



MONTHLY BUDGET REVIEW

Fiscal Year 2006

A Congressional Budget Office Analysis

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

October 6, 2006

CBO estimates that the federal budget deficit was about \$250 billion in fiscal year 2006, around \$68 billion less than the shortfall recorded in 2005. Relative to the size of the economy, that deficit was equal to 1.9 percent of the gross domestic product (GDP), down from 2.6 percent in 2005. This estimate is based on data from the *Daily Treasury Statements* and CBO projections; the Treasury Department will report the actual deficit for fiscal year 2006 later this month.

ESTIMATES FOR SEPTEMBER (Billions of dollars)

	Actual FY2005	Preliminary FY2006	Estimated Change
Receipts	252	283	31
Outlays	216	229	13
Surplus	36	54	18

Sources: Department of the Treasury; CBO.

The budget surplus was about \$54 billion in September, CBO estimates, \$18 billion more than the surplus recorded in the same month last year. The government typically runs a surplus in September because of the influx of revenues from quarterly tax payments.

Receipts in September were about \$31 billion (or 12 percent) higher than receipts in September 2005. Net corporate receipts continued to show healthy growth, increasing by \$15 billion (or 21 percent). Steady growth in corporate profits probably explains most of that increase, although some of it likely stems from settlements of past years' taxes and a recent change in tax law that required large firms to accelerate some payments from 2007 into 2006. Nonwithheld individual income and payroll taxes rose by \$9 billion (or 18 percent), mainly from quarterly estimated payments of taxes for 2006. Withheld individual income and payroll taxes rose by about \$6 billion (or 5 percent).

Outlays in September were up by about 6 percent compared with spending in September 2005. A number of factors contributed to that result. Because the first day of October fell on a weekend in both 2005 and 2006, certain payments that would ordinarily have been made in October were instead made at the end of September each year. In 2005, about \$13 billion in payments was shifted

from October to September, \$3 billion more than the amount that was shifted this year (the 2006 shift was smaller because of a legislated change in the timing of certain Medicare payments). In addition, a legislated delay in Medicare payments moved more than \$4 billion in spending that would ordinarily have been made this September into fiscal year 2007. Finally, the Department of Education reported about \$12 billion more in outlays for student loans this September than it did last September. That difference occurred mostly because the department recorded a large portion of the subsidy costs for this year's loan consolidations in September, whereas much of last year's costs were recorded in March 2006. In September, the department also revised the estimated subsidy costs of some loans and loan guarantees made in previous years. In the absence of all of those factors, outlays in September would have grown by about 4 percent from 2005 to 2006.

FISCAL YEAR TOTALS (Billions of dollars)

	Actual FY2005	Preliminary FY2006	Estimated Change
Receipts	2,153	2,406	253
Outlays	2,472	2,656	185
Deficit (-)	-318	-250	68

Sources: Department of the Treasury; CBO.

CBO estimates that the federal deficit was about \$250 billion in 2006, down from \$318 billion in the previous year. The estimated deficit is about \$10 billion lower than CBO projected this summer, primarily because receipts of corporate income taxes were greater than expected. Estimated receipts and outlays for 2006 reflect an accounting adjustment that the Treasury made in August, involving withheld taxes on Social Security benefits, which reduced both amounts by about \$6 billion and did not affect the deficit.

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 RECEIPTS
(Billions of dollars)

Major Source	Actual FY2005	Preliminary FY2006	Percentage Change
Individual Income	927	1,049	13.1
Corporate Income	278	354	27.1
Social Insurance	794	833	5.0
Other	<u>154</u>	<u>170</u>	10.8
Total	2,153	2,406	11.8

Sources: Department of the Treasury; CBO.

CBO estimates that receipts in 2006 were about \$253 billion (or 11.8 percent) higher than in 2005. That percentage increase would be the second highest since 1981, surpassed only by last year's 14.5 percent growth. The growth in 2006 receipts far exceeded an estimated 6.6 percent increase in nominal GDP, causing revenues to rise as a share of GDP for the second year in a row—to about 18.4 percent, up from 17.6 percent in 2005. The 2006 figure is just above the 18.2 percent average experienced since 1965.

Receipts of individual income taxes, the largest tax source, increased by an estimated \$122 billion (or 13.1 percent) in 2006, and receipts of social insurance (payroll) taxes, the second largest source, rose by \$39 billion (or 5 percent). Most of the combined increase came from amounts withheld from employees' paychecks, which climbed by about \$103 billion, or about 7 percent. Those gains reflect the strength of wages and salaries during the year.

Nonwithheld receipts of individual income and payroll taxes gained about \$69 billion, or 19 percent, in 2006. About half of those gains occurred in April and May, when payments of amounts due with individuals' tax returns for 2005 boosted receipts. Quarterly payments of estimated taxes were also strong throughout the year. Data should become available in coming months that will identify which sources of income grew strongly and indicate whether significant changes occurred in the distribution of income among taxpayers facing different tax rates.

CBO estimates that receipts in 2006 from corporate income taxes grew strongly for the third straight year, increasing by about \$75 billion (or 27 percent) to \$354 billion. That surge boosted corporate receipts to about 2.7 percent of GDP, the highest point since 1978—the result of very robust corporate profits, which, as a share of GDP, have reached a level not seen in decades.

TOTAL OUTLAYS
(Billions of dollars)

Major Category	Actual FY2005	Preliminary FY2006	Percentage Change	
			Actual	Adjusted ^a
Defense—Military	474	500	5.3	6.1
Social Security				
Benefits	514	545	6.0	6.2
Medicare	336	378	12.6	16.5
Medicaid	182	181	-0.5	-0.5
Other Programs				
and Activities	<u>775</u>	<u>817</u>	5.4	6.7
Subtotal	2,280	2,420	6.1	7.4
Net Interest on the Public Debt	<u>191</u>	<u>237</u>	23.6	23.9
Total	2,472	2,656	7.5	8.7

Sources: Department of the Treasury; CBO.

a. Excludes the effects of payments that were shifted because of weekends or legislated payment delays. Also excludes the August 2006 adjustment involving withheld taxes on Social Security benefits; instead, corrects the figures on a month-by-month basis.

Outlays ended the year about 7.5 percent above 2005 levels, CBO estimates. Spending was equal to about 20.3 percent of GDP in 2006, close to the 20.5 percent share averaged since 1965 but somewhat larger than in the past five years, when spending averaged 19.6 percent of GDP. A number of accounting changes and calendar-related shifts in payment dates reduced the year-over-year growth rate. Adjusted for those factors, spending increased by 8.7 percent in 2006, the fastest rate of increase since 1990.

Spending for flood insurance claims, disaster relief, and other assistance in the aftermath of Hurricanes Katrina and Rita added roughly \$50 billion to outlays in 2006. Escalating interest costs—up by \$45 billion, or 24 percent—also had a significant impact on spending growth. Rising interest rates and higher inflation accounted for about three-fourths of the growth in outlays for net interest on the public debt.

Excluding hurricane-related spending and interest costs, outlays for all other federal programs rose by about 6 percent on an adjusted basis, compared with annual increases averaging about 8 percent over the 2001-2005 period.

The 16.5 percent increase in Medicare outlays was boosted by spending for the new prescription drug benefit. Other Medicare spending was about 6.7 percent higher than in 2005. Spending for Medicaid—which rose at an average annual rate of 9 percent over the previous five years—was virtually unchanged relative to its 2005 level, partly because the Medicare drug program covered some costs previously paid by Medicaid.