The Outlook for Deficits and Debt

Name: ______________________________ **Date:** ______________

Overview

Federal budget deficits are set to increase rapidly this year and over the next four years, the Congressional Budget Office projects, and then to remain largely stable relative to the size of the economy—but at a very high level by historical standards—over the rest of the projection period. Those deficits would result in rising federal debt. Moreover, CBO's baseline projections reflect a number of significant changes to tax and spending policies that are scheduled to take effect under current law. If those changes did not occur, deficits and debt would be substantially larger.

Rising Deficits

As required by law, when constructing its baseline projections, CBO incorporates the assumption that current laws governing taxes and spending will generally remain unchanged in future years. Under that assumption, in CBO's baseline, federal deficits average $1.2 trillion per year and total $12.4 trillion over the 2019–2028 period. As a percentage of gross domestic product (GDP), the deficit increases from 3.5 percent in 2017 to 5.4 percent in 2022. Thereafter, the deficit fluctuates between 4.6 percent and 5.2 percent of GDP from 2023 through 2028. Over the past 50 years, the annual deficit has averaged 2.9 percent of GDP.

Growing Debt

The large deficits over the next 10 years would cause the national debt to rise steadily. Relative to the nation's output, debt held by the public is projected to increase from 76.5 percent of GDP in 2017 to 96.2 percent at the end of 2028. At that point, federal debt would be higher as a percentage of GDP than at any point since just after World War II—and heading still higher. Federal debt held by the public consists mostly of the securities that the Treasury issues to raise cash to fund the federal government's activities and to pay off its maturing liabilities. The Treasury borrows money from the public by selling securities (bonds) in financial markets; that debt is purchased by various buyers in the United States, by private investors overseas, and by the central banks of other countries. Of the $14.7 trillion in federal debt held by the public at the end of 2017, 57 percent ($8.3 trillion) was held by domestic investors and 43 percent ($6.3 trillion) was held by foreign investors. Under the assumptions that govern CBO's baseline, the federal government is projected to borrow another $14.0 trillion from the end of 2017 through 2028, boosting debt held by the public to 96 percent of GDP by the end of the projection period. That amount of debt relative to the size of the economy would be the greatest since 1946 and more than double the 50-year average of 41 percent.

Consequences of Growing Debt

Such high and rising debt would have significant negative consequences, both for the economy and for the federal budget, including these:

- When interest rates return to more typical, higher levels, federal spending on interest payments would increase substantially.
- Because federal borrowing reduces national saving over time, the nation's capital stock ultimately would be smaller, and productivity and total wages would be lower than would be the case if the debt was smaller.
- Lawmakers would have less flexibility than otherwise to use fiscal policies (government tax and spending policies) to respond to unexpected challenges.
- The likelihood of a fiscal crisis in the United States would increase. Specifically, the risk would rise of investors' becoming unwilling to finance the government's borrowing unless they were compensated with very high interest rates. If that occurred, interest rates on federal debt would rise sharply relative to rates of return on other assets.

Source: Congressional Budget Office, "The Budget and Economic Outlook 2018 to 2028," April, 2018