

WNTS Insight

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New CBO data project reduced deficits, sluggish growth

The Congressional Budget Office (CBO) has released updated economic and budget projections for federal fiscal years 2012-2021, incorporating the recently enacted Budget Control Act of 2011. As a result of that legislation, the 10-year cumulative deficit is estimated to decline by \$2.1 trillion to \$3.5 trillion. Annual deficits under CBO's "baseline" would decline below 2 percent of gross domestic product (GDP) by 2014 and stay low through the remainder of the 10-year period. However, alternative projections assuming different policies -- including failure to adhere to the spending caps in the Budget Control Act and extension of expiring individual income tax relief -- would result in significant deficits throughout the 10-year period.

Budget Projections

The federal budget deficit is estimated to reach \$1.3 trillion in fiscal year 2011, or 8.5 percent of GDP. In March CBO estimated a FY 2011 budget deficit that was more than \$100 billion higher, or \$1.4 trillion.

Beyond 2011, the enactment of the Budget Control Act results in a significant reduction in projected deficits. Annual deficits are projected to decline under the CBO baseline to 3.2 percent of GDP in 2013, 1.6 percent in 2014, and 1.2 percent in 2021.

The CBO baseline assumes continuation of current law. Under this baseline, which assumes that the individual income tax relief enacted in 2001 and 2003 expires as scheduled along with other expiring tax provisions, revenues would climb steadily over the projection period, from 15.3 percent of GDP in 2011 to 20.9 percent in 2021, well above the historical average of 18 percent.

CBO presents alternative projections assuming changes from current law with respect to certain policies. For example, extension of the 2001/2003 individual



income tax relief and indexation of the individual alternative minimum tax are estimated to increase the 10-year cumulative deficit by \$4.6 trillion. Holding discretionary spending constant as a share of GDP -- in contrast to the reductions legislated as part of the Budget Control Act -- would increase the 10-year deficit by \$2.8 trillion. A phase-down of military operations in Iraq and Afghanistan would reduce the 10-year deficit by \$1.3 trillion.

Economic Outlook

Although CBO's economic projections were made in early July and do not incorporate more recent signs of economic weakness, CBO's projections assume sluggish economic growth over the next two years.

- Real GDP growth projections were revised downward for 2011, 2012, and 2013, to 2.4 percent, 2.6 percent, and 1.7 percent, respectively. CBO assumes that expiration of the 2001 and 2003 tax cuts and the spending cuts under the Budget Control Act will reduce growth in 2013. In later years, economic growth is assumed to be higher as the economy recovers and government borrowing is reduced.
- CBO expects the unemployment rate to remain high, falling slightly to 8.9 percent by the end of 2011 and 8.5 percent by the end of 2012. The rate is projected to fall slowly in later years and reach its long-run level of 5.2 percent by 2017.
- Interest rates and inflation are expected to remain low.

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