United States Senate Budget Committee

JEFF SESSIONS | Ranking Member

CBO Report: After Doubling In Last Six Years, Debt Will Explode In Coming Decades

Budget Office Confirms That Reining In Debt Would Promote Economic Growth

The latest Long-Term Budget Outlook of the Congressional Budget Office (CBO) projects that debt held by the public will grow from almost $13 trillion today to $21 trillion 10 years from now and $53 trillion in 25 years under the assumption that current law is unchanged. (CBO discusses only public debt in its long-term outlook, but it is necessary to bear in mind that gross debt, which includes intragovernmental obligations that must be honored, is and will continue to be significantly higher.) Public debt has already doubled between the end of 2008 and today, and would quadruple over the next 25 years.

CBO has repeated its warning that large and continually growing debt increases the probability of a fiscal crisis striking the United States. This would result in a dangerous surge in the interest rates demanded by investors in U.S. government debt, accelerating the ongoing deterioration of the nation's finances. Taking into account economic feedback effects from a burdensome debt and the higher interest rates that would be demanded by bondholders, CBO estimates that in 2039, debt held by the public would reach 111 percent of the nation's output as measured by gross domestic product (GDP). **Debt at that level would be almost triple the 39 percent of GDP average during the past 40 years.**

The long-term outlook has worsened since CBO's last report in September 2013. Largely this is the effect of lower revenues in CBO's April 2014 baseline—primarily the result of a weaker economy—projected forward for the next 15 years, as well as mostly offsetting changes in projections of noninterest spending. The combination results in debt held by the public that is 3 percentage points higher than the 108 percent of GDP projected by CBO last year.

A significant portion of the debt buildup comes from paying interest costs on the accumulated debt. Because every penny of the interest expense must itself be borrowed, the stock of debt rises as the return to more normal rates of interest increase debt service costs. A single year's interest payments are estimated to grow from $221 billion last year to a staggering $876 billion in 2024. By 2039, interest costs will exceed every major category of spending other than Social Security. Interest projections would have been higher but for the fact that CBO lowered its real long-term interest rate projection to 2.2 percent this year, down 0.5 percent from the 2.7 percent assumption used last year.

The other major pressures on the long-term budget outlook come from growing spending for Social Security and the government's major health care programs (Medicare, Medicaid, and

Obamacare exchange subsidies). CBO now projects that the combined Social Security trust funds will be exhausted within 15 years, one year sooner than the agency projected 10 months ago. **The costs of the major health care programs will also almost triple as a share of GDP relative to the average of the past 40 years**, and account for two-thirds of the increase in Social Security and major health care programs taken as whole. The expansion of Medicaid and Obamacare exchange subsidies by themselves account for almost two-thirds of the higher projected costs for major health care programs in 10 years, and over one-fourth in 25 years.

CBO also provides an alternative fiscal scenario, which assumes that the spending controls required by the Budget Control Act are abandoned, that future changes to the Medicare physician payment formula (the so-called "doc fix") are not paid for, and that federal non-interest spending apart from Social Security and the major health care programs stay constant as a share of GDP. Under this scenario, including economic feedback effects, the debt grows to 183 percent of GDP in 25 years. Notably, in this model CBO is unable to project debt past 2050 because the agency assumes that there would be no purchasers of U.S. government debt at such extreme levels of debt.

CBO's report underscores the destructive economic consequences of growing deficits and rapidly rising federal debt. Consistent with the consensus view of nearly all economists, CBO finds that rising debt slows the economy as private borrowers find themselves competing with the federal government for available credit. Because lenders generally believe that public debt is a safer investment than private debt, private firms are "crowded out" of credit markets by the U.S. Treasury. In addition, income tax bracket creep slowly increases effective marginal tax rates, which reduces the pace of economic activity. Finally, larger transfer payments to working-age adults discourage participation in the economy and boost the drop-out rate, which further slows the rate of economic growth and undermines job creation.

One way to see the effects of a slower economy is through the slowdown's effects on per person wealth in the extended baseline. The slower economy reduces inflation-adjusted GNP per person when compared with better debt outcomes in the first 10 years of CBO's 25-year outlook. The per-capita effects are substantial: a $2 trillion decline in deficits over the first 10 years would yield a $2,000 per person benefit. A $4 trillion reduction in deficits would produce a wealth gain of $4,000.

Another way to view the effects of our worsening fiscal condition on the economy is to gauge how much lower or higher the level of GNP would be if debt is better or worse than the extended baseline. Under the "worst case" alternative fiscal scenario, CBO estimates that the level of GNP could be as much as 8 percent lower, with a central estimate of 5 percent lower. However, if Congress manages to enact policies that reduce deficits, GNP could be as much as 4 percent higher than baseline when deficits are $2 trillion lower and 7 percent higher when the first 10 years of deficits fall by $4 trillion.

In sum, CBO's report shows that lower deficits yield significant economic benefits: more wealth per person and better overall economic opportunities. In addition, with lower deficits, the federal budget outlook brightens as revenues naturally rise through economic growth and fewer Americans require government assistance.