LONG-RANGE FISCAL POLICY BRIEF

CBO

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A 125-Year Picture of the Federal Government's Share of the Economy, 1950 to 2075

Summary

This policy brief presents a long view of the federal government's finances and the potential impact of two critical drivers of federal spending: the government's largest entitlement programs—Social Security, Medicare, and Medicaid—and interest on the federal debt held by the public. Under the projections shown here, outlays for those entitlement programs would rise from 8 percent of gross domestic product (GDP) today to 21 percent in 2075, which would exceed the share of GDP now absorbed by all federal revenues. Even if other major categories of federal spending remained fixed as a share of GDP, the growth of those programs would push total federal spending well above the level that it has been throughout much of the post-World War II period. Left unchecked, such spending could cause major deficits to emerge, propelling the government's debt and interest expenditures to unprecedented levels. The total cost of government, including interest expense, could more than double as a share of the economy, rising from 19 percent of GDP in 2002 to 40 percent in 2075.

Introduction

Presenting a 125-year picture of the financial affairs of the federal government, this policy brief shows the size of the federal budget in relation to the general economy from the middle of the last century through the projected retirement years of the children of the post-World War II baby boomers. Of course, the future path of the budget is highly uncertain and subject to wide variation. Except for the first 10 years, which is the period covered by the Congressional Budget Office's (CBO's) projection of a baseline, the path shown here is simply a representation based on an illustrative set of key assumptions.

Using CBO's new long-range projection model, the report merges the actual revenue and spending trends from 1950 through 2001 with projections for 2002 through 2075. For that purpose, the federal budget totals include the operations of the Social Security trust funds, which by law are considered to be "off-budget" Treasury accounts. The report expresses the budget figures as a share of gross domestic product (GDP) so that the magnitude of federal receipts and expenditures can be observed in relation to the total economic activity of the nation in any given year and over time.[1]

Assumptions

The figures and tables of this report illustrate a potential path for the budget that highlights projections of spending under current policies for the largest federal entitlement programs—Social Security, Medicare, and Medicaid—and projections of net interest. Social Security spending reflects growth in both the number of recipients and wages, upon which benefits are calculated. Medicare and Medicaid spending also reflects the increasing number of recipients as well as higher costs for medical care. For these projections, the rise in health care costs per recipient is assumed to slow to a growth rate of 1 percentage point faster than per capita GDP. While seemingly large, that rate is less than it has been in recent decades.

It is spending for the major entitlement programs and interest, because of the commitments involved and their sheer magnitude, that has the largest potential to constrain future Congresses. Moreover, much of the government's remaining spending consists of discretionary outlays, the levels for which the Congress will determine annually.

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1. The nature of future taxes and spending as well as the aggregate difference between them can affect the growth of the economy. For this analysis, however, no macroeconomic effects that might result from the fiscal policies reflected by the projections are considered.

Given the wide array of discretionary programs (with purposes ranging from national defense to research by the National Institutes of Health), this category of spending, unlike the major entitlement programs, does not easily lend itself to projections that merge economic and demographic assumptions with legislative rules for the payment of benefits. Thus, for this presentation, the projections assume that defense, nondefense discretionary, and all other spending (that is, other than that for Social Security, Medicare, Medicaid, and interest) will remain fixed as a share of GDP beginning in 2012, the last year of CBO's March 2002 10-year baseline projections. The projections also assume for analytical purposes that aggregate federal revenues will level out at 19 percent of GDP in 2020, reflecting the higher end of the range over which they have fluctuated during the post-World War II period (18 percent was the average from 1950 through 2001).

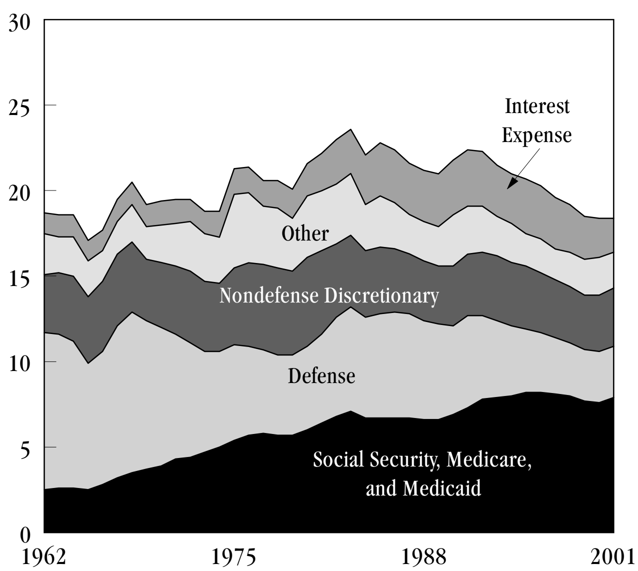
Trends, 1950 to the Present

Spending by the federal government grew from approximately 3 percent of GDP in 1925 to 15.6 percent in 1950. Following the Depression, World War II abruptly boosted federal spending to approximately 42 percent of GDP, but afterward it dropped and resumed a less volatile trend. Notably, over the past 40 years, Social Security, Medicare, and Medicaid have collectively become the largest component of the federal budget (*see Figure 1 and Table 1*). In 1962, with Social Security outlays representing only 2.5 percent of GDP and Medicare and Medicaid not yet created, spending for all other government activities accounted for 86 percent of noninterest federal outlays. The largest share was for national defense, which accounted for more than half of noninterest outlays and represented 9.2 percent of GDP. By 2000, spending for Social Security, Medicare, and Medicaid equaled 7.6 percent of GDP, triple the 1962 level for Social Security alone. While still constituting less than half of all federal expenditures, the three programs combined accounted for the largest share of the government's total outlays. Defense spending had fallen to 3 percent of GDP, and all other noninterest spending stood at 5.4 percent. Interest expenditures, whose share of GDP rose steadily from 1.2 percent in 1962 to a high of 3.3 percent in 1991, stood at 2.3 percent in 2000.

Figure 1.

Federal Outlays, 1962 to 2001

(As a percentage of GDP)



Source: Congressional Budget Office.

Table 1.

Federal Outlays, 1962 to 2001

(As a percentage of GDP)

Fiscal Year	Social Security, Medicare, and Medicaid	Defense	Nondefense Discretionary	Other	Interest Expense	Total
1962	2.5	9.2	3.4	2.4	1.2	18.8
1965	2.5	7.4	3.9	2.1	1.2	17.2
1970	3.9	8.1	3.8	2.2	1.4	19.3
1975	5.4	5.6	4.5	4.3	1.5	21.3
1980	6.0	4.9	5.2	3.6	1.9	21.6
1985	6.7	6.1	3.9	3.0	3.1	22.9
1990	6.9	5.2	3.5	3.0	3.2	21.8
1995	8.2	3.7	3.7	1.9	3.2	20.7
2000	7.6	3.0	3.3	2.2	2.3	18.4
2001	7.9	3.0	3.4	2.1	2.0	18.4

Source: Congressional Budget Office.

Projections, 2002 to 2075

According to the projected path for the budget shown in this report, outlays for Social Security, Medicare, and Medicaid (based on the current rules for benefits) would nearly double again as a share of GDP by 2035, rising to 15 percent. If spending for all other government activities

Table 2.

Federal Outlays by Category, 1950 to 2075

(As a percentage of GDP)

Fiscal Year	Social Security	Medicare	Medicaid	Social Security, Medicare, and Medicaid Combined	All Other Spending, Excluding Interest Expense	Interest Expense	Total
1950	0.3	n.a.	n.a.	0.3	13.5	1.8	15.6
1960	2.2	n.a.	n.a.	2.2	14.2	1.3	17.7
1962	2.5	n.a.	*	2.5	15.1	1.2	18.8
1970	2.9	0.7	0.3	3.9	12.8	1.4	19.3
1980	4.3	1.2	0.5	6.0	13.7	1.9	21.6
1990	4.3	1.9	0.7	6.9	11.7	3.2	21.8
2000	4.2	2.2	1.2	7.6	8.5	2.3	18.4
2010	4.4	2.7	1.8	8.8	7.6	0.8	17.2
2020	5.4	3.6	2.3	11.3	7.1	-0.5	17.9
2030	6.2	4.9	2.8	13.9	7.1	-0.2	20.8
2040	6.2	6.0	3.4	15.5	7.1	1.1	23.8
2050	6.0	6.7	3.9	16.7	7.1	3.1	26.9
2060	6.1	7.7	4.3	18.1	7.1	5.8	31.0
2070	6.2	8.9	4.9	20.0	7.1	9.4	36.5
2075	6.2	9.6	5.3	21.1	7.1	11.5	39.7

Source: Congressional Budget Office.
* = less than 0.05 percent.

in 2035 remained roughly the same share of GDP as projected for 2012 (7 percent), Social Security, Medicare, and Medicaid would account for almost 70 percent of all noninterest expenditures. By 2050, outlays for the three programs would equal 17 percent of GDP and by 2075, 21 percent—exceeding the share of GDP now absorbed by all federal revenues (*see Figure 2 and Table 2*).[2]

Conclusion

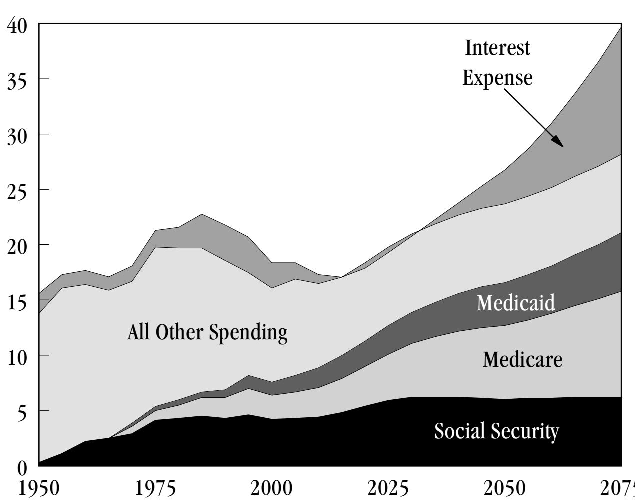
Under the assumptions CBO made for this 125-year picture of the federal government's finances, the projected rise in expenditures for Social Security, Medicare, and Medicaid would drive total federal outlays well above the level that they have been throughout much of the post-

2. For the purpose of this analysis, the projected shortfall of dedicated taxes to finance Social Security and Medicare is ignored, and spending for those programs reflects the commitments for benefits prescribed by the payment rules currently in place.

Figure 2.

Federal Outlays by Category, 1950 to 2075

(As a percentage of GDP)



Source: Congressional Budget Office.

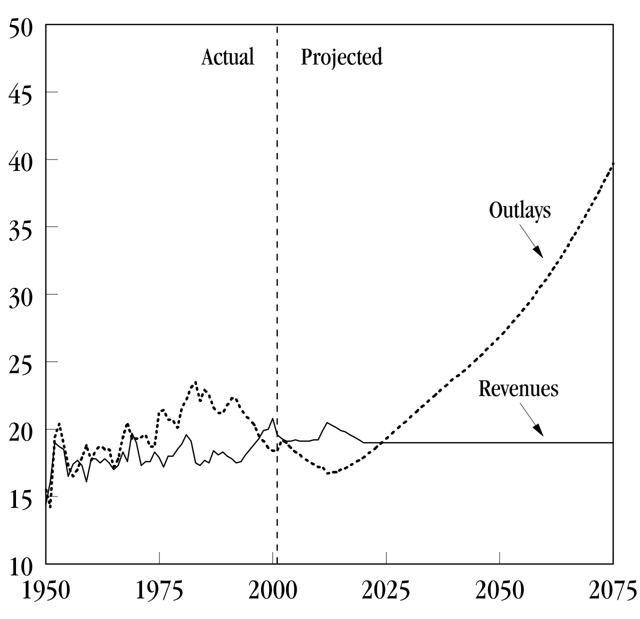
World War II period. The core costs of the federal government—that is, ignoring net interest on the debt—could rise from approximately 18 percent of GDP today to 24 percent in 2050 and 28 percent in 2075. Left unattended, that steady escalation in spending could cause major deficits to emerge and thereby push the government's debt and interest expenditures to unprecedented levels. The total cost of government, including interest expense, could more than double as a share of the economy, rising from 19 percent of GDP today to 40 percent in 2075 (*see Figure 3 and Table 3*).

Certainly, the long-range outlook presented here is subject to change, as the underlying economic and demographic factors will undoubtedly vary from the assumptions used. However, the Congress can alter it as well by legislating changes in the policies that drive the numbers. ■

Figure 3.

Federal Revenues, Outlays, Deficits, and Surpluses, 1950 to 2075

(As a percentage of GDP)



Source: Congressional Budget Office.

Table 3.

Federal Revenues, Outlays, Deficits, and Surpluses, 1950 to 2075

(As a percentage of GDP)

Fiscal Year	Revenues	Total Outlays	Budget Deficit (-) or Surplus
1950	14.4	15.6	-1.1
1960	17.8	17.7	0.1
1970	19.0	19.3	-0.3
1980	18.9	21.6	-2.7
1990	18.0	21.8	-3.9
2000	20.8	18.4	2.4
2010	19.2	17.2	2.0
2020	19.0	17.9	1.1
2030	19.0	20.8	-1.8
2040	19.0	23.8	-4.8
2050	19.0	26.9	-7.9
2060	19.0	31.0	-12.0
2070	19.0	36.5	-17.5
2075	19.0	39.7	-20.7

Source: Congressional Budget Office.

Note: Numbers in the tables and text may not add up to totals because of rounding.

Related CBO Publication: *Social Security: A Primer* (September 2001).

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