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## KATRINA RELIEF AND FEDERAL SPENDING AND DEFICITS

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Some conservative lawmakers and pundits are arguing that while the funding for relief and recovery efforts from the hurricane may be money that the nation has to spend, the costs will swell federal spending to dangerous and unprecedented levels. This claim is being used both to advance calls for sharp cuts in other domestic programs — in order to offset the costs of relief and recovery efforts — and to reject any suggestion that the tax cuts of recent years be revisited to even a modest degree.

The rhetoric about an explosion in federal spending is not supported by the facts.

- **Even with the hefty Katrina relief and recovery costs, total projected federal spending will not be high by historical standards.** If relief and recovery from Katrina costs \$150 billion over the next five years, total federal spending over this period is projected to equal, on average, 20 percent of GDP. (We use a five-year period because the Congressional Budget Office projects that Katrina costs will be spread over the years through 2009, with the largest costs occurring in 2006 and 2007.) If Katrina costs total \$200 billion, total federal spending will average 20.1 percent of GDP over the next five years.

In either case, *this level of spending will be lower, as a share of the economy, than federal spending in every year from 1975 through 1996.* (The estimates of 20 percent and 20.1 percent of GDP are based on Congressional Budget Office projections. They include the costs of all current programs, the new costs of the Medicare prescription drug benefit, the continued costs of operations in Iraq and Afghanistan, assuming that those costs phase down over coming years, and the costs from Hurricane Katrina.<sup>1</sup>)

- **Total projected federal revenues are low by historical standards.** Total revenues in 2006 through 2010 are projected to average 17.2 percent of GDP. (This assumes that expiring tax

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<sup>1</sup> All projections cited here start with the baseline in the Congressional Budget Office's August 2005 report, *The Budget and Economic Outlook: An Update*. That baseline is then adjusted to include the effects of the following policies, as shown in Table 1-6 of CBO's report: (1) extending the expiring tax cuts (except for the provision dealing with repatriation of profits held abroad by American corporations); (2) continuation of relief from the Alternative Minimum Tax; (3) and a phase-down of activities in Iraq and Afghanistan. The projections of the cost of Katrina relief reflect CBPP's estimate of outlays from appropriations of \$150 billion or \$200 billion for Katrina relief, based on CBO's estimate of outlays from the \$62 billion in Katrina relief that has already been appropriated.

cuts and relief from the Alternative Minimum Tax are continued.) This is lower than in any year from 1977 through 2002.

In other words, even with the large relief and recovery costs, deficits will stem more from lower-than-normal levels of tax revenue than from unusually high levels of spending.

- **The tax cuts enacted in 2001 and 2003 cost more each year than the total amount likely to be spent on Katrina.** The cost of the tax cuts enacted in 2001 and 2003 is *\$225 billion this year alone* and will climb to higher levels each year in the future, as more of the tax cuts enacted in 2001 take full effect. Assuming that expiring tax provisions are extended and AMT relief is continued, the cost of the tax cuts will average \$250 billion a year over the next five years. The cost of the tax cuts *in a single year* exceeds the total anticipated costs of all expenses related to the hurricane over the years to come.
- **The costs of Iraq also are likely to exceed the costs of Katrina.** According to the Congressional Research Service, a total of \$192 billion has been appropriated for the war in Iraq.<sup>2</sup> Some who now decry the costs of Katrina have not been as vocal about the costs of the war.
- **The nation's serious deficit problem predated Katrina.** The Congressional Budget Office has projected that before Katrina struck, the deficit would exceed \$300 billion every year for the next 10 years and total nearly \$4.5 trillion over the 2006-2015 period, if the expiring tax cuts are extended, AMT relief is continued, and the costs of the war in Iraq and Afghanistan phase down.
- **Spending for Katrina will add relatively little to the large deficits already projected for the next 10 years.** If total funding for the response to Katrina equals \$150 billion, the deficit will be increased by a total of \$230 billion over the next ten years (\$150 billion in direct costs, plus \$80 billion to pay interest on the \$150 billion that will have to be borrowed and thus will be added to the debt). This will be on top of the deficit of \$4.5 trillion projected for 2006 through 2015 *without* the hurricane's costs. The projected deficit thus will be increased by about five percent. The only permanent cost stemming from Katrina will be the added interest payments on the debt, which will average about \$10 billion a year in 2011 through 2015.

If direct costs of the response to Katrina were to total \$200 billion, the total increase in the deficit over 10 years would be \$307 billion, and the cost of paying interest on the debt incurred to pay for the \$200 billion would average \$13.5 million a year in 2011 through 2015.

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<sup>2</sup> Steve Bowman, "Iraq: U.S. Military Operations," Congressional Research Service, updated July 5, 2005.