CONGRESSIONAL BUDGET OFFICE

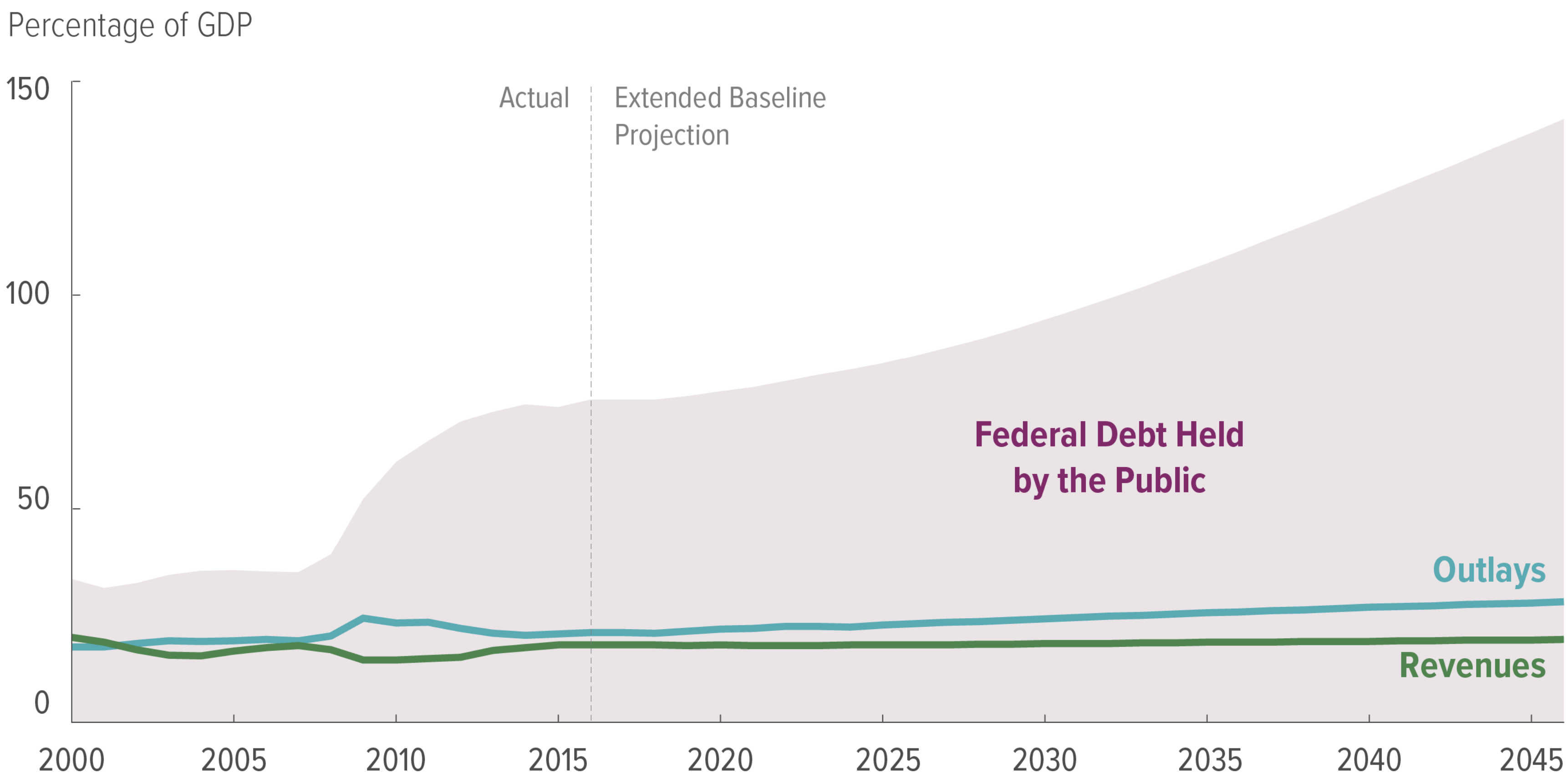
The 2016 Long-Term Budget Outlook in 22 Slides

July 2016

For more details, see www.cbo.gov/publication/51580.

If current laws governing taxes and spending did not change, the condition of the federal budget would worsen considerably over the next three decades, as debt grew larger in relation to the economy than ever recorded in U.S. history.

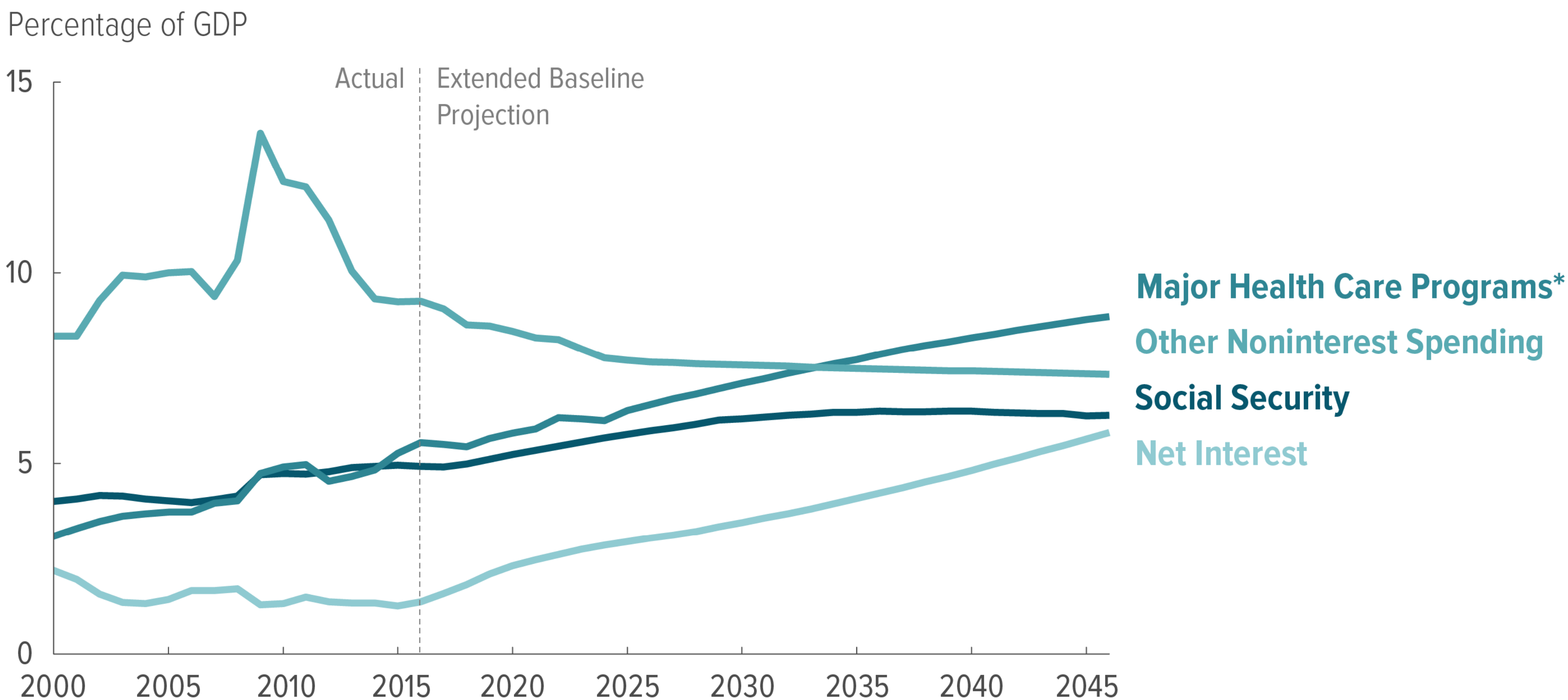
Federal Debt, Spending, and Revenues



CBO's extended baseline projections show a substantial imbalance in the federal budget; that is, revenues are projected to fall short of spending by steadily increasing amounts. (Those projections incorporate the assumption that current laws governing taxes and spending generally remain the same.) As a result, projected federal debt tops 140 percent of GDP 30 years from now.

Federal spending is projected to rise noticeably in relation to the economy—from 21.1 percent of GDP in 2016 to 28.2 percent in 2046—because of spending growth in a few of the largest programs and escalating interest costs on the government's debt.

Components of Federal Spending

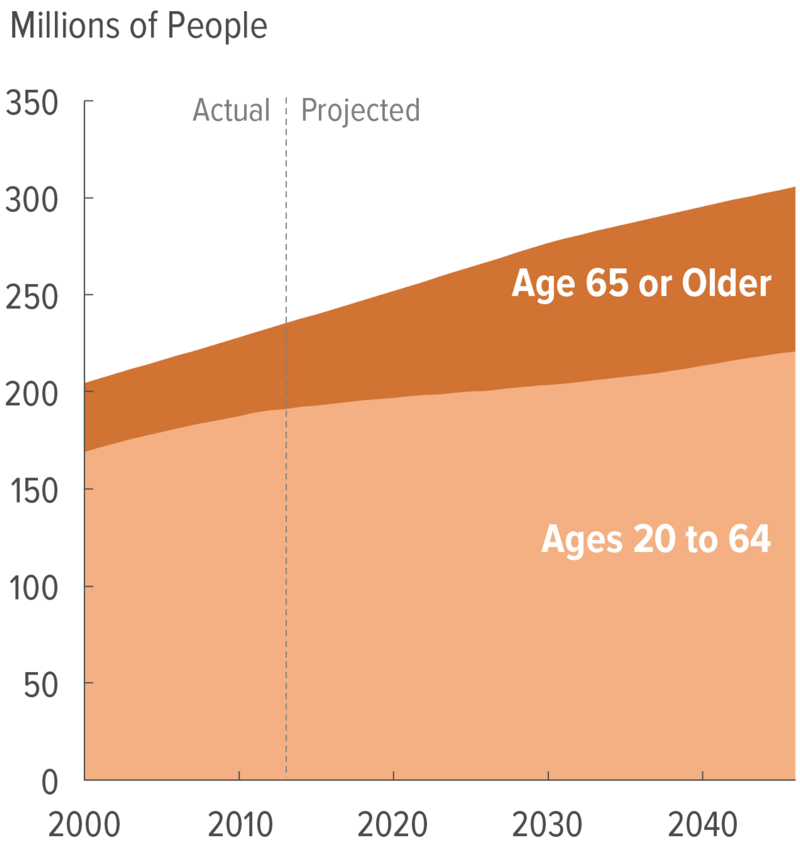


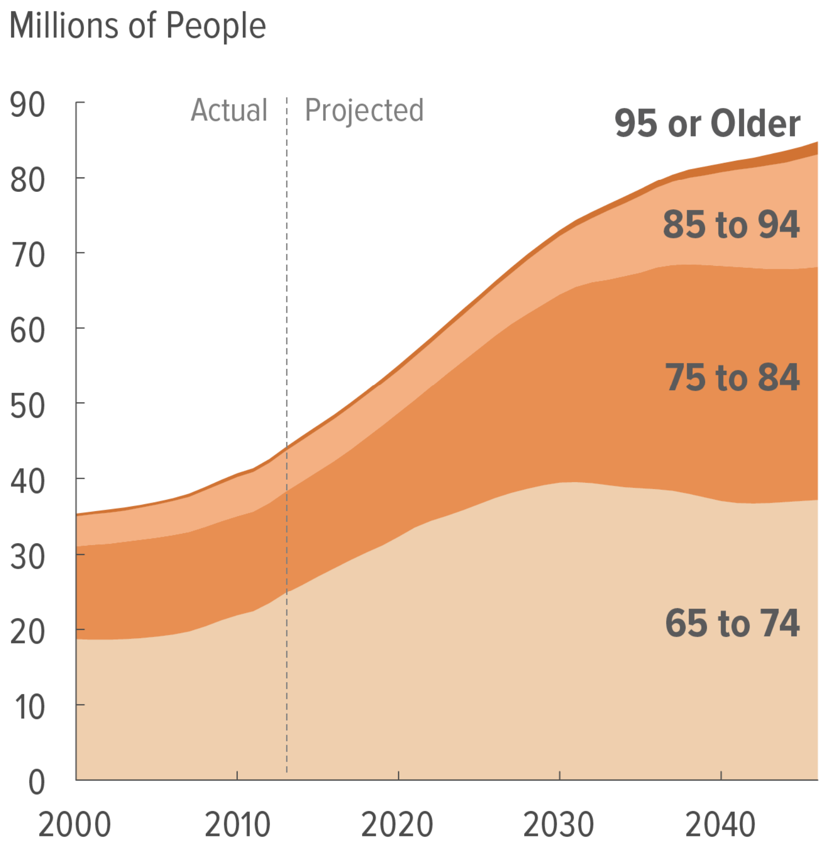
* Consists of spending on Medicare (net of offsetting receipts), Medicaid, and the Children's Health Insurance Program, as well as outlays to subsidize health insurance purchased through the marketplaces established under the Affordable Care Act and related spending.

Measured as a percentage of GDP, spending on Social Security and the major health care programs (primarily Medicare) would grow more than other noninterest spending would fall. That would occur even though that other noninterest spending—for defense, transportation, child nutrition, certain veterans' benefits, and many other programs and activities—would drop to its smallest percentage of GDP in more than 70 years. Net interest costs on the government's debt are projected to rise sharply.

Three factors explain most of the projected growth in spending: aging, rising health care spending per person, and rising interest rates.

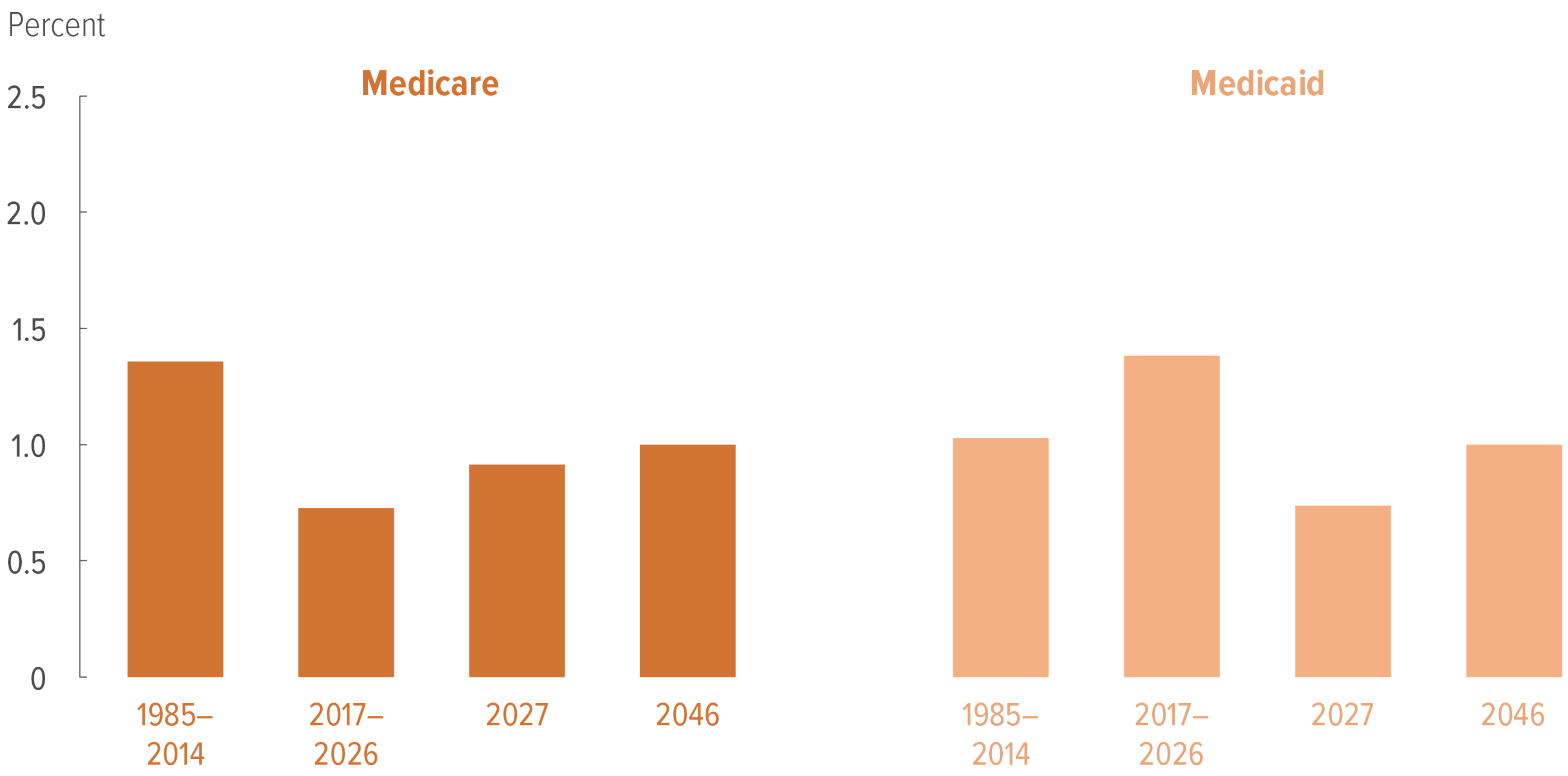
Changes in Population, by Age Group





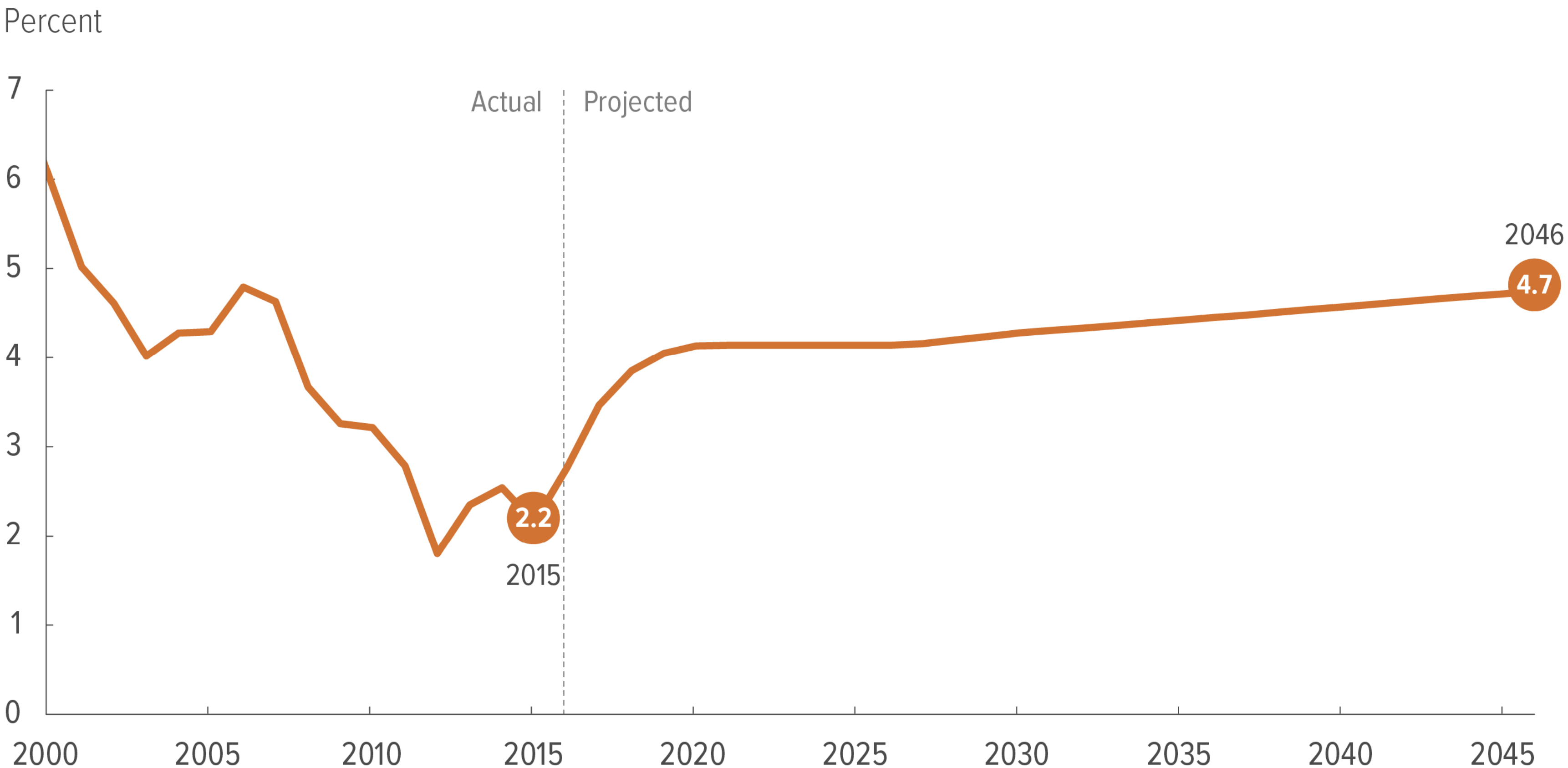
Much of the spending growth for Social Security and the major health care programs results from the aging of the population: As members of the baby-boom generation grow older and as life expectancy continues to increase, the percentage of the population age 65 or older is anticipated to grow sharply, boosting the number of beneficiaries of those programs. By 2046, in CBO's projections, spending for those programs for people 65 or older accounts for about half of all federal noninterest spending.

Estimated and Projected Rates of Excess Cost Growth



The rest of the projected growth in spending for Social Security and the major health care programs is driven by health care costs per beneficiary, which are projected to increase more quickly than GDP per person (after the effects of aging and other demographic changes are removed). CBO projects that such excess cost growth will continue in part because of the effects of new medical technologies and rising personal income.

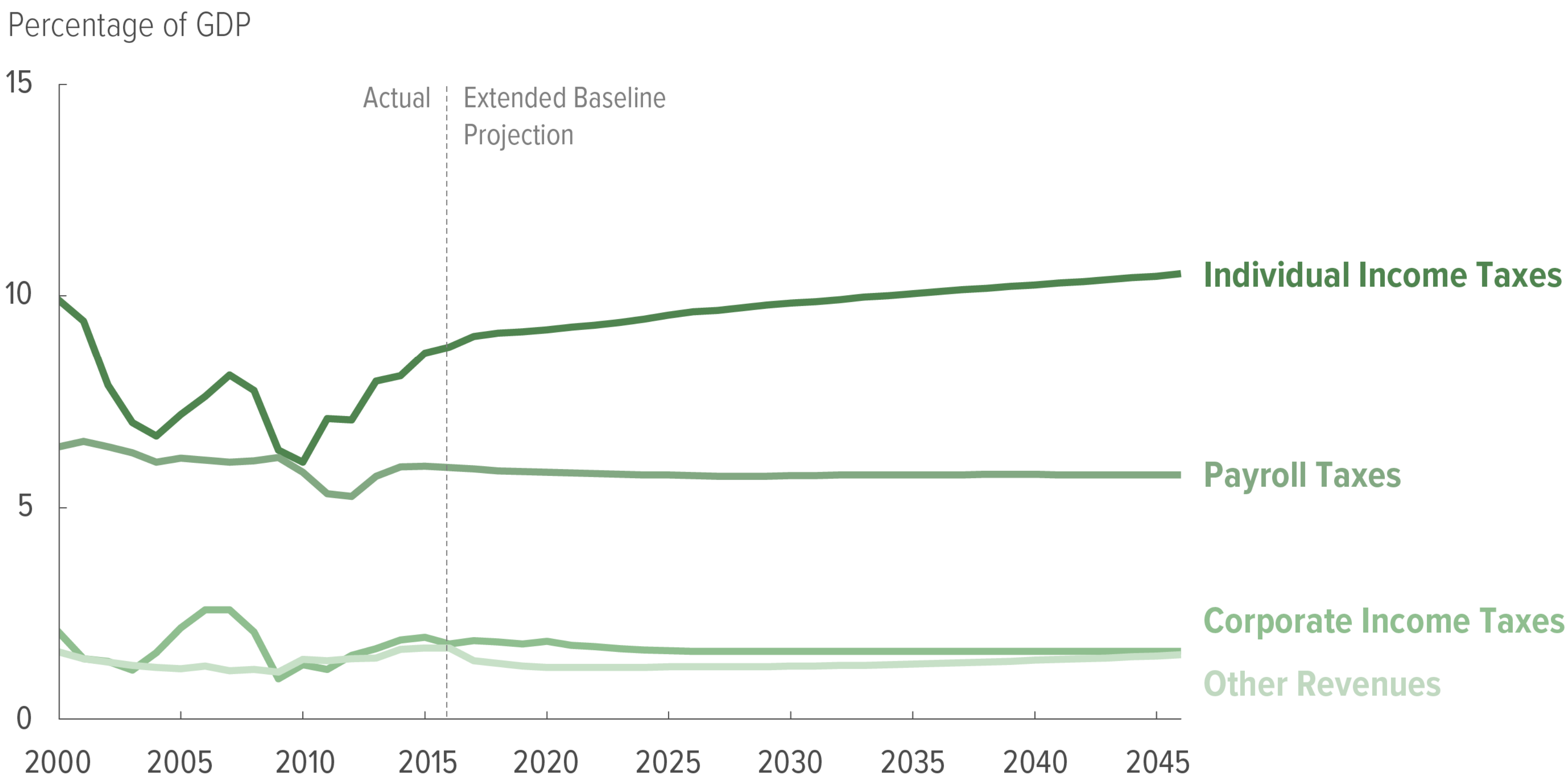
Interest Rate on 10-Year Treasury Notes



Interest rates are unusually low at present. As the economy grows, however, they are projected to rise, increasing the cost of interest on the government's debt. Growth in net interest costs and growth in debt reinforce each other: Rising interest costs push up deficits and debt, and rising debt pushes up interest costs.

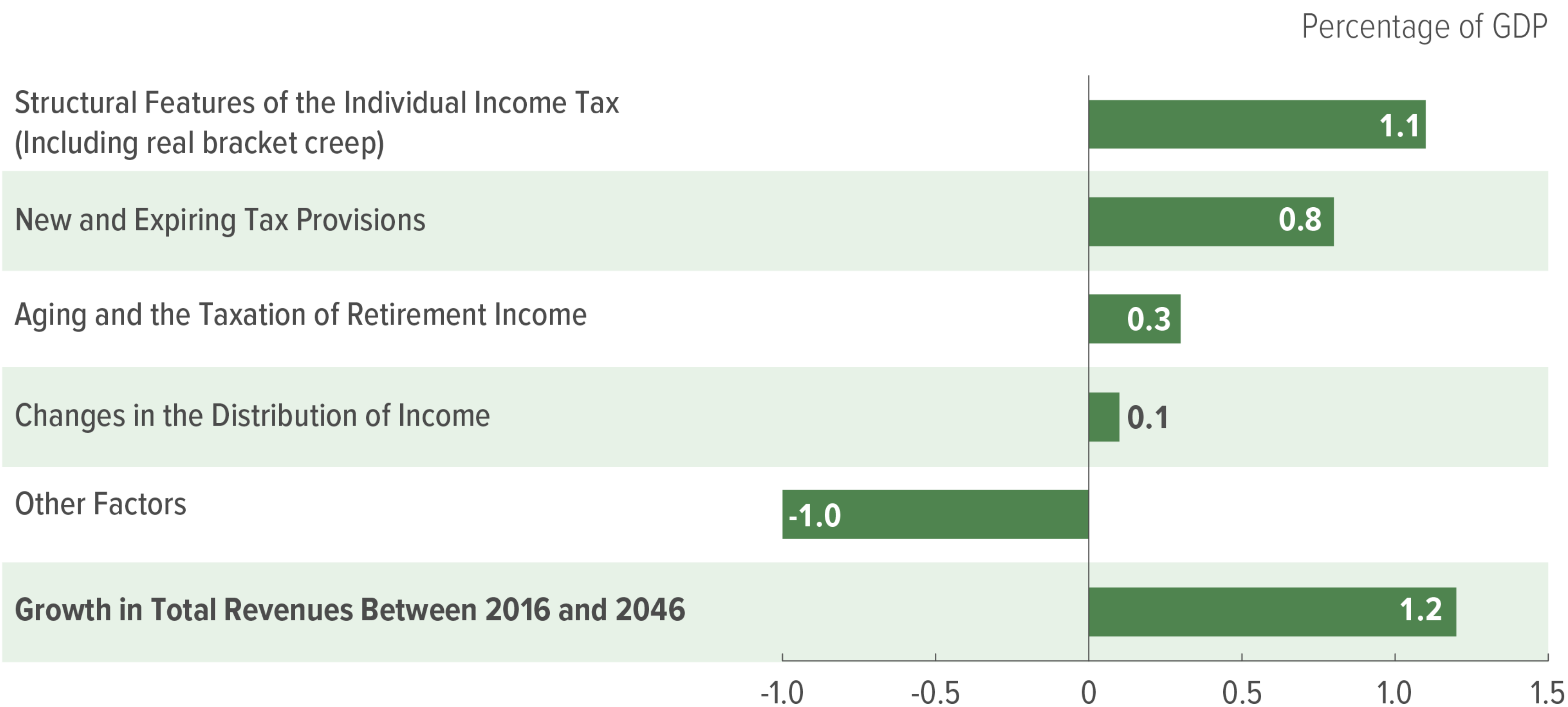
Federal revenues would also increase—from 18.2 percent of GDP in 2016 to 19.4 percent in 2046—if current laws remained generally unchanged, but they would increase much more slowly than federal spending.

Components of Federal Revenues



The modest projected growth in revenues relative to GDP over the next three decades is primarily attributable to increases in individual income tax receipts. Receipts from all other sources, taken together, are projected to decline.

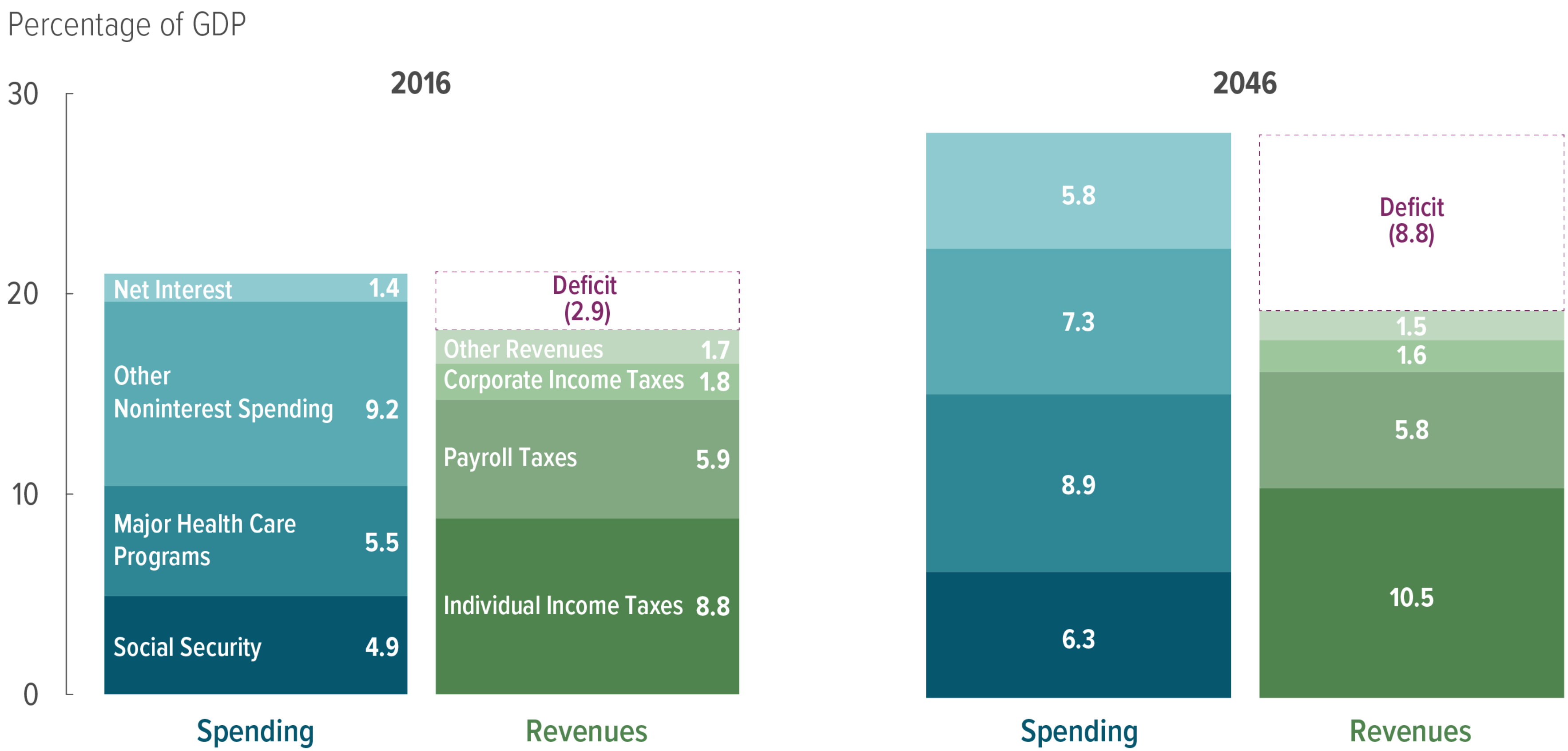
Sources of Growth in Federal Revenues Between 2016 and 2046



The projected rise in revenues would occur for two main reasons. First, real bracket creep is expected to continue over the long term; that is, people's income would grow faster than inflation, so more of it would be pushed into higher tax brackets. Second, a new excise tax on certain employment-based health insurance plans would generate a growing amount of revenues in relation to the size of the economy.

Because the growth in revenues would not keep pace with the growth in spending over the long term, budget deficits would grow (if current laws governing taxes and spending remained generally the same).

The Federal Budget Under the Extended Baseline



Not only would budget deficits grow, but the composition of the budget would continue to shift, as it has for the past several decades.

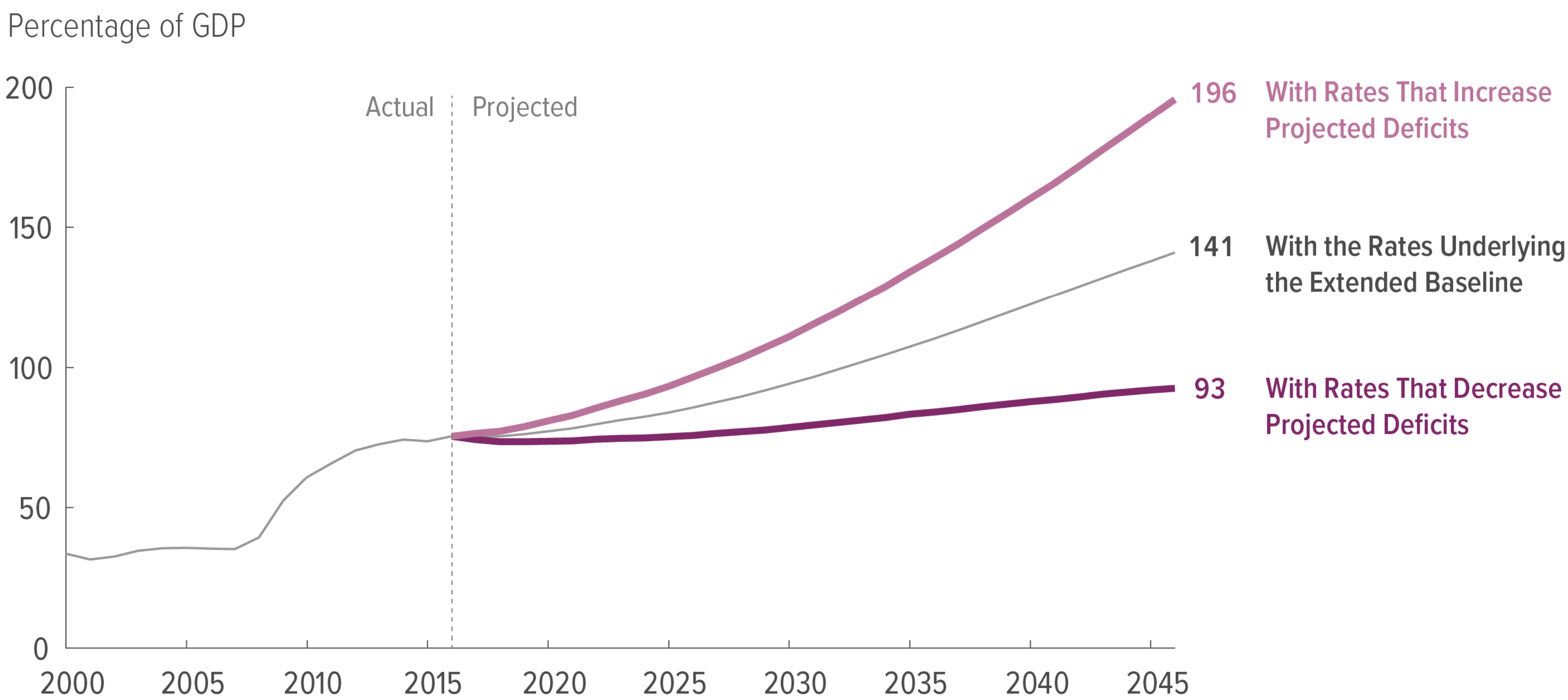
Because of the growing deficits, federal debt held by the public is projected to total 141 percent of GDP in 2046. The prospect of such large debt poses substantial risks for the nation and presents policymakers with significant challenges.

Federal Debt Held by the Public

High and rising federal debt would reduce national saving and income in the long term; increase the government's interest payments, thereby putting more pressure on the rest of the budget; limit lawmakers' ability to respond to unforeseen events; and increase the likelihood of a fiscal crisis.

Even if future tax and spending policies matched the policies specified in current law, budgetary outcomes would undoubtedly differ from CBO's projections because of changes in the economy, demographics, and other factors.

Projected Federal Debt Based on Different Rates of Labor Force Participation, Productivity Growth, Interest on Federal Borrowing, and Excess Cost Growth for Federal Spending on Medicare and Medicaid



CBO varied some key factors in its projections of debt—changing them in ways based largely on the variation over time in their 30-year averages, as well as on a consideration of possible economic and demographic developments. In the resulting projections, debt in 2046 ranges from 93 percent of GDP to 196 percent, both much higher than today's 75 percent.

To put the budget on a sustainable path, lawmakers would have to make major changes to tax policies, spending policies, or both.

To show how such changes in law would affect the long-term fiscal imbalance, CBO took two approaches. First, it estimated how large changes in spending or revenues would have to be if lawmakers wanted federal debt in 2046 to meet two chosen goals.

The Size of Policy Changes Needed to Make Federal Debt Meet Two Possible Goals in 2046

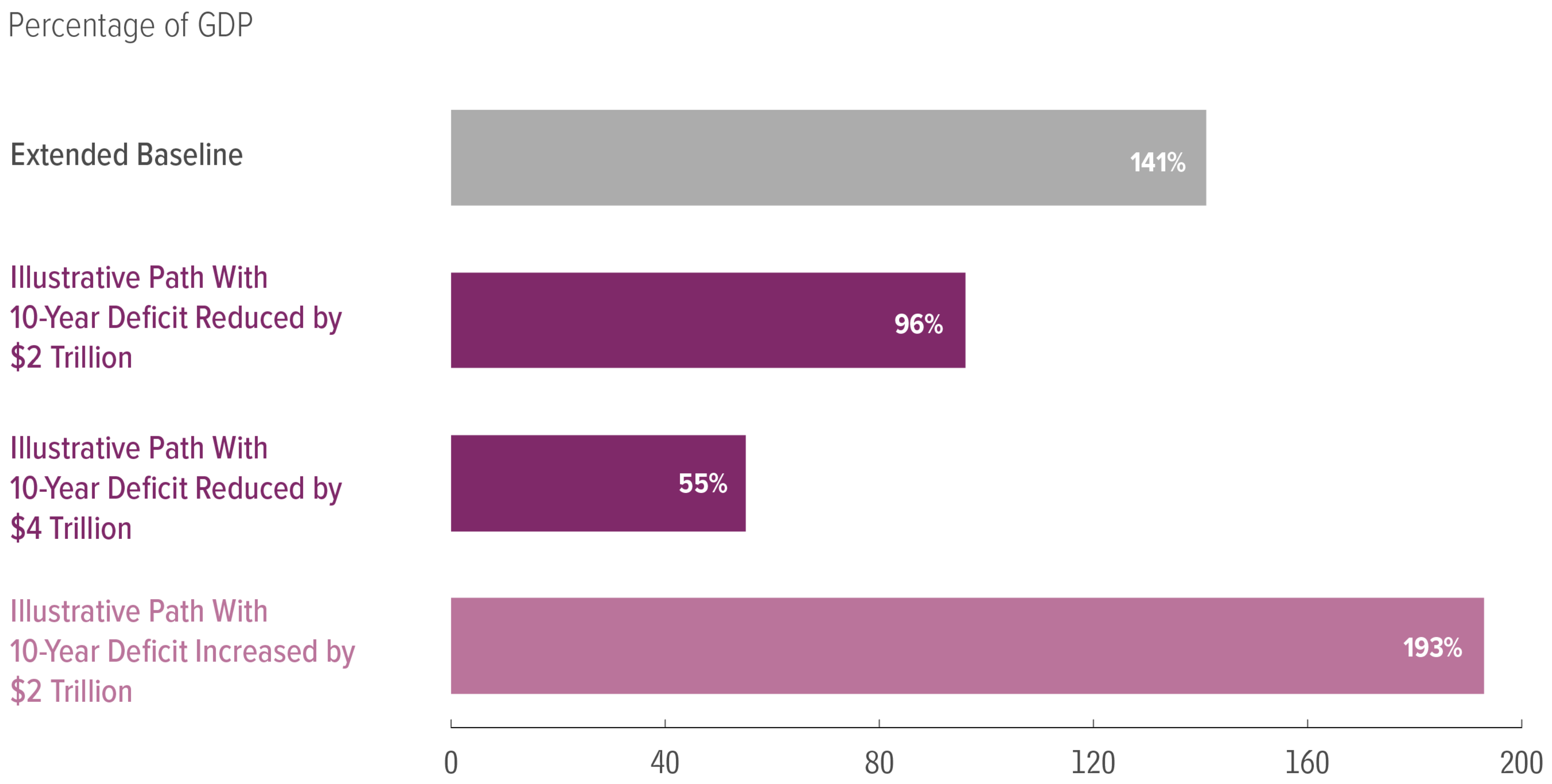
If lawmakers aimed for debt in 2046 to equal . . .	39% of GDP (Its 50-year average)	75% of GDP (Its current level)
Each year, they would need to increase revenues or reduce noninterest spending by . . .	2.9% of GDP, which is equal to a 16% increase in **revenues** or a 14% cut in **spending**	1.7% of GDP, which is equal to a 9% increase in **revenues** or an 8% cut in **spending**
In 2017, that would amount to . . .	**$560 billion,** which is equal to **$1,700** per person	**$330 billion,** which is equal to **$1,000** per person
If the changes were increases (of equal percentage) in all types of revenues, one effect in 2017 is that taxes per household would be higher than under current law by . . .	$1,900	$1,100
If the changes were cuts (of equal percentage) in all types of noninterest spending, one effect in 2017 is that initial Social Security benefits would be lower than under current law by . . .	$2,600	$1,500

Values for taxes are for households in the middle fifth of the income distribution. Under current law, their taxes are projected to average $12,200.

Values for benefits are averages for people in the middle fifth of the lifetime earnings distribution who were born in the 1950s and who would claim benefits at age 65. Under current law, their benefits are projected to be $18,700.

Second, CBO approached the issue from the other direction, estimating how two illustrative deficit-reduction paths would affect debt in 2046. For the sake of comparison, the agency also examined one illustrative deficit-increasing path.

Federal Debt in 2046 Under Various Budgetary Paths



The two deficit-reduction paths that CBO analyzed would gradually decrease deficits through unspecified increases in tax revenues, cuts in spending, or both. In the long run, the reduced deficits and debt would make output and income higher, and the ratio of federal debt to GDP lower, than they would be under the extended baseline. The third path would gradually increase deficits, leading to a decline in output and an increase in the ratio of debt to GDP.

In deciding how quickly to reduce deficits, lawmakers face trade-offs. Waiting would mean a greater accumulation of debt, larger changes needed to achieve a particular long-term outcome, and more uncertainty about future policies. Acting sooner would weaken the economic expansion over the following two years or so and give people little time to plan or adjust.

About This Document

Leigh Angres, Stephanie Hugie Barello, Maureen Costantino, Devrim Demirel, Jonathan Huntley, Geena Kim, Marina Kutyavina, Xiaotong Niu, Charles Pineles-Mark, Joshua Shakin, Michael Simpson, and Julie Topoleski contributed to this presentation.

For more details, see *The 2016 Long-Term Budget Outlook* (July 2016), www.cbo.gov/publication/51580, which is the result of work by many analysts at CBO.