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NEW CBO REPORT SHOWS ONLY MODEST FISCAL IMPROVEMENT Deficits Projected at \$2.9 - \$3.4 Trillion Over 10 Years If Policies Do Not Change

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Several key findings and conclusions emerge from the new Congressional Budget Office report on the budget and the economy issued today.¹

- *The CBO report shows significant improvement in the ten-year budget outlook, but the improvement is not nearly as large as a casual reader of the report might think.* Part of what appears to be an improvement is an artificial change that results mechanically from the methodology CBO must use. In its new report, CBO assumes that the \$70 billion in Iraq supplemental appropriations provided so far for fiscal year 2007 will be repeated every year for the next 10 years, while CBO's previous 10-year forecast (issued in August 2006) mechanically assumed that the \$120 billion in Iraq funding provided for 2006 would be repeated each year. Similarly, the new baseline projections assume no nondefense emergency supplemental appropriations over the next 10 years (because none have been provided so far for 2007), while CBO's August baseline projections assumed that the \$56 billion provided in 2006 (primarily for hurricane relief) would be repeated each year. These differences produce the appearance of a reduction in projected deficits of close to \$1.2 trillion over 10 years (including effects on interest payments on the debt), but that appearance is

KEY FINDINGS

- The new CBO ten-year budget forecast shows improvement from last summer's CBO forecast.
- More than half of the improvement since last August, however, is due to arbitrary rules CBO must follow in projecting emergency supplemental appropriations; CBO says it reflects no "changes in the underlying budgetary environment."
- The remaining portion of the improvement in the ten-year forecast is mainly due to lower projected Medicare and Medicaid costs, rather than higher revenues. The CBO data do not support claims that the tax cuts are paying for themselves and producing exceptional economic growth.
- The CBO estimates also show that if current policies are continued (i.e., if the tax cuts and AMT relief are extended and no changes are made in programs such as Medicare and Social Security), combined deficits over the next decade will total \$2.9-\$3.4 trillion.
- The CBO figures indicate that the long-term budget outlook remains grave.

¹ *The Budget and Economic Outlook: Fiscal Years 2008 to 2017*, Congressional Budget Office, January 24, 2007.

artificial. As the CBO report points out, these changes — which account for more than half of the improvement in the 10-year deficit projections — are “unrelated to the changes in the underlying budgetary environment.”²

- *Is the glass half empty or half full?* When the CBO figures are adjusted to address these anomalies, two findings stand out. On the one hand, the fiscal picture over the coming 10 years still shows significant improvement compared to previous CBO forecasts. On the other hand, the 10-year forecast is still discouraging. Furthermore, the long-term forecast remains bleak. As the CBO report states, “The favorable pattern of these projections over the next 10 years, does not, however, indicate a substantial change in the nation’s long-term budgetary challenges.”³
- *The 10-year forecast under a continuation of current policies with the anomalies corrected: deficits of \$2.9 to \$3.4 trillion.* In its “official” forecast, CBO is required to follow current law — and hence to assume that all of the tax cuts will expire, relief from the Alternative Minimum Tax will end, and as noted above, the Iraq conflict will continue to cost about \$70 billion a year over the next 10 years. Fortunately, CBO also provides estimates for alternative scenarios. Based on those estimates, the new CBO projections indicate that if the tax cuts are extended, AMT relief is continued, and costs for the war in Iraq phase down over coming years, the accumulated deficits over the next 10 years will total either \$2.9 trillion or \$3.4 trillion, depending on which of two alternative CBO scenarios one uses for how the costs in Iraq will phase down over time. (This compares to a projection of approximately \$3.7 trillion in projected deficits based on CBO’s August 2006 report.)

These projections also show mounting deficits after 2012, underscoring the point that the long-term budget picture remains grave.

- *The main cause of the improvement is lower projected Medicare and Medicaid costs, not higher tax revenues.* The CBO report projects higher tax revenues in the next few years than CBO previously had predicted. But while the Administration claims that the recent upturn in revenues indicates that the President’s tax cuts have “worked” in boosting growth and permanently raising the path of revenues, CBO now projects slightly lower real economic growth than it did last year and no permanent increase in revenues compared with what it projected in August. Over the ten years as a whole, CBO projects higher revenues (than it did in August) of \$99 billion (excluding the cost of legislation enacted since last August), or only three-tenths of one percent. In contrast, CBO projects lower Medicare and Medicaid costs over the next 10 years of \$519 billion, or a little more than six percent, compared to its August report.
- *The CBO report does not support claims that the tax cuts are paying for themselves, producing record revenues, and promoting exceptional economic growth.* As recent Center analyses demonstrate, such claims are unfounded.⁴ Economic growth in this recovery remains below average for post-World War II recoveries. Similarly, revenue growth over the current business cycle remains below revenue growth over comparable periods of earlier business cycles. These developments would continue to be true under the CBO forecasts.

² *The Budget and Economic Outlook*, pp. 11-12.

³ *The Budget and Economic Outlook*, p. 1.

⁴ See “Examining The President’s Recent Claim About Tax Cuts, Revenues, And The Economy,” Center on Budget and Policy Priorities, January 23, 2007.