



MONTHLY BUDGET REVIEW

Fiscal Year 2003

A Congressional Budget Office Analysis

Based on the *Monthly Treasury Statement* for September and the *Daily Treasury Statements* for October

November 7, 2003

The federal government recorded a total budget deficit of \$374 billion in fiscal year 2003, \$216 billion more than the deficit recorded in 2002. At about 3.5 percent of gross domestic product (GDP), the 2003 deficit is the largest since 1993 relative to the size of the economy. The on-budget deficit grew for the third consecutive year—to \$535 billion—while the off-budget surplus, which includes transactions of the Social Security trust funds and the Postal Service, has remained steady since 2001 at about \$161 billion.

FISCAL YEAR TOTALS (In billions of dollars)

| | 2000 | 2001 | 2002 | 2003 |
|---|-------|-------|-------|-------|
| Receipts | 2,025 | 1,991 | 1,853 | 1,782 |
| Outlays | 1,789 | 1,864 | 2,011 | 2,157 |
| Surplus or Deficit (-) | 236 | 127 | -158 | -374 |
| On-budget | 86 | -33 | -317 | -535 |
| Off-budget | 150 | 161 | 160 | 161 |
| Surplus or Deficit (-) as a Percentage of GDP | 2.4 | 1.3 | -1.5 | -3.5 |

SOURCES: Department of the Treasury; CBO.

Since the government recorded a surplus of \$236 billion in 2000, the budgetary situation has worsened for three consecutive years. Receipts in 2003 fell for the third year in a row, dropping by \$71 billion, while outlays increased by \$146 billion over their 2002 level. The rate of spending growth in 2003, at 7.2 percent, was slightly below the 7.9 percent increase recorded in 2002 but still well above the 4 percent average for the previous decade.

TOTAL RECEIPTS (In billions of dollars)

| Major Source | Actual FY2002 | Actual FY2003 | Percentage Change |
|-------------------|------------------|------------------|----------------------|
| Individual Income | 858 | 794 | -7.5 |
| Corporate Income | 148 | 132 | -11.0 |
| Social Insurance | 701 | 713 | 1.7 |
| Other | <u>146</u> | <u>144</u> | -1.5 |
| Total | 1,853 | 1,782 | -3.8 |

SOURCES: Department of the Treasury; CBO.

Receipts in fiscal year 2003 totaled \$1,782 billion, which was 3.8 percent below their 2002 level of \$1,853 billion and 12 percent below their peak of \$2,025 billion in 2000. Falling receipts from individual and corporate

income taxes—the result of tax policy and weak income growth—accounted for almost all of the decline in total receipts over the past three years. In 2003, total receipts were 16.5 percent of GDP, down substantially from the post-World War II peak of 20.8 percent reached in 2000, and the lowest percentage since 1959.

Receipts from individual income taxes fell by \$65 billion, or 7.5 percent, in 2003. About \$34 billion of that decline came from nonwithheld receipts, mostly representing liabilities for tax year 2002, which were largely paid to the Internal Revenue Service by April 15. Those final settlements of the prior year's liability fell for the second year in a row to below the amounts received in fiscal year 1997. In addition, receipts withheld from paychecks declined by \$16 billion. An increase of \$14 billion in refunds in 2003, about the amount of advance refunds called for in the Jobs and Growth Tax Relief Reconciliation Act of 2003, also contributed to the decline.

Receipts from corporate taxes fell by \$16 billion, or about 11 percent, in fiscal year 2003. (They were down by 36 percent from their level in fiscal year 2000.) Increases in profits in recent months have begun to boost those receipts. Corporate receipts would have risen by about \$12 billion (or 9 percent) in 2003 if not for two legislated delays in due dates for payments that shifted receipts between fiscal years.

Receipts from social insurance taxes rose by \$12 billion, or 1.7 percent, in fiscal year 2003. Those receipts have continued to rise in the past two years, although at much slower rates than the 6 percent to 7 percent annual growth experienced from 1997 through 2001. They have not been directly affected by the recent tax cuts and largely follow aggregate wages and salaries.

Other tax receipts fell by \$2 billion, with declines in receipts from estate and gift taxes and Federal Reserve earnings partially offset by increases in other sources of revenue.

NOTE: Unless otherwise indicated, the figures in this report include the Social Security trust funds and the Postal Service fund, which are off-budget. Numbers may not add up to totals because of rounding.

TOTAL OUTLAYS
(In billions of dollars)

| Major Category | Actual FY2002 | Actual FY2003 | Percentage Change | |
|------------------------------------|------------------|------------------|----------------------|-----------------------|
| | | | Actual | Adjusted ^a |
| Defense—Military | 332 | 389 | 17.1 | 16.0 |
| Social Security | | | | |
| Benefits | 448 | 467 | 4.1 | 4.1 |
| Medicare | 256 | 277 | 8.2 | 6.9 |
| Medicaid | 148 | 161 | 8.9 | 8.9 |
| Unemployment | | | | |
| Insurance | 55 | 58 | 6.0 | 6.0 |
| Other Programs and Activities | <u>593</u> | <u>644</u> | 8.5 | 9.1 |
| Subtotal | 1,832 | 1,994 | 8.9 | 8.7 |
| Net Interest on the Public Debt | <u>179</u> | <u>162</u> | -9.6 | -9.6 |
| Total | 2,011 | 2,157 | 7.2 | 7.1 |

SOURCES: Department of the Treasury; CBO.

a. Excludes the effects of payments that were shifted because of legislative action or changes in the accounting of certain health payments of the Department of Defense.

Programmatic spending (which excludes net interest on the public debt) grew by almost 9 percent in 2003, on the heels of an 11 percent increase in 2002, both well above the 4 percent average annual growth experienced during the 1990s. In contrast, net interest on the public debt has declined by 25 percent over the past two years as a result of lower interest rates. In total, outlays in 2003 were 20.0 percent of GDP, the highest percentage since 1996.

Spending by the Department of Defense (DoD) has been a significant source of outlay growth, posting double-digit gains for the second year in a row. Defense was the only major category of spending that grew more rapidly in 2003 than in 2002, rising 16 percent this year compared with 13 percent last year (adjusted for accounting changes). Of the department's \$57 billion increase in outlays in 2003, roughly half stemmed from funds provided for the war in Iraq and continuing operations for the war on terrorism. DoD's spending, which grew by a total of only 10 percent from 1986 through 2001, has risen by 34 percent since then.

Other spending has also accelerated in the past two years. After growing at an average annual rate of about 5 percent from 1991 through 2001, nondefense spending (excluding net interest on the public debt) increased by 10 percent in 2002 and by 7 percent in 2003. Outlays for activities of the Department of Homeland Security rose sharply in 2003, driven by an \$8 billion increase for the

Transportation Security Administration. Significant increases in spending were also recorded by the Departments of Education, Veterans Affairs, Housing and Urban Development, and Agriculture, as well as for the Public Health Service, refundable tax credits, and emergency fiscal relief for states.

A relatively small cost-of-living increase dampened growth in Social Security outlays, which rose by 4.1 percent in 2003, slightly below the average annual growth of about 5 percent over the past decade. This was the third consecutive year of decelerating growth for the Medicare program; spending increased by 6.9 percent in 2003 (adjusted for timing shifts), compared with growth of 9 percent in 2002 and 10 percent in 2001. Medicaid outlays grew by 8.9 percent in 2003, down from the 13 percent increase recorded in 2002 but close to the average growth rate of 10 percent over the previous 10 years.

ESTIMATES FOR OCTOBER
(In billions of dollars)

| | Actual FY2003 | Preliminary FY2004 | Estimated Change |
|-------------|------------------|-----------------------|---------------------|
| Receipts | 125 | 135 | 11 |
| Outlays | 179 | 206 | 27 |
| Deficit (-) | -54 | -71 | -17 |

SOURCES: Department of the Treasury; CBO.

CBO estimates that the government recorded a deficit of \$71 billion in October—\$17 billion more than the shortfall recorded in the same month last year. The \$27 billion increase in outlays reflects both growth in spending and the effects of the calendar—November 1 fell on a weekend this year, thereby shifting about \$11 billion in outlays from November into October. Without that timing shift, outlays would have risen by about 9 percent. October outlays were boosted by \$5 billion in payments to states for emergency fiscal relief, largely completing the \$10 billion in payments authorized by the Jobs and Growth Tax Relief Reconciliation Act of 2003.

Receipts rose in October by about \$11 billion compared with October of a year ago. Most of that increase, \$8 billion, resulted from higher receipts of corporate income taxes. Those receipts were boosted in part by recent legislation that allowed corporations to delay until October about \$5 billion in payments otherwise due in September.