FACT SHEET
CBO BUDGET OUTLOOK
FY 2008-2018

PREPARED BY: MAJORITY STAFF, SENATE BUDGET COMMITTEE
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CBO Budget Outlook Shows Higher Deficit in 2008; Bleak Long-Term Picture Remains Unchanged

The Congressional Budget Office's (CBO) January Budget and Economic Outlook shows that the deficit will worsen in 2008. This short-term deterioration is due, at least in part, to the slowing economy. Moreover, the CBO baseline projection of $219 billion actually understates the likely deficit in 2008, because it excludes expected costs such as an economic stimulus package and the additional war funding requested by President Bush. <u>Once these costs are added in, the deficit in 2008 is likely to exceed $350 billion, and the debt is likely to increase by over $600 billion</u>.

CBO's ten-year projections show an explosion in federal deficits and debt if we continue to follow the President's deficit-financed tax and spending policies. Once the on-going cost of the war in Iraq and Afghanistan and the extension of expiring tax cuts, including AMT relief, are factored in, CBO projections show the continuation of significant deficits. By 2013, the deficit would reach $450 billion under the President's policies. These deficits would be occurring at the worst possible time – just as the baby boom generation begins to retire. Over the long-term, CBO analyses have detailed the enormous challenges we face as rising health care and retirement costs overwhelm the budget.

Deficits, debt, and decline are the unfortunate legacy of this Administration. This legacy reduces our flexibility as we work to address the current economic slowdown. The CBO forecast reinforces how vital it is that, in developing a package to boost the economy in the short-term, we do nothing to worsen the already unsustainable long-term budget outlook. In fact, the best route to restore confidence in the economy is both to enact a carefully-crafted, quickly-timed, and temporary stimulus package, and to begin the process of tackling our long-term fiscal challenges.

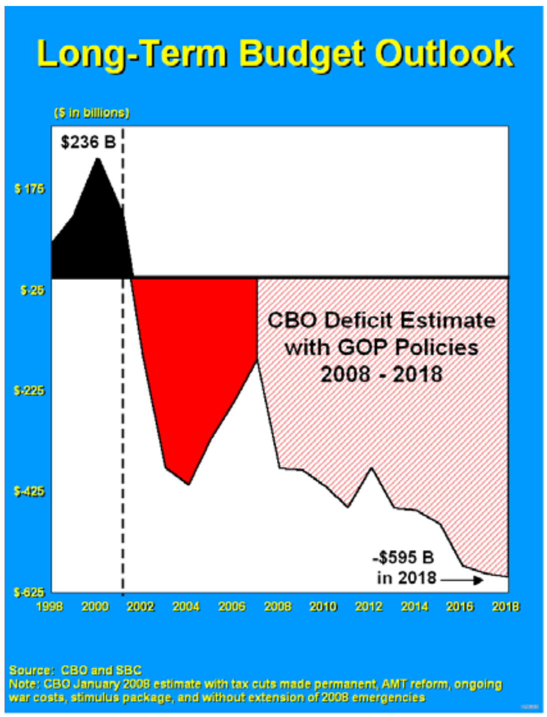
Continuation of GOP policies leads to large deficits. The official CBO estimates of the budget baseline understate likely deficits over the next decade, because CBO must calculate these estimates under a strict set of guidelines. For example, CBO assumes that all expiring tax cuts do in fact expire and that relief from the Alternative Minimum Tax (AMT) is not provided after 2007. Similarly, the projections do not include the additional $105 billion in supplemental funding for operations in Iraq and Afghanistan requested by the President. A far different picture emerges when we adjust the CBO baseline estimates for policies that are key components of the President's agenda.

Specifically, after adjusting the CBO baseline by removing the $1.2 trillion cost of extending the defense and non-contingent nondefense emergency funding provided in 2008, we can then add in the cost of:

- making the Bush tax cuts and other expiring tax cuts permanent ($2.7 trillion);
- extending AMT relief ($1.3 trillion);
- funding ongoing military operations in Iraq and the war on terrorism ($1.0 trillion); and,
- the debt service associated with these policy adjustments[1] ($1.2 trillion).

These adjustments add $6.3 trillion to the ten-year CBO projection, for a total deficit of $4.8 trillion over the decade. (see table on page 5)

These estimates show that the modest decline in the deficit that we have seen over the past few years would be reversed, and that deficits would rise again throughout the decade under the President's policies. Deficits would exceed $450 billion in 2013 and approach $600 billion by 2018 under this scenario.



Growth in federal debt far greater than deficits. The deficits we face this decade don't tell the whole story about the nation's finances and our growing debt burden. The debt is mounting far more rapidly than the deficit figures indicate, because they hide the fact that we are borrowing from Social Security, which is temporarily in surplus, and from the other trust funds.

For example, in 2008, the federal government is expected to borrow $197 billion from Social Security alone and another $65 billion primarily from Medicare and other trust funds. So while the deficit is estimated to increase by $379 billion in 2008, the gross debt is estimated to increase by $641 billion.

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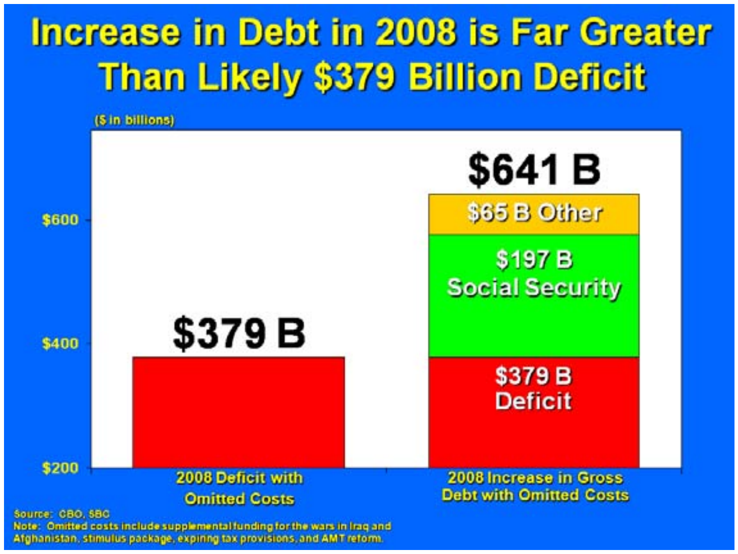
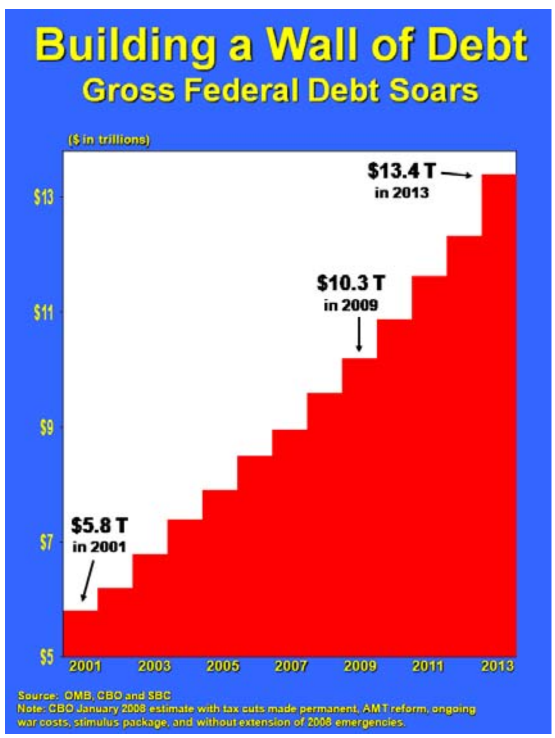
[1]Also includes debt service associated with a 2008 stimulus package costing $145 billion.



Bush policies add to the wall of debt. Under President Bush, gross federal debt has climbed from $5.8 trillion at the end of 2001 to an estimated $10.3 trillion at the end of 2009, the President's final year in office. Under the policies reflected in the adjusted CBO projections, the country's total debt would soar to $13.4 trillion by 2013. At a time when we should be paying down debt to prepare for the coming retirement of the baby boom generation, the President's policies have instead dramatically increased our debt and worsened our long-term outlook.



The explosion of debt is also a concern because we are becoming increasingly reliant on foreigners to buy our debt and finance our deficits. We now owe Japan almost $600 billion; China almost $400 billion; the United Kingdom more than $300 billion; and "oil exporters" more than $100 billion. It took 42 Presidents 224 years to run up a trillion dollars of external debt. Incredibly, President Bush has more than doubled that amount.

Stimulus and the Long-Term Outlook. The new CBO forecast helps to frame the current debate in Congress on how to provide effective stimulus to the economy. It makes clear that whatever steps we take in the short-run to boost the economy should not worsen the budget situation over the long-run. This point was also made by Federal Reserve Chairman Ben Bernanke in testimony before the House Budget Committee:

> *"[A]ny program should be explicitly temporary, both to avoid unwanted stimulus beyond the near-term horizon and, importantly, to preclude any increase in the federal government's structural budget deficit....A fiscal initiative at this juncture could prove quite counterproductive, if, for example, it provided economic stimulus at the wrong time or compromised fiscal discipline in the longer term."*

In its recent report "Options for Responding to Short-term Economic Weakness," CBO argues that, to be most effective, a timely and temporary stimulus package should consist of policies that increase economic activity the most for a given budgetary cost. CBO examined the latest economic research on the effects of alternative approaches to stimulus and its findings echo the consensus view among economists that the most effective policies for short-term stimulus are those that direct money to people likely to spend most of the federal assistance quickly, typically low- and moderate-income households.

Among the options examined in the report, CBO finds that increasing direct transfer payments to households – such as through Unemployment Insurance or Food Stamps – and some types of temporary tax relief – such as a refundable, lump-sum tax rebate – are policies most likely to provide timely and temporary stimulus that could boost overall demand substantially. Incentives for new business investment are likely to be less effective forms of stimulus. Experience has shown that businesses do not have the flexibility to adjust their investment plans quickly enough to take advantage of short-term incentives. CBO lists a number of stimulus options that are likely to be least effective: an across-the-board income tax cut (wealthier taxpayers are less likely to spend it) and a cut in corporate tax rates. Finally, extending the 2001 and 2003 Bush tax cuts set to expire in 2011 is not likely to have any effect on short-term demand this year, according to CBO.

Conclusion. The nation faces significant challenges in both the short-term and long-term. We are bearing the burden of the Bush Administration's fiscal policies, with its massive build-up of debt, which has occurred at the worst time, as the baby boomers prepare to retire.

Getting stimulus into the economy as quickly as possible is a crucial concern. As long as the stimulus measures are timely, temporary, and well-targeted, we can boost the economy without worsening our structural deficit or undermining our commitment to fiscal discipline. But to restore confidence in the economy, we should also begin to tackle our long-term problems. The American people expect that we will make the tough choices to put our fiscal house back in order.

CBO January 2008 Baseline Deficits With GOP Policies

($ billions)	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2009-18
CBO January 2008 Baseline	**-219**	**-198**	**-241**	**-117**	**87**	**61**	**96**	**117**	**95**	**151**	**223**	**274**
Do not extend 2008 emergencies	--	43	80	102	116	126	135	144	153	163	173	1,234
CBO Jan. without emergencies	**-219**	**-155**	**-161**	**-15**	**203**	**187**	**231**	**261**	**248**	**313**	**395**	**1,507**
Extension of tax cuts and other expiring tax provisions	-6	-17	-28	-178	-292	-325	-341	-357	-373	-392	-412	-2,716
AMT reform	-6	-75	-76	-89	-103	-118	-134	-151	-170	-191	-215	-1,322
Ongoing war costs	-30	-96	-128	-135	-120	-107	-93	-81	-79	-79	-79	-996
Economic stimulus	-116	-29	--	--	--	--	--	--	--	--	--	-29
Debt service on adjustments	-2	-10	-23	-40	-65	-94	-126	-161	-198	-239	-284	-1,240
CBO January with GOP policies	**-379**	**-382**	**-415**	**-457**	**-377**	**-458**	**-463**	**-489**	**-573**	**-588**	**-595**	**-4,796**
Increase in Gross Debt	**641**	**682**	**739**	**795**	**750**	**823**	**836**	**866**	**933**	**953**	**965**	**--**

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