

## Informed Budgeteer:

### BUSH BUDGET BLUEPRINT

- Last week, President Bush submitted what the Administration called a budget blueprint—an outline of the full budget request that will arrive in early April. Perhaps not coincidentally, “blueprint” is very often the way the annual congressional budget resolution is described. So the *Bulletin* has recapitulated the President’s budget aggregates in the same way that the budget resolution is typically summarized.
- As the table below shows, under the President’s policies, the surplus would be \$231 billion in 2002, and surpluses would accumulate to \$3.4 trillion over the next 10 years, even after implementation of the President’s spending proposals and the \$1.6 trillion tax cut. Those \$3.4 trillion in surpluses would be used to pay down all of the debt that is available to be paid down—about \$2 trillion—leaving \$1.3 trillion in accumulated excess cash.

<b>Summary of Bush Budget</b>				
\$ in Billions				
		2002	2002-2006	2002-2011
<b>Discretionary:</b>				
Defense	BA	325	1,716	3,686
	OT	319	1,676	3,603
Nondefense	BA	336	1,775	3,814
	OT	373	1,971	4,216
Subtotal	BA	661	3,490	7,500
	OT	692	3,646	7,819
Mandatory Outlays		1,079	5,984	13,982
Net Interest Outlays		188	796	1,127
Total Outlays		1,959	10,426	22,929
Revenues		2,191	11,751	26,362
Unified Surplus		231	1,325	3,433
On-budget		60	261	842
Off-budget		171	1,064	2,591
Accumulated Excess Cash			0	1,288

- Contributing to the existence of this excess cash balance is \$0.8 trillion in on-budget surpluses that the Administration suggests could be available for Medicare reform, defense needs identified after the ongoing review, or other emerging priorities.
- Of course, if the Congress and the President later determine that some of these surpluses should be allocated to agreed-upon needs, then the amount of accumulated excess cash would be less.
- The President has requested that a new discretionary cap be set for 2002 at \$661 billion in budget authority, which is the same as the baseline level that adjusts appropriations provided in 2001 for inflation (4 %). Within this new cap, the largest real increases are requested for education, health, income security, science, and general government (as shown in the table following).
- But since the total pot of resources available for discretionary spending remains fixed under the President’s proposal, other programs would have to be reduced to make room for the increases. Details on such reductions, however, will not be available until April.
- Within this new discretionary cap, the President’s blueprint suggests a new mechanism to control the abuse of the “emergency” designation that has allowed spending to occur in excess of statutory caps for the last several years.
- The budget reflects \$5.6 billion (shown in the Allowances function--920) as a National Emergency Reserve that would only be available upon agreement between the Congress and the President. This proposal represents an interesting effort to actually budget for real emergencies, rather than assume that they won’t occur in the future—a weakness of many past budget proposals from many quarters.

<b>Discretionary Spending Totals in the Bush Budget</b>				
\$ in Billions				
		2001	2002	% Change
Defense- 050	BA	311.3	324.9	4.4
	OT	299.6	319.1	6.5
International Affairs- 150	BA	22.7	23.9	5.3
	OT	24.1	24.5	1.7
Science- 250	BA	20.8	22.0	6.0
	OT	19.6	21.1	7.6
Energy- 270	BA	3.1	2.8	-10.1
	OT	3.1	3.0	-2.9
Environment- 300	BA	28.8	26.4	-8.3
	OT	27.7	27.8	0.3
Agriculture- 350	BA	5.1	4.8	-5.4
	OT	5.5	5.5	-0.7
Commerce- 370	BA	0.7	-0.3	-147.6
	OT	1.8	0.3	-82.6
Transportation- 400	BA	19.0	15.9	-16.0
	OT	48.9	52.9	8.3
Regional Development- 450	BA	11.0	10.1	-8.1
	OT	11.4	11.7	2.9
Education/Social Services- 500	BA	61.2	65.3	6.8
	OT	55.5	61.8	11.4
Health- 550	BA	38.9	41.0	5.5
	OT	34.0	38.6	13.4
Medicare- 570	BA	3.4	3.4	2.7
	OT	3.3	3.4	3.5
Income Security- 600	BA	39.5	42.8	8.5
	OT	45.4	46.9	3.3
Social Security- 650	BA	3.4	3.5	2.1
	OT	3.6	3.5	-3.0
Veterans- 700	BA	22.5	23.5	4.5
	OT	22.3	23.4	4.9
Justice- 750	BA	29.9	29.7	-0.6
	OT	28.9	30.9	6.9
General Government- 800	BA	14.0	14.8	5.8
	OT	14.5	14.7	1.0
Allowances- 920	BA	0.0	6.0	--
	OT	0.0	2.7	--
<b>Total</b>	BA	635.0	660.7	4.0
	OT	649.1	691.7	6.6
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Defense	BA	311.3	324.9	4.4
	OT	299.6	319.1	6.5
Nondefense	BA	323.8	335.7	3.7
	OT	349.5	372.7	6.6

### PRESIDENT’S ECONOMIC PROJECTIONS

- The President’s Budget is based on conservative economic assumptions that include the recent moderation in growth and, on average, lag behind the consensus forecast produced by the Blue Chip economists over the next ten years.

<b>OMB and Blue Chip Economic Assumptions: February 2001</b>				
	2001	2002	2003	2002-2011
Real GDP Growth				
OMB	2.4	3.3	3.2	3.2
Blue Chip	2.1	3.5	3.2	3.4
CPI				
OMB	2.7	2.6	2.6	2.5
Blue Chip	2.6	2.4	2.7	2.6
Unemployment				
OMB	4.4	4.6	4.5	4.6
Blue Chip	4.5	4.5	4.5	4.6

SOURCE: OMB

- OMB projects that the real economy will grow only 2.4% this year and thereafter grow at a 3.2% rate through 2011, which is consistent with the rate of growth experienced since 1990, including the recession. Over 10 years the Blue Chip projects real GDP will grow

at a 3.4% rate, two-tenths of a percentage point faster than OMB. If the economy grows as fast as the Blue Chips project, than this differential would generate an additional \$488 billion in surpluses from 2002-11.

- Under the President’s Budget, inflation is assumed to decline from 3.4% in 2000 to 2.7% in 2001 and remain relatively stable through 2011. In comparison the Blue Chip consensus is slightly more optimistic in the near-term with CPI falling to 2.6% and roughly continuing at this pace over the ten year horizon.
- Labor markets are forecast to loosen as unemployment increases from 4.0% in 2000 to 4.4% in 2001. While the Blue Chip consensus expects unemployment to be slightly higher than OMB this year, both forecasts look for unemployment to rise gradually averaging 4.6% over the long-term.

### THE DEBT PAYDOWN

- Under President Bush’s budget proposal, the gross public debt will fall by \$2 trillion, from \$3.2 trillion in the current fiscal year to \$1.2 trillion in 2011, which will be about 7 percent of GDP. OMB asserts it would be difficult – and costly for taxpayers – to retire more than \$2 trillion in debt by 2011.
- Of the \$1.2 trillion in debt that would remain in 2011, about \$0.8 trillion will be long-term bonds that have yet to mature. Getting the holders of these bonds to sell them back to the Treasury would cost, according to OMB, a “penalty premium” of \$50-\$150 billion. The “penalty premium” would have to be financed through higher taxes or lower government spending.
- The penalty premium would arise, in part, because bondholders would know the Treasury is determined to repurchase debt and hold out for higher prices. Also, as more debt is repurchased, a higher share of the remaining debt would be held by bondholders reluctant to give up their Treasury securities.
- The balance of \$0.4 trillion in public debt remaining in 2011 consists of non-marketable debt such as savings bonds, bonds used by states and localities to temporarily store money, and Brady bonds that were issued to ease the Latin America debt crisis. Although some have suggested the Bush budget would leave too much debt, the proposal would leave less debt than the final baseline projections of the previous administration.

<b>Debt Held by the Public (Gross)</b>		
\$ in Billions		
	Clinton Baseline	Bush Budget
2007	1,587	1,585
2008	1,490	1,404
2009	1,362	1,279
2010	1,290	1,208
2011	1,238	1,158

### AN ILLUSTRATION OF PROGRESSIVITY

- The MIT Dictionary of Modern Economics, third edition, defines a progressive tax as a situation where the proportion of income taken in tax (the tax rate) rises with income or spending power. The Joint Committee on Taxation (JCT) published data for 2001 that illustrates just how progressive our income tax system is.

<b>Distribution of Income &amp; Federal Income Tax Liability*-2001</b>		
Income Category	Income - % of total	Income Tax- % of total

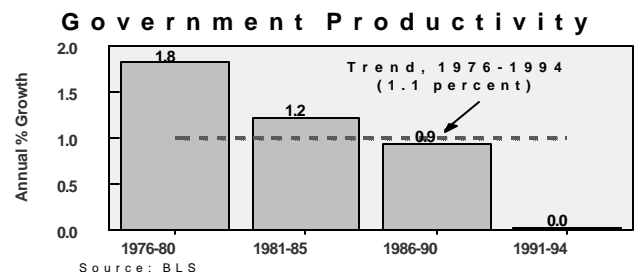
Bottom 90%	58.0	31.8
Top 10%	42.0	68.2
Top 5%	31.3	56.6
Top 1%	17.2	35.9

Source: JCT, JCX-2-01, February 27, 2001. \*Includes the outlay portion of the EIC.

- The bottom 90% of earners, those with incomes under \$107,455, will earn 58% of total income in 2001, and will pay 31.8% of total income taxes. The top 5%, with incomes above \$145,199, will earn 31.3% of total income in 2001 and will pay 56.6% of total income taxes. The top 1%, with incomes above \$340,306, will earn 17.2% of total income but will pay 35.9% of total taxes in 2001.
- After JCT completes the analysis of President Bush’s tax plan it will be apparent that his plan makes our already quite progressive system even more progressive.

### GOVERNMENT PRODUCTIVITY

- Productivity growth is the driving force behind the ongoing economic expansion, and, as Federal Reserve Chairman Alan Greenspan has stated, it is a key factor in generating budget surpluses. While much is known about productivity in the private sector, there has been relatively little discussion about government productivity.
- Between 1967 and 1994 the Bureau of Labor Statistics (BLS) measured government productivity and reported their results in a report entitled, “The Federal Productivity Measurement Program: Final Results”. Unlike the private sector, which produces goods and services, the federal government produces mostly services that can be difficult to measure. In order to overcome this problem BLS counted a combination of intermediate outputs (services consumed by the government) and final outputs (services consumed by the public) to determine government productivity.
- The data revealed that the growth of productivity declined from an average of 1.8% in 1976-80 to 0.0% in 1991-94. During the same time frame non-farm productivity growth increased from an average of 1.2% to 1.7%.



- Within separate government functions productivity growth varied dramatically. For example, in the electric power generation and distribution function, productivity declined 1.0% per year on average throughout the entire time data was collected. Periodic oil embargos, reductions in nuclear power generation and occasional droughts that reduced hydroelectric power production account for most of the declines.
- In the finance and accounting function, productivity increased an average of 3.8% per year as the impact of automation and electronic payments reduced the need for labor to process government payrolls and deposits.
- What caused government productivity growth to decline? A decline in production requires some combination of a drop in hours, jobs or output per worker per hour (productivity). While slowdowns in the

private sector often lead to quick reductions in hours or jobs, the government was reluctant to cut jobs or hours, preferring instead to absorb the output slowdown by demanding less per worker-hour. In the surveys BLS collected from participating agencies, managers often noted that workload was affected by legislative changes, greater utilization of technology and climatic disturbances thereby causing fluctuations in output.

#### **Senate Budget Committee Hearing Schedule**

March 6: Administration's FY 2002 Budget; Witness: Tommy G. Thompson, Secretary, Department of Health and Human Services. Dirksen 608; 10 am.