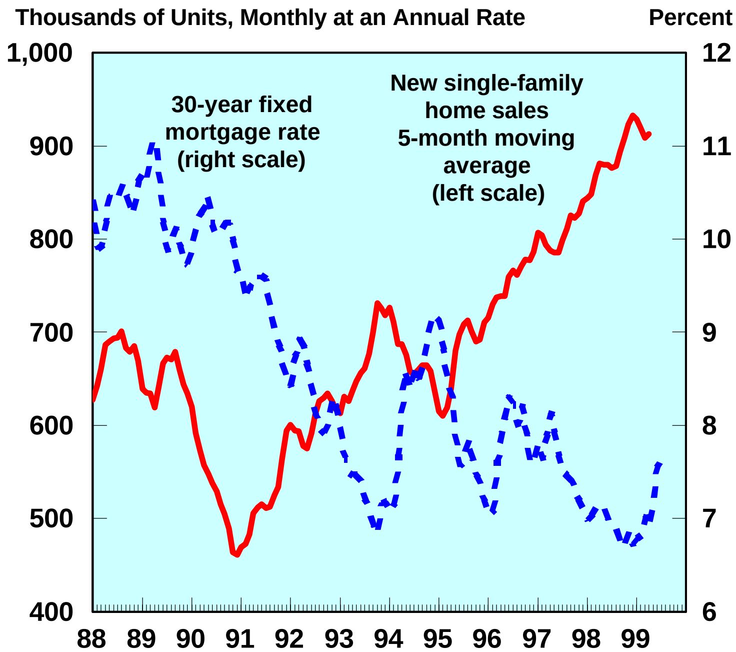
Source: National Association of Realtors

- Lower mortgage interest rates contributed to making housing more affordable. ***Housing affordability conditions since 1993 have been the most favorable since the early 1970's***.

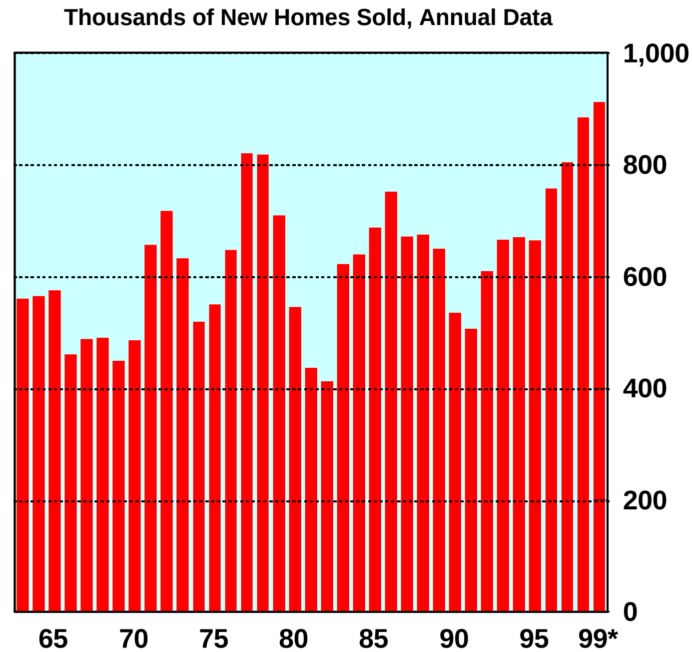
- The index shown above measures the size of a mortgage for which a family earning the median income can qualify, relative to the median price of a home. An index reading of 100 means that a family with median income can qualify for a mortgage that would allow it to purchase a median-priced home. ***Since 1993, half of all households had at least 30 percent more income than required to buy the average home.***

- Lower monthly payments and the strong economy have opened the housing market over the past six years to many more families whose income may be below the median level.

HOME SALES RISE AS MORTGAGE RATES FALL



..AND SALES HAVE HIT A RECORD



* First six months at an annual rate.

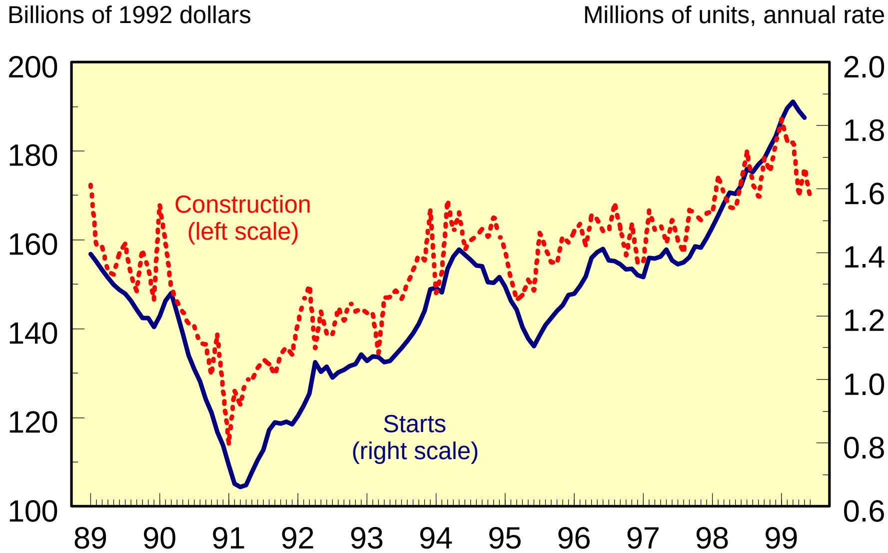
Source: Federal Reserve and U.S. Bureau of the Census

- ***Favorable housing affordability has led to a record-setting pace of home sales***. It is estimated that a sustained drop of 1 percentage point in the mortgage interest rate paves the way for roughly 70,000 new home purchases per year. That effect, coupled with low unemployment, rising income and wealth, and high levels of consumer confidence, have spurred sales of both new and existing homes to all-time highs.

- New single-family home sales totaled 885,000 in 1998, ***exceeding the previous record set in 1977 by 8 percent***. Through the first half of 1999, new home sales were on an annual pace of over 910,000.

- ***Resales of existing homes also hit new peaks***, according to the National Association of Realtors. Sales of existing single-family homes reached almost 5 million last year, ***more than 13 percent above the old record of 1997.*** Resales in 1999 continue to climb.

HOUSING STARTS AND CONSTRUCTION



Source: U.S. Bureau of the Census

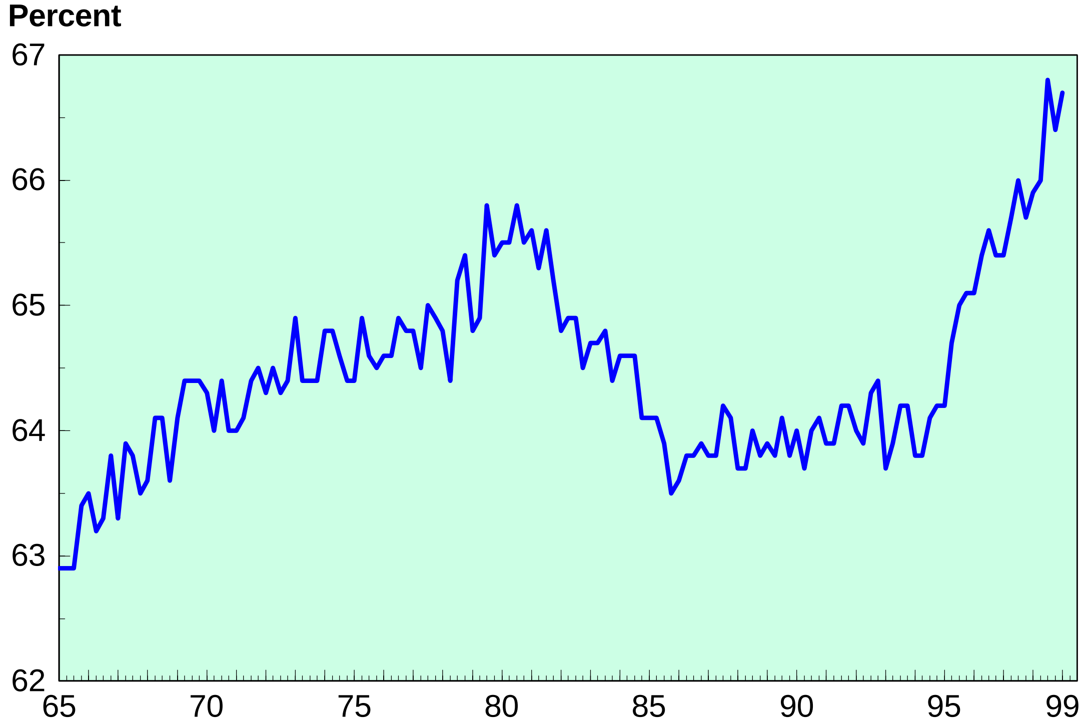
- Demand for new housing and residential improvements, financed at lower interest rates, has led to ***strong growth in real construction spending*** since the beginning of 1993. Real expenditures on residential building have grown at a 4 percent annual rate from early 1993 through the first five months of this year.

- ***Starts of new homes***, both single and multi-family, ***increased by one-third*** since 1992, rising to 1.6 million in 1998. That made last year the ***best year for home building since 1977 and 1978,*** when the baby boom generation began to have a significant impact on the housing market.

- ***The growth of new housing prompted large gains in construction of new retail establishments as well***. The commercial real estate market picked up beginning in 1994, with real construction spending growing by an annual average of almost 8 percent since then.

- ***Growth in residential and commercial construction has contributed to sizable gains in overall construction employment***. Since January 1993, construction jobs have increased by more than a third, rising by 1.7 million jobs to 6.3 million as of this June.

HOMEOWNERSHIP RATE THE HIGHEST EVER

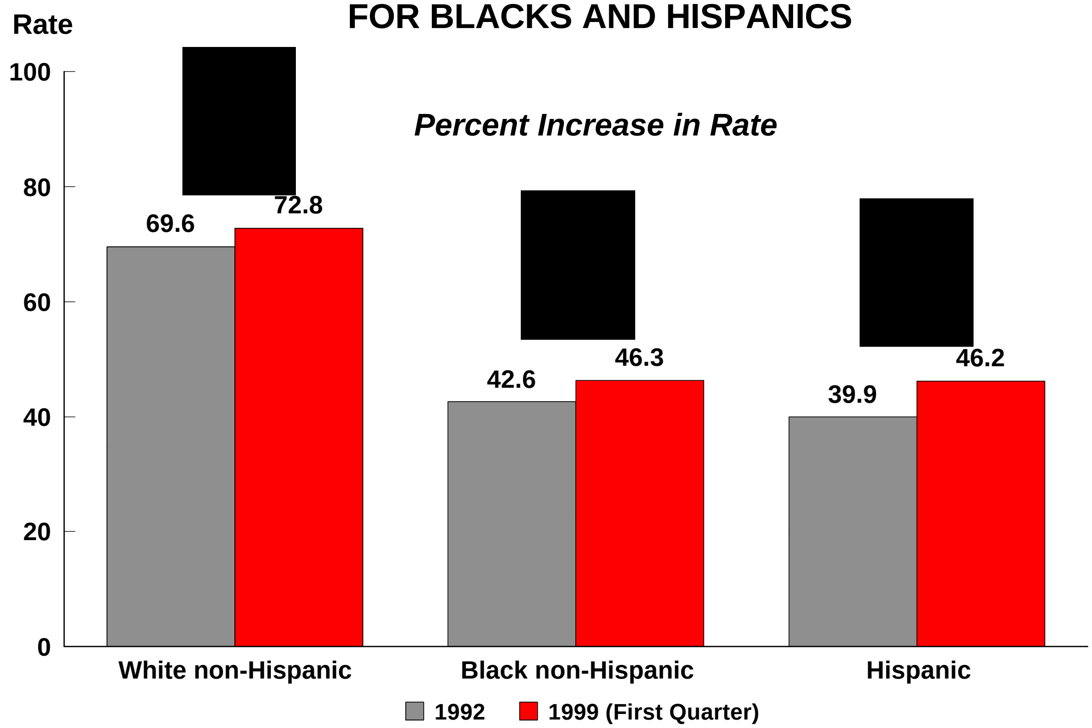


Source: U.S. Bureau of the Census

- ***Since the first quarter of 1993, an additional 7.9 million families have become homeowners***. For the first time ever, the number of families in the U.S. who own their own homes topped 69 million and is nearing 70 million.

- After falling in the early 1980s and stagnating through the mid 1980s until 1993, ***the homeownership rate rose to an historical high of 66.8 percent in 1998***. Prior to the recent period, the old record homeownership rate was 65.8 percent, set in the third quarter of 1980.

HOMEOWNERSHIP RATES HAVE RISEN FASTER FOR BLACKS AND HISPANICS



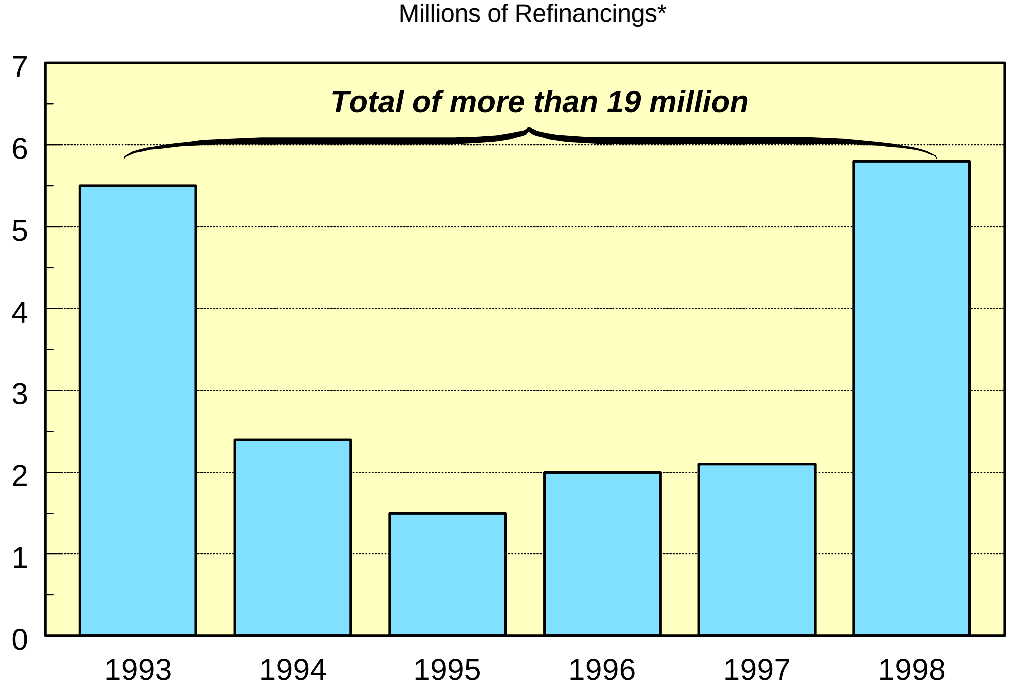
Source: U.S. Bureau of the Census

- The expansion in the homeownership rate has been most pronounced for groups that have typically had lower participation in the housing market. While the homeownership rate for black and Hispanic households still remains below that of white households, ***both minority groups have enjoyed much more rapid growth in homeownership than the rest of the population over the past six years***.

- The homeownership rate for black non-Hispanic households increased from 42.6 percent in 1992 to 46.3 percent by the first quarter of 1999. The rate for Hispanic households rose from 39.9 percent to 46.2 percent.

- In addition to low mortgage rates and a strong economy, Administration actions such as lowering FHA mortgage insurance premiums and forming the National Partners in Homeownership program have contributed to the expansion in homeownership.

REFINANCINGS HAVE MADE HOMEOWNERS BETTER OFF



*Estimated by Treasury Department

- In addition to lowering finance costs to purchase a home, ***falling mortgage interest rates have allowed homeowners to save money by refinancing their existing mortgages***. As mortgage interest rates fell below 7 percent in 1993, refinancings surged to nearly 5-1/2 million that year. Those homeowners shaved about 2 percentage points off their mortgage rate on average, ***saving about $1,800 a year in interest payments for a typical-sized loan.***

- The stream of refinancings continued through 1998, when another drop in mortgage rates last year spurred an additional round of refinancings. Many families refinanced more than once over the 1993-1998 period. ***Since 1993, total mortgage refinancings have topped 19 million.***

- Many homeowners who refinanced borrowed a larger amount than their old loan but because of lower mortgage rates were able to keep their monthly payments steady. That extra cash was used in a variety of ways that helped families to be better off, such as making home improvements, paying off other higher-rate existing debt, buying a car, or paying for college.

- Other homeowners chose to refinance 30-year mortgage loans with shorter loan terms such as 15 years, thereby building up equity in their homes more quickly. Some with adjustable rate loans took advantage of the historically low rates to lock in the low financing costs by converting to a fixed-rate loan.