Background Information on the Federal Budget Outlook

What is the long-term outlook for the federal budget?

“The long-term outlook for the federal budget has worsened dramatically over the past several

years, in the wake of the 2007–2009 recession and slow recovery. Between 2008 and 2012,

financial turmoil and a severe drop in economic activity, combined with various policies

implemented in response to those conditions, sharply reduced federal revenues and increased

spending. As a result, budget deficits rose: They totaled $5.6 trillion in those five years, and in

four of the five years, they were larger relative to the size of the economy than they had been in

any year since 1946. Because of the large deficits, federal debt held by the public soared, nearly

doubling during the period. It is now equivalent to about 74 percent\* of the economy’s annual

output, or gross domestic product (GDP)—a higher percentage than at any point in U.S. history

except a seven-year period around World War II.

If current law remained generally unchanged in the future, federal debt held by the public would

decline slightly relative to GDP over the next few years, CBO [Congressional Budget Office]

projects. After that, however, growing budget deficits—caused mainly by the aging of the

population and rising health care costs—would push debt back to, and then above, its current

high level. The deficit would grow from less than 3 percent of GDP this year to more than 6

percent in 2040. At that point, 25 years from now, federal debt held by the public would exceed

100 percent of GDP.

Moreover, debt would still be on an upward path relative to the size of the economy.

Consequently, the policy changes needed to reduce debt to any given amount would become

larger and larger over time….”

Source: Congressional Budget Office, “The 2015 Long-Term Budget Outlook,” June 16, 2015

\*Note that since this was written the federal debt held by the public is now about 75% of GDP

What consequences would a large and growing federal debt have?

“How long the nation could sustain such growth in federal debt is impossible to predict with any

confidence. At some point, investors would begin to doubt the government’s willingness or ability

to meet its debt obligations, requiring it to pay much higher interest costs in order to continue

borrowing money. Such a fiscal crisis would present policymakers with extremely difficult choices

and would probably have a substantial negative impact on the country. Unfortunately, there is

no way to predict confidently whether or when such a fiscal crisis might occur in the United

States. In particular, as the debt-to-GDP ratio rises, there is no identifiable point indicating that a

crisis is likely or imminent. But all else being equal, the larger a government’s debt, the greater

the risk of a fiscal crisis.

Even before a crisis occurred, the high and rising debt that CBO projects in the extended baseline

would have macroeconomic effects with significant negative consequences for both the

economy and the federal budget:

• The large amount of federal borrowing would draw money away from private investment

in productive capital over the long term, because the portion of people’s savings used to

buy government securities would not be available to finance private investment. The

result would be a smaller stock of capital, and therefore lower output and income, than

would otherwise have been the case, all else being equal. (Despite those reductions,

output and income per person, adjusted for inflation, would be higher in the future than

they are now, thanks to the continued growth of productivity.)

• Federal spending on interest payments would rise, thus requiring the government to raise

taxes, reduce spending for benefits and services, or both to achieve any targets that it

might choose for budget deficits and debt.

• The large amount of debt would restrict policymakers’ ability to use tax and spending

policies to respond to unexpected challenges, such as economic downturns or financial

crises. As a result, those challenges would tend to have larger negative effects on the

economy and on people’s well-being than they would otherwise. The large amount of

debt could also compromise national security by constraining defense spending in times

of international crisis or by limiting the country’s ability to prepare for such a crisis.”

Source: Congressional Budget Office, “The 2015 Long-Term Budget Outlook,” June 16, 2015