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BASIC QUESTIONS AND ANSWERS ABOUT THE DEFICIT

1. How big is the deficit?

- In fiscal year 2006, which ended October 1, the federal deficit was $248 billion, meaning the government spent $248 billion — or 10 percent — more than it collected that year.
- Put another way, this means that for every $10 of taxes the U.S. government collected last year, it spent $11 to support federal programs (such as Social Security, Medicare, defense, and education) and to pay interest on past borrowing.
- A deficit of $248 billion works out to about $825 per American.

For more information, click here. [http://www.cbpp.org/10-11-06bud.htm]

2. Is the deficit getting better or worse?

Some have claimed that the deficit is improving because the final deficit figure for 2006 ($248 billion) was substantially lower than deficit estimates made earlier in the year. However, the latest projections from the nonpartisan Congressional Budget Office show that the deficit will remain high over the next decade, averaging $350 billion per year, if the tax cuts enacted since 2001 and measures to protect the middle class from the Alternative Minimum Tax are extended. (The tax cuts are scheduled to expire by the end of 2010.)

Since 2000, the budget has undergone virtually its largest six-year deterioration in the past half-century, from a *surplus* equal to 2.4 percent of the Gross Domestic Product in fiscal year 2000 to a *deficit* of 1.9 percent of GDP in 2006.*

For more information, click here. [http://www.cbpp.org/10-11-06bud.htm]

3. What caused today's deficits?

Some have argued that the emergence of deficits was largely due to the 2001 economic downturn. Congressional Budget Office figures show, however, that new tax cuts and spending increases approved by Congress since 2001 were a much bigger cause, accounting for nearly two-

* The only six-year period in the past half-century that experienced a worse budget deterioration was 1998-2004, and the single largest cause of the 1998-2004 and 2000-2006 deteriorations was the same: the recent tax cuts (see question 3).

thirds of the budgetary deterioration that occurred over the 2001-2006 period.

Others have blamed the emergence of deficits on increases in domestic spending. But between 2001 and 2006, increases in domestic spending account for just 16 percent of the cost of the legislation Congress enacted during that period. Tax cuts and increases in defense, homeland security, and other international spending account for the other 84 percent.

In fact, between 2001 and 2006, tax cuts alone account for fully half of the total cost of legislation enacted by Congress during that period, making them single largest contributor to the emergence of deficits.

For more information, click here. [http://www.cbpp.org/9-27-06tax.htm]

4. What impact do tax cuts have on the deficit?

Some have claimed that tax cuts "pay for themselves" — in other words, the economy expands so much as a result of tax cuts that it produces the same level of revenue as it would have *without* the tax cuts. However, a recent analysis by the Treasury Department confirms what other analysts have long said: tax cuts don't come close to paying for themselves.

The Treasury analysis found that if the costs of extending the Administration's tax cuts are not offset by spending reductions, extending the tax cuts would slightly *decrease* long-run economic growth. Even if the costs of extending the tax cuts are offset by spending cuts, the Treasury study found the tax cuts would at best have only small positive effects on the economy, which would pay for at most 10 percent of the tax cuts' total cost. (The tax cuts have so far been financed by deficits, and supporters have offered no proposals to offset the cost of extending them.)

It's worth noting that the federal budget would have been balanced last year if not for the revenue loss caused by the tax cuts. In fiscal year 2006, the tax cuts enacted since 2001 cost $251 billion, including the increased interest payments on the national debt, according to Congressional Budget Office estimates. This is slightly more than the 2006 deficit ($248 billion).

This means that even with the spending for the wars in Iraq and Afghanistan and the response to Hurricane Katrina, the federal budget would have been in balance last year if the tax cuts had not been enacted, or if they had been offset by increases in other taxes or by cuts in programs.

For more information, click here [http://www.cbpp.org/7-27-06tax.htm]

5. Has Congress cut spending to shrink the deficit?

The 109th Congress reduced funding for domestic programs through 2011 by a total of $75 billion. But Congress also enacted new tax cuts that will cost $116 billion over that period, as well as $489 billion in "emergency" funding for Iraq, Afghanistan, the war on terror, and the response to Hurricane Katrina and other natural disasters.

The net effect of these actions will be to make deficits $535 billion *larger* through 2011 than they otherwise would be. Put another way, the 109th Congress and the President took our already large projected budget deficits and enacted legislation that will make them larger.

For more information, click here. [http://www.cbpp.org/policy-points9-29-06.htm]

6. What is the long-term forecast for the deficit?

The budget outlook for the next decade is bleak. As noted above, the nonpartisan Congressional Budget Office projections show that if the President's tax cuts are made permanent and relief from the Alternative Minimum Tax is extended, deficits will average about $350 billion a year for the next ten years (2007-2016), even if the costs of the wars in Iraq and Afghanistan decline substantially in a few years.

The outlook for later decades is even more sobering. As the baby boomers retire and health-care costs continue to rise, the combination of those effects and the President's tax cuts (if they are made permanent) would cause the deficit to explode. That, in turn, would drive the national debt — already close to $5 trillion — to record heights. By around 2036, the debt would be roughly as large as the U.S. economy, and by 2050 the debt would be a projected 189 percent of the size of the economy. (The current record is 110 percent of the economy, reached during World War II.)

For more information, click here. [http://www.cbpp.org/10-11-06bud.htm]

7. How could deficits affect Americans?

Deficits are not always harmful. By running temporary deficits during an economic downturn, for example, the federal government can boost a weak economy and cushion the effects of the downturn on Americans.

Unfortunately, we are now on course for *large, persistent* deficits that would ultimately cause significant harm. In the decades ahead, borrowing by the U.S. government is slated to consume a large share of the capital available for investment, crowding out other investments that could spur long-term economic growth. The result, as Federal Reserve Chairman Ben Bernanke has predicted, may be severe. "By holding down the growth of national saving and real capital accumulation," Bernanke told Congress in March, "the prospective increase in the budget deficit will place at risk future living standards of our country." To avoid this scenario, the federal government will ultimately have to bring in substantial additional revenues and/or make deep cuts in current programs.

It also should be noted that deficits increase the size of the national debt, which in turn increases the size of the annual interest payments the government must make on the debt. Already those interest payments are beginning to squeeze other budget priorities. In 2006, the federal government spent $1 out of every $12 on interest payments, or $227 billion. That's more than we spend on education, housing, veterans' care, and environmental protection, combined.

For more information, click here. [http://www.brookings.edu/views/testimony/orszag/20060928.pdf]