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OFFICIAL FACTS CONTRADICT ADMINISTRATION STATEMENTS: DECLINE IN 2004 DEFICIT ESTIMATE IS NOT DUE TO FASTER ECONOMIC GROWTH

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On September 7, the Congressional Budget Office released a report estimating that the budget deficit will equal \$422 billion in fiscal year 2004. Although this is \$46 billion larger than the deficit in 2003, the increase in the deficit is smaller than had been projected earlier in the year, when CBO estimated the 2004 deficit would hit \$477 billion. This led Vice President Cheney to declare, in referring to the fact that the \$422 billion deficit is smaller than was projected earlier, “That’s a direct result of economic growth that came about as a result of the tax changes that the President put through, and the Congress supported.”¹ Numerous Republican lawmakers and others associated with the Administration issued similar statements, implying that economic growth has been faster than expected. In addition, some press stories reported as fact, without attributing it to the Vice President or other officials, the claim that the change in estimates is due to a stronger economy.

But the Vice President’s statement is demonstrably incorrect. This is not a matter of debate or interpretation; it is a simple matter of fact. Overall economic growth has been equal to what CBO expected when it issued its \$477 billion deficit estimate earlier this year. Since economic growth was the same — not faster — as earlier projected, the higher-than-expected revenues cannot have resulted from faster growth.

- **Over the first three quarters of fiscal year 2004, economic equaled what CBO forecast in January.** Commerce Department data show that the real gross domestic product — the overall measure of the state of the economy — was 4.8 percent larger in the first three quarters of this fiscal year than in the same period last year. In other words, real GDP growth equaled 4.7 percent over this period. In issuing its higher deficit estimates earlier in the year, CBO projected that the economy would grow by 4.8 percent over this period.
- **CBO has marginally *lowered* its expectations of economic growth over the full fiscal year.** CBO now expects the economy to grow 4.6 percent over fiscal year 2004, after adjusting for inflation. (This is shown in Appendix Table C-2 of the updated “Budget and Economic Outlook.”) This growth rate is revised slightly downward from CBO’s earlier projection of 4.7 percent growth for the fiscal year. (That projection can be found in Table E-3 of CBO’s January “Budget and Economic Outlook”).

¹ Vice President Dick Cheney, quoted in Edmund L. Andrews, “Deficit Analysis and Bush Differ: Budget Agency Calculates Smaller 5-Year Decline,” *The New York Times*, September 8, 2004, p. A1.

CBO does expect that revenues will be \$54 billion higher in fiscal year 2004 than it had projected earlier in the year, and this difference accounts for virtually all of CBO's downward re-estimate of the 2004 deficit. But, as noted, the increased revenues are not due to faster economic growth. In fact, it appears that part of the increase in the revenues may be due to *adverse* economic developments. Factors that help to explain the higher-than-expected revenues include the following:

- According to CBO, the Treasury received an additional \$30 billion as a result of taxpayers receiving smaller refunds and making larger tax payments this year when they filed their 2003 income tax returns than the Treasury had expected. This \$30 billion in additional revenue comes from 2003 tax returns; essentially none of this can be attributed to unexpected economic growth since CBO issued its earlier forecast.
- Inflation has increased, and that tends to push up revenue collections. Over the first three quarters of the fiscal year, inflation has proceeded at a 3.0 percent annual pace. Last spring, CBO expected inflation to proceed at a 1.5 percent annual pace over this period.
- High-income individuals and corporations may be receiving a greater share of the income in the nation than previously anticipated, with ordinary workers receiving a smaller share. The federal tax system collects a higher percentage of income from high-income households than from typical workers. As a result, increases in income disparities tend to produce increased federal revenues.

Trends in tax receipts provide some evidence that such a widening of income disparities has been occurring. So far in 2004, personal income tax receipts have been modestly higher than expected and corporate tax revenues have enjoyed an unanticipated increase (although they remain well below their historical norm). At the same time, payroll tax receipts, which come disproportionately from the wages and salaries of ordinary workers, appear to be *lower* than CBO had anticipated. Income tax revenues come in higher, and payroll tax revenues lower, when income disparities widen.

Such trends would result in higher-than-expected revenue intake. CBO does not yet have enough data to know exactly why revenues are higher than expected, and other factors also may help explain the revenue increase. But faster-than-expected overall economic growth is clearly not among them.