



# Congressional Budget Office

## Choices for Federal Spending and Taxes

Presentation at the University of Michigan

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Director

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# Five Key Questions

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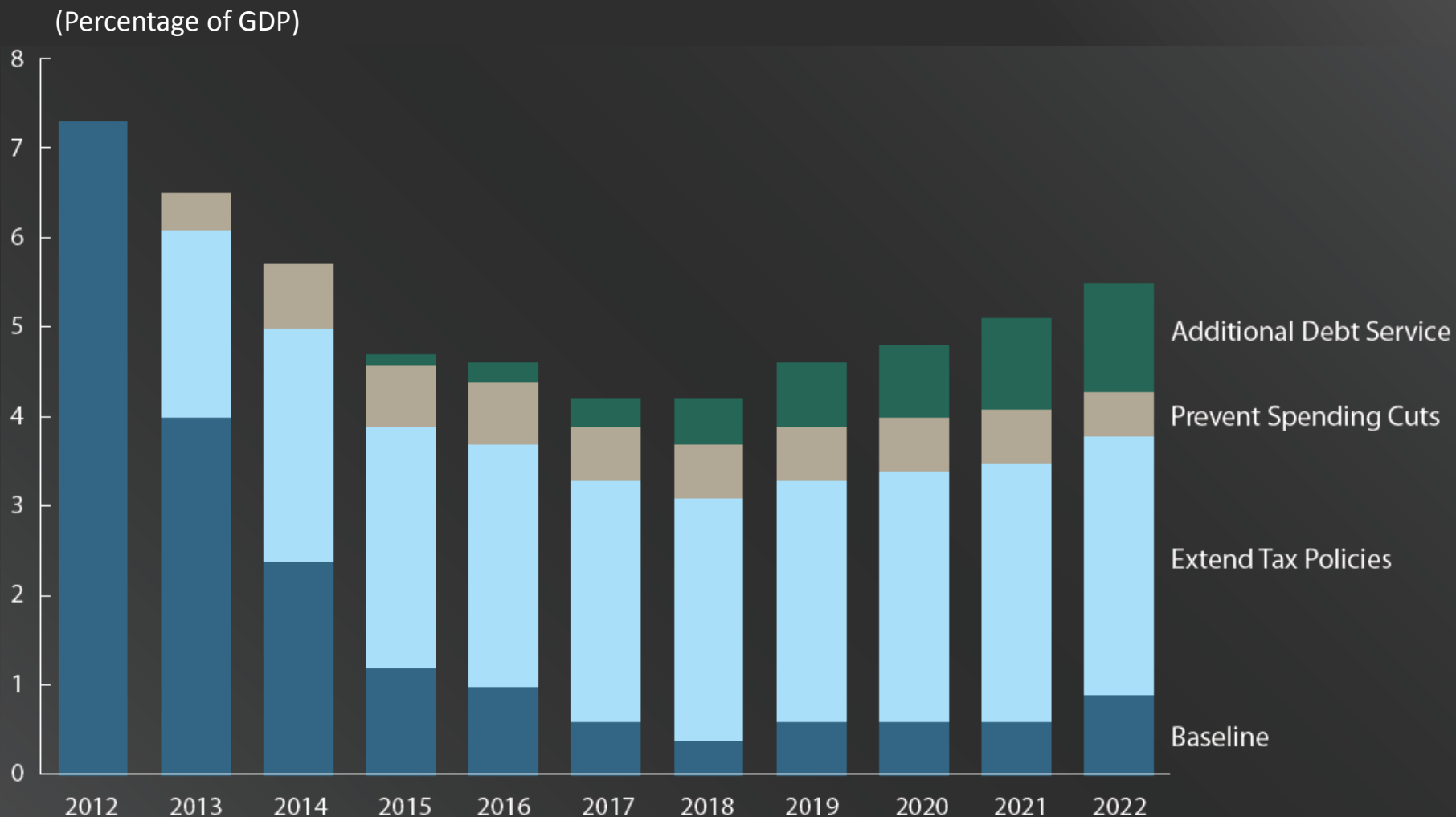
- 1) How Big Are Projected Federal Deficits and Debt?**
- 2) What Factors Are Putting Increasing Pressure on the Budget?**
- 3) What Are the Consequences of Rising Federal Debt?**
- 4) What Kinds of Policy Changes Could Lead to a More Sustainable Budgetary Path?**
- 5) What Criteria Might Be Used to Evaluate Policy Changes?**

# Question #1

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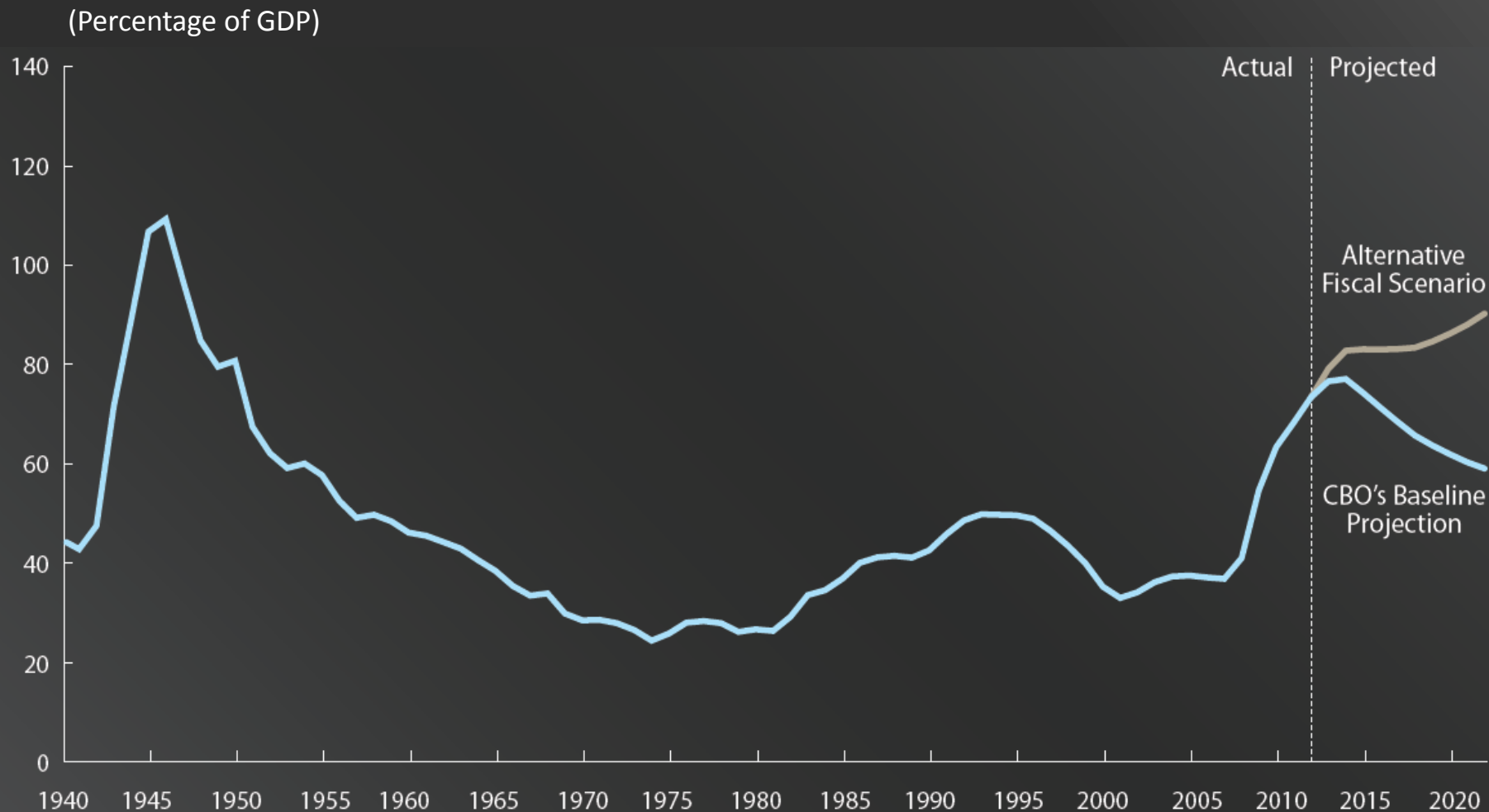
**How Big Are Projected Federal Deficits and Debt?**

# Deficits Projected in CBO's Baseline and Under An Alternative Fiscal Scenario



Estimates from *An Update to the Budget and Economic Outlook: Fiscal Years 2012 to 2022* (August 2012).

# Federal Debt Held by the Public, Historically and As Projected in CBO's Baseline and Under an Alternative Fiscal Scenario



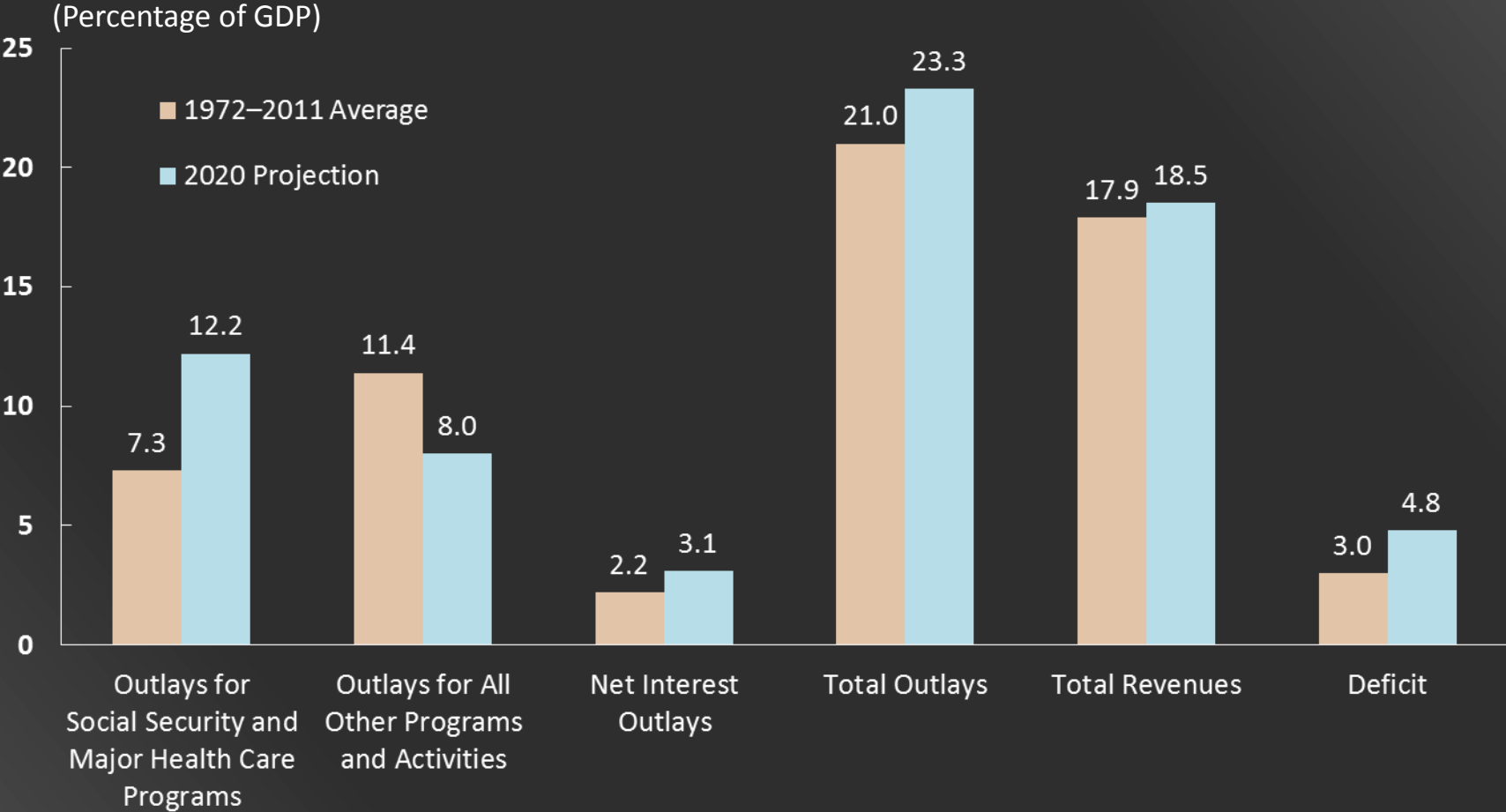
Estimates from *An Update to the Budget and Economic Outlook: Fiscal Years 2012 to 2022* (August 2012).

# Question #2

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**What Factors Are Putting Increasing Pressure on the Budget?**

# Components of the Federal Budget in 2020 Under the Alternative Fiscal Scenario, Compared with Their Averages Since 1972



Estimates from *An Update to the Budget and Economic Outlook: Fiscal Years 2012 to 2022* (August 2012).

# We Cannot Go Back to the Past Combination of Tax and Spending Policies

Existing federal programs are becoming much more expensive because of:

- The aging of the population, and
- Rising costs for health care.

As a result of those factors and others, outlays for Social Security and the major federal health care programs are projected to total 12.2 percent of GDP in 2020 under the alternative fiscal scenario, compared with an average of 7.3 percent over the past 40 years.



# Question #3

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**What Are the Consequences of Rising Federal Debt?**

# Rising Federal Debt Would Have Significant Harmful Consequences for the Federal Budget and the Economy

- Higher interest payments on federal debt.
- A reduction in national saving.
- Limits on policymakers' ability to use tax and spending policies to respond to unexpected challenges, such as economic downturns or financial crises.
- An increase in the likelihood of a fiscal crisis.

# Question #4

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**What Kinds of Policy Changes Could Lead to a More Sustainable Budgetary Path?**

# Three Possible Goals For Deficit Reduction in 2020

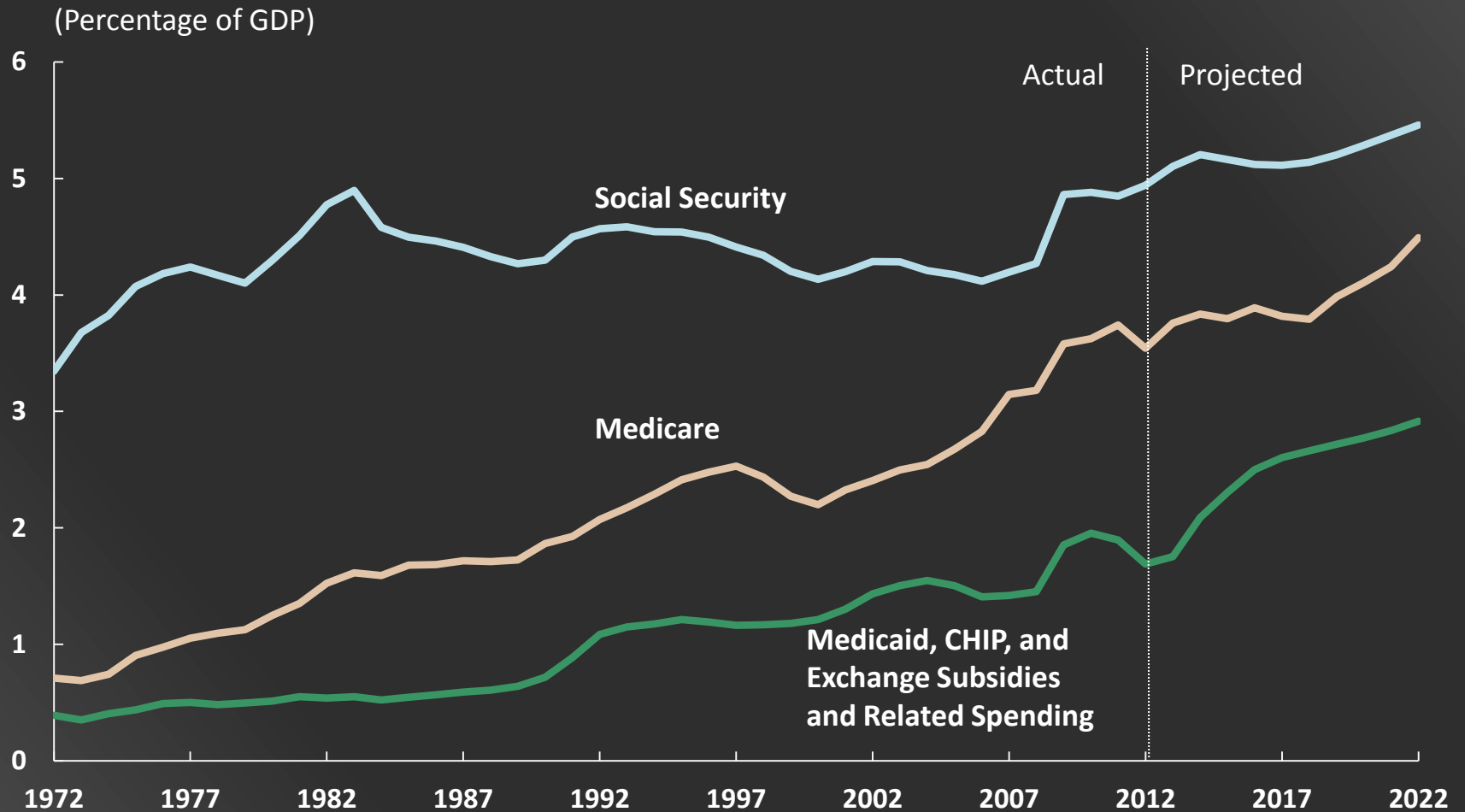
Approximate Amount of Deficit Reduction in 2020 (relative to AFS)	Impact on Budget Outcomes
\$1 Trillion	Balance the budget by 2020; debt would be on a steadily declining path relative to GDP.
\$750 Billion	Starting from the AFS, return roughly to deficits and debt under the baseline; debt would be on a slightly downward-sloping trajectory relative to GDP.
\$500 Billion	Debt would be no larger a percentage of GDP at the end of 2020 than it is projected to be at the end of 2013 under the alternative fiscal scenario (about 79 percent).

# Three Broad Categories of Changes

Putting the federal budget on a path that is more likely to be sustainable than what would occur if current policies were continued will require the United States to change those policies in at least one of the following ways:

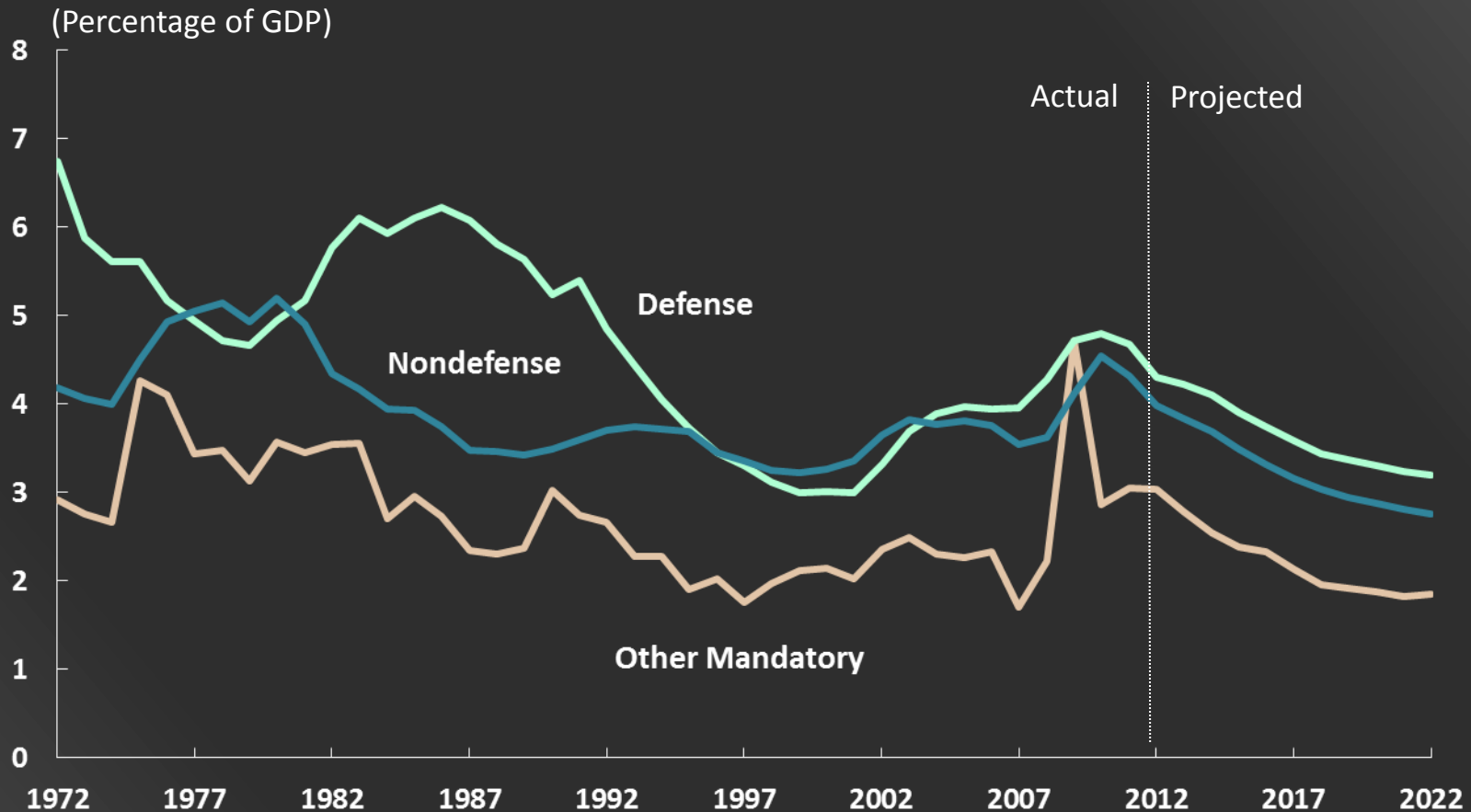
- Make major reductions (relative to current policies) in the benefits that people receive when they get older,
- Substantially reduce the role of the rest of the federal government (relative to the size of the economy) beyond the reductions that are already projected to occur, or
- Raise revenues significantly above their historical average as a percentage of GDP.

# Spending on Social Security and Major Federal Health Care Programs, Historically and Under the Alternative Fiscal Scenario



Estimates from *An Update to the Budget and Economic Outlook: Fiscal Years 2012 to 2022 (August 2012)*.

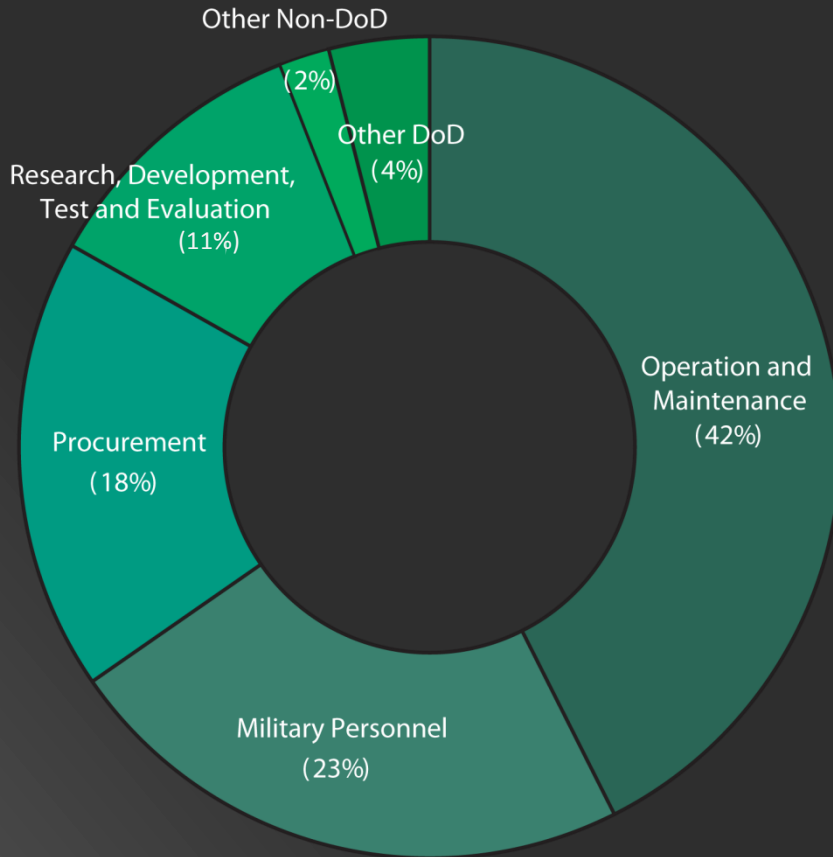
# Discretionary and “Other Mandatory” Spending, Historically and Under the Alternative Fiscal Scenario



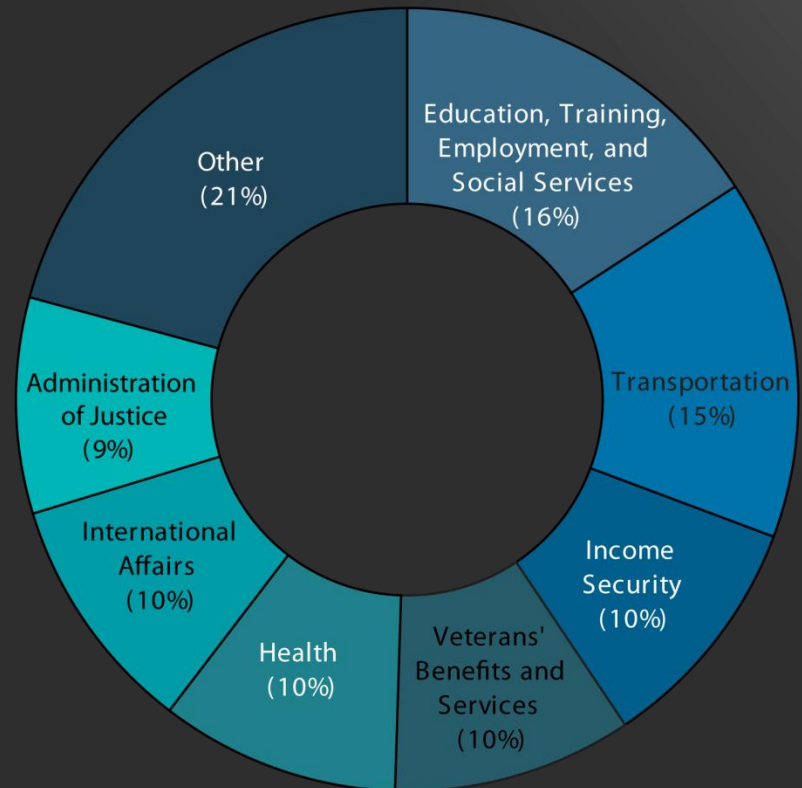
Estimates from *An Update to the Budget and Economic Outlook: Fiscal Years 2012 to 2022 (August 2012)*. “Other Mandatory” includes programs designed to provide income security, such as the Supplemental Nutrition Assistance Program and unemployment compensation; retirement benefits for civilian and military federal employees; benefits for veterans; support for agriculture; and other activities. Estimates incorporate the assumption that the automatic spending reductions required by the Budget Control Act do not take effect, although the original caps on discretionary appropriations remain in place and are met through proportional reductions in defense and nondefense discretionary budget authority.

# Discretionary Funding for 2012: \$1,251 Billion

## Defense \$670 Billion

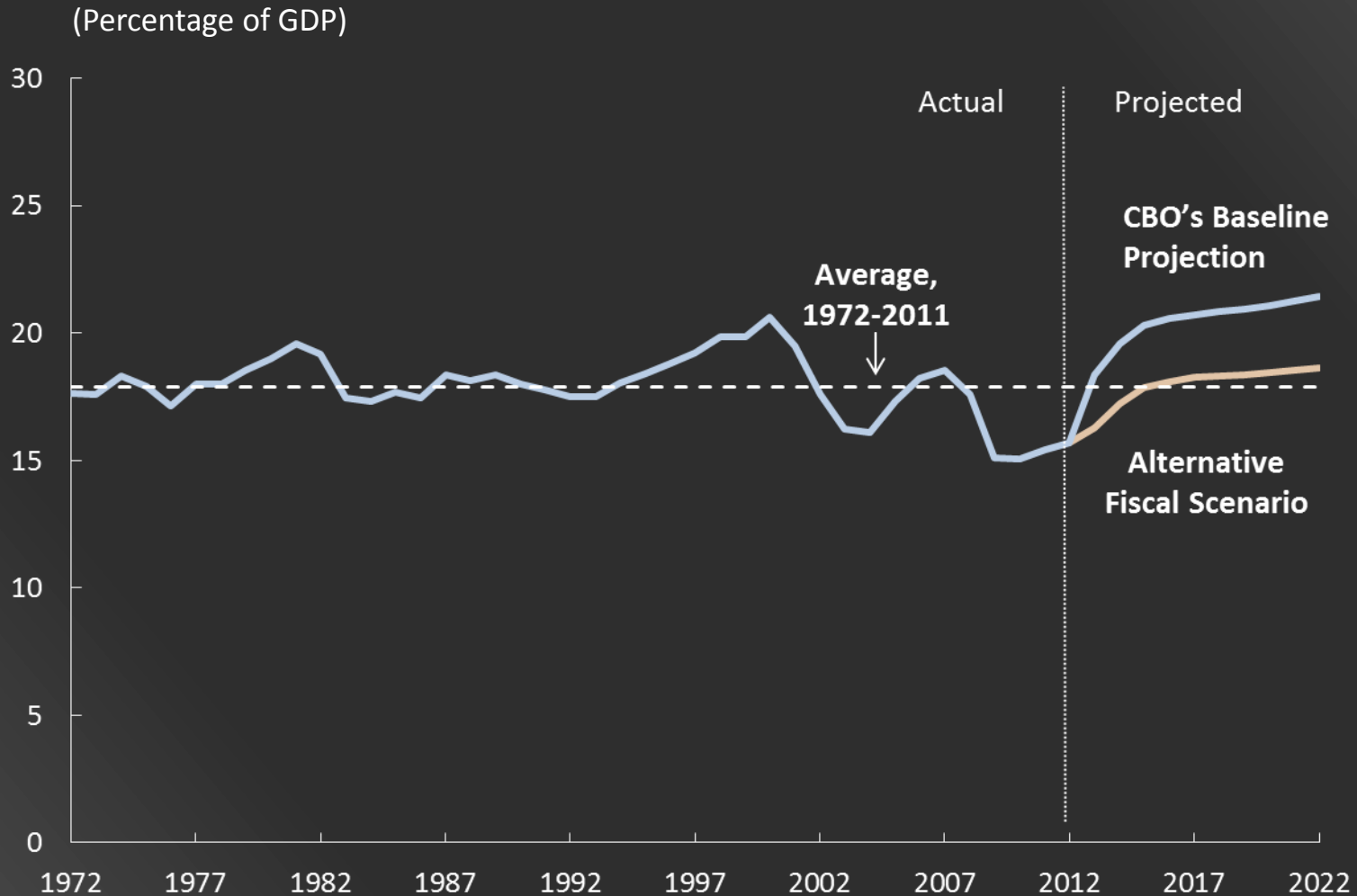


## Nondefense \$581 Billion



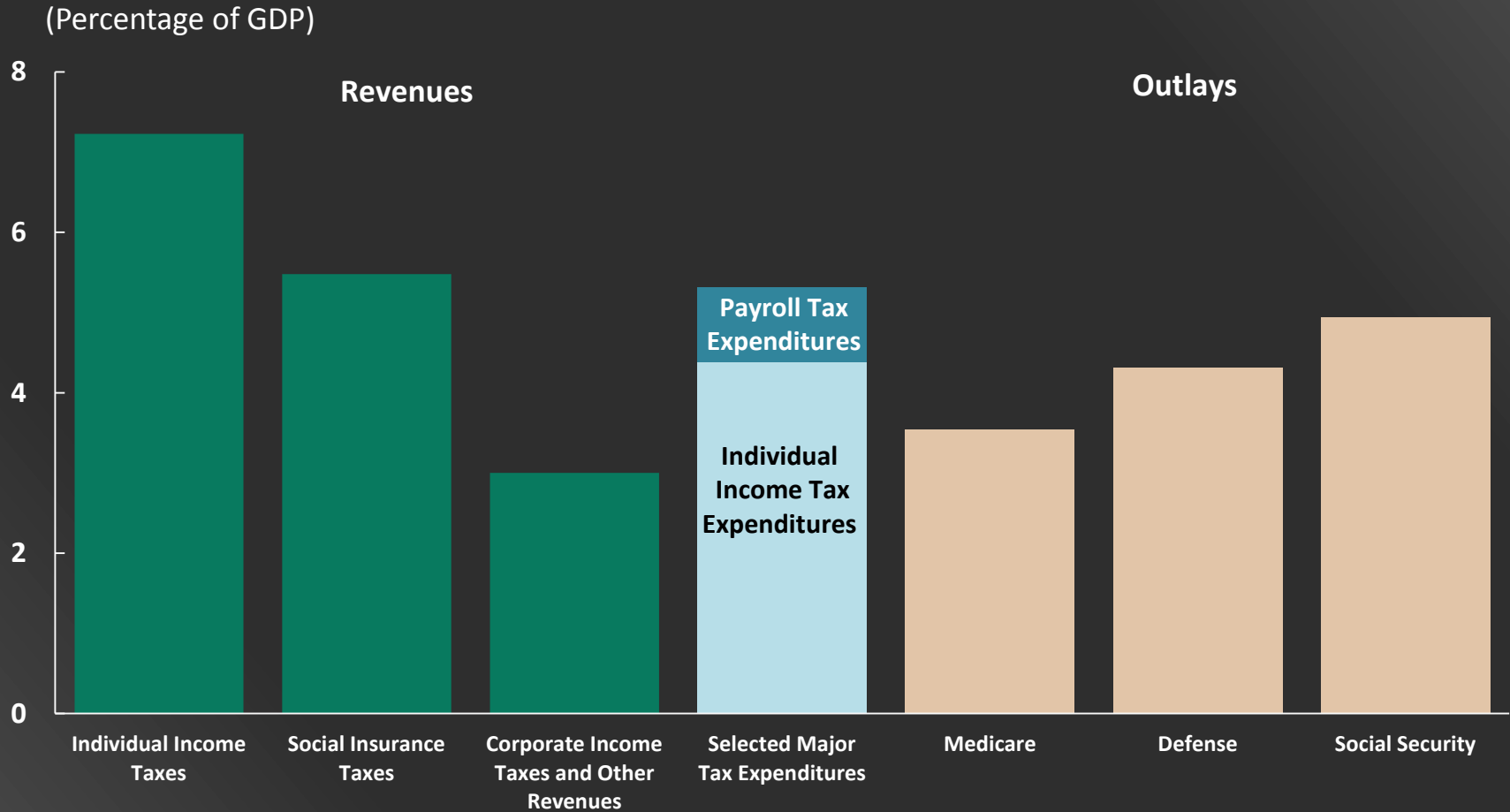


# Revenues Projected in CBO's Baseline and Under the Alternative Fiscal Scenario



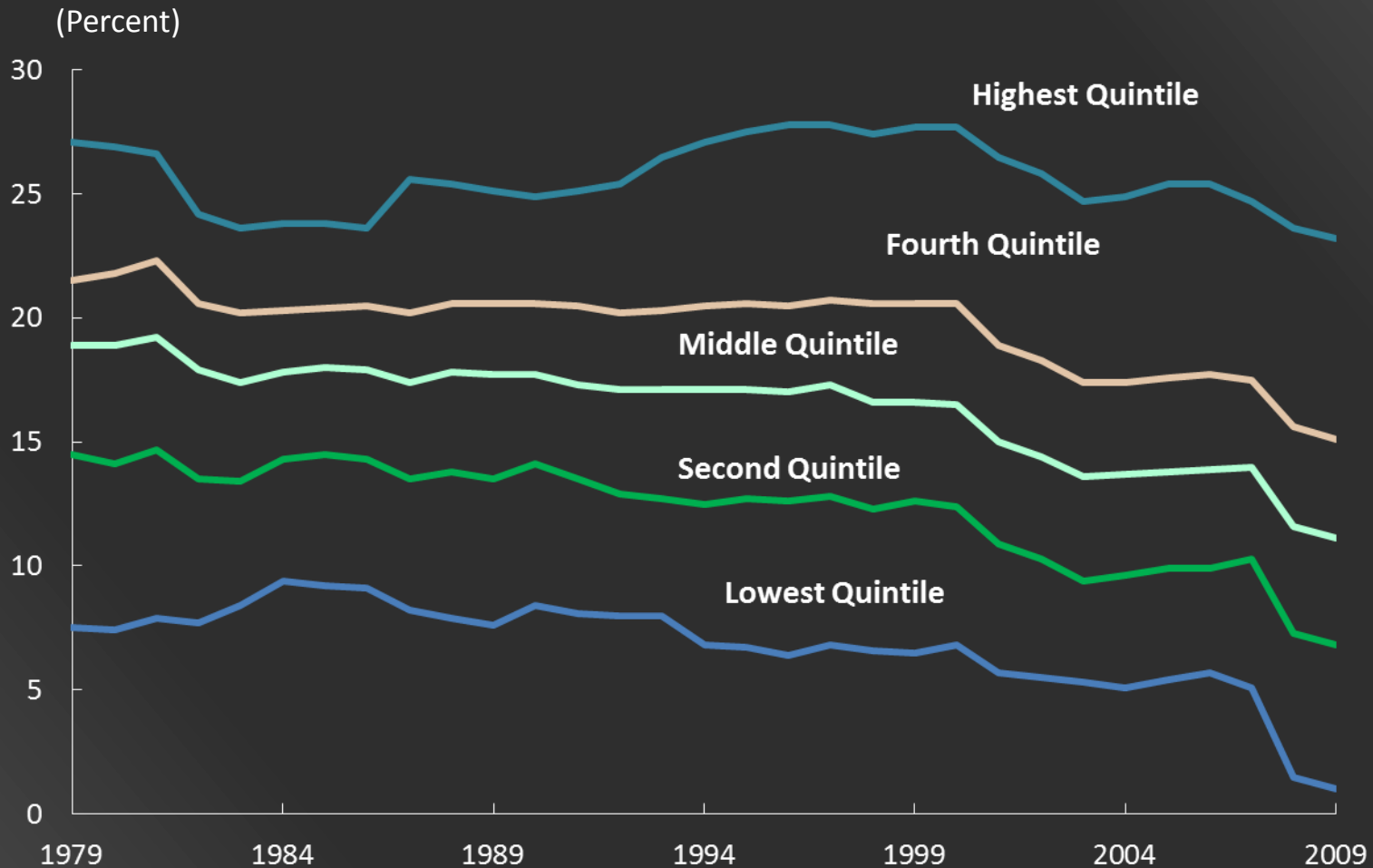
Estimates from *An Update to the Budget and Economic Outlook: Fiscal Years 2012 to 2022* (August 2012).

# Selected Major Tax Expenditures in 2012, Compared with Other Categories of Revenues and Outlays



Estimates of revenues and outlays from *An Update to the Budget and Economic Outlook: Fiscal Years 2012 to 2022 (August 2012)*. Estimates of tax expenditures based on estimates by the staff of the Joint Committee on Taxation and included in *The Budget and Economic Outlook: Fiscal Years 2012 to 2022 (January 2012)*.

# Total Average Federal Tax Rates for All Households, by Before-Tax Income Group, 1979 to 2009



Data from *The Distribution of Household Income and Average Federal Tax Rates, 2008 and 2009*.

# Question #5

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**What Criteria Might Be Used to Evaluate Policy Changes?**

# Determining What Combination of Policies to Pursue Is Challenging and Many Factors May Play a Role

- How big would the government be?
- How would the government's resources be allocated among various priorities?
- How much would deficits be reduced in the next 10 years and beyond?
- What would the economic impact be in the short term and over the long term?
- Who would bear the burden of the proposed changes in tax and spending policies?

# Conclusion

## To put the budget on a path...

...that is more likely to be sustainable than what would occur if current policies were continued, lawmakers will need to adopt a combination of policies that will require people to pay more for their government, accept less in government benefits and services, or both. However, achieving the amount of deficit reduction necessary to shrink the debt relative to the size of the economy—or even to keep the debt from growing—will be a formidable task.