

CBO : Debt crisis looms absent major policy changes

By ANDREW TAYLOR The Associated Press

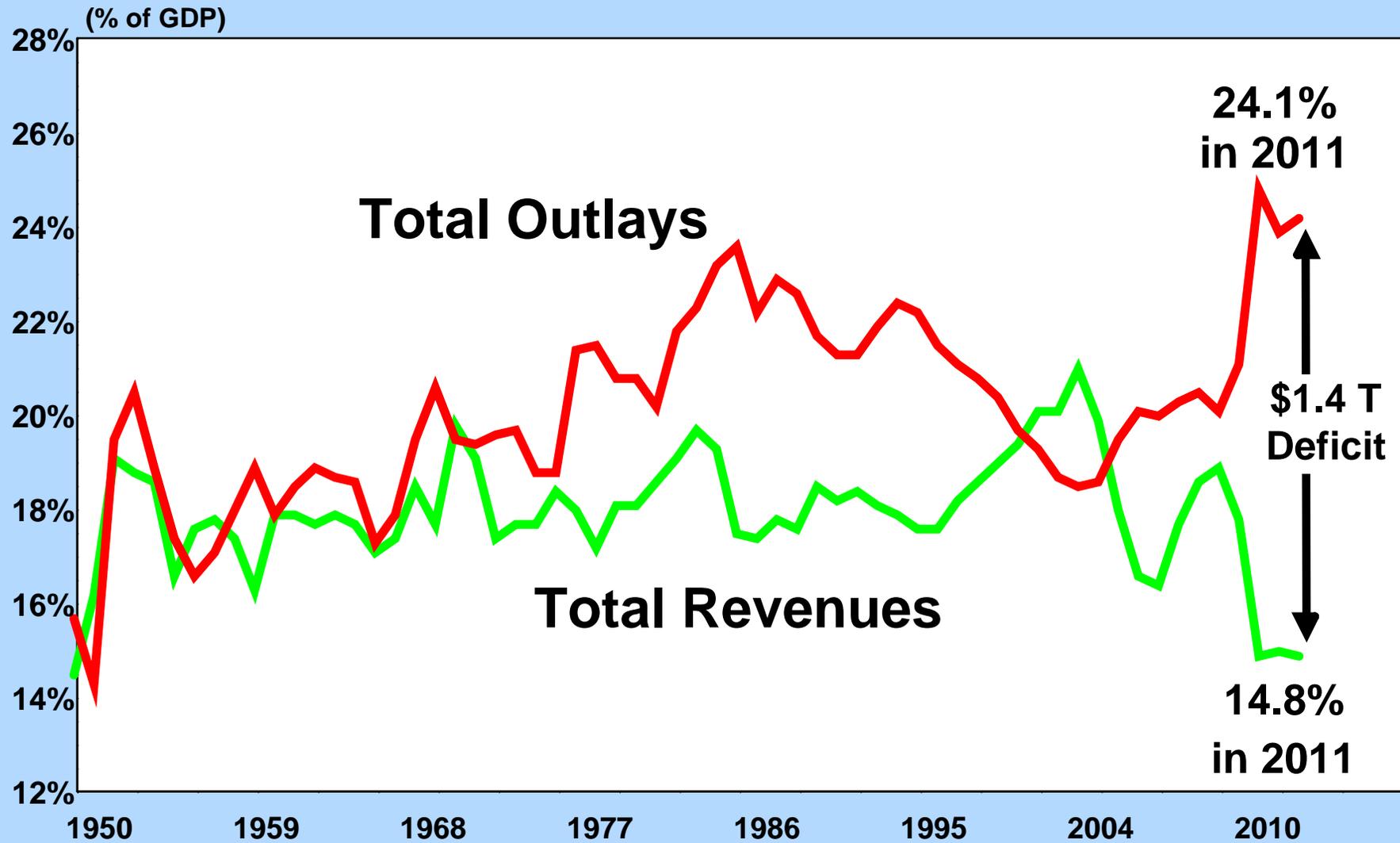
WASHINGTON (AP) — A new report says that the national debt is on pace to equal the annual size of the economy within a decade, levels that could provoke a European-style debt crisis unless policymakers in Washington can slam the brakes on spiraling deficits. The Congressional Budget Office study offers a fresh reminder of what's at stake in ongoing talks led by Vice President Joe Biden that are aimed at cutting more than \$2 trillion from the federal deficit over the coming decade as the price for permitting the government to take on more debt to pay current obligations. CBO says the debt increases the probability of a fiscal crisis in which investors lose faith in U.S. bonds and force policymakers to make drastic spending cuts or tax hikes.

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U.S. Currently Borrowing 40 Cents of Every Dollar It Spends



Spending and Revenues



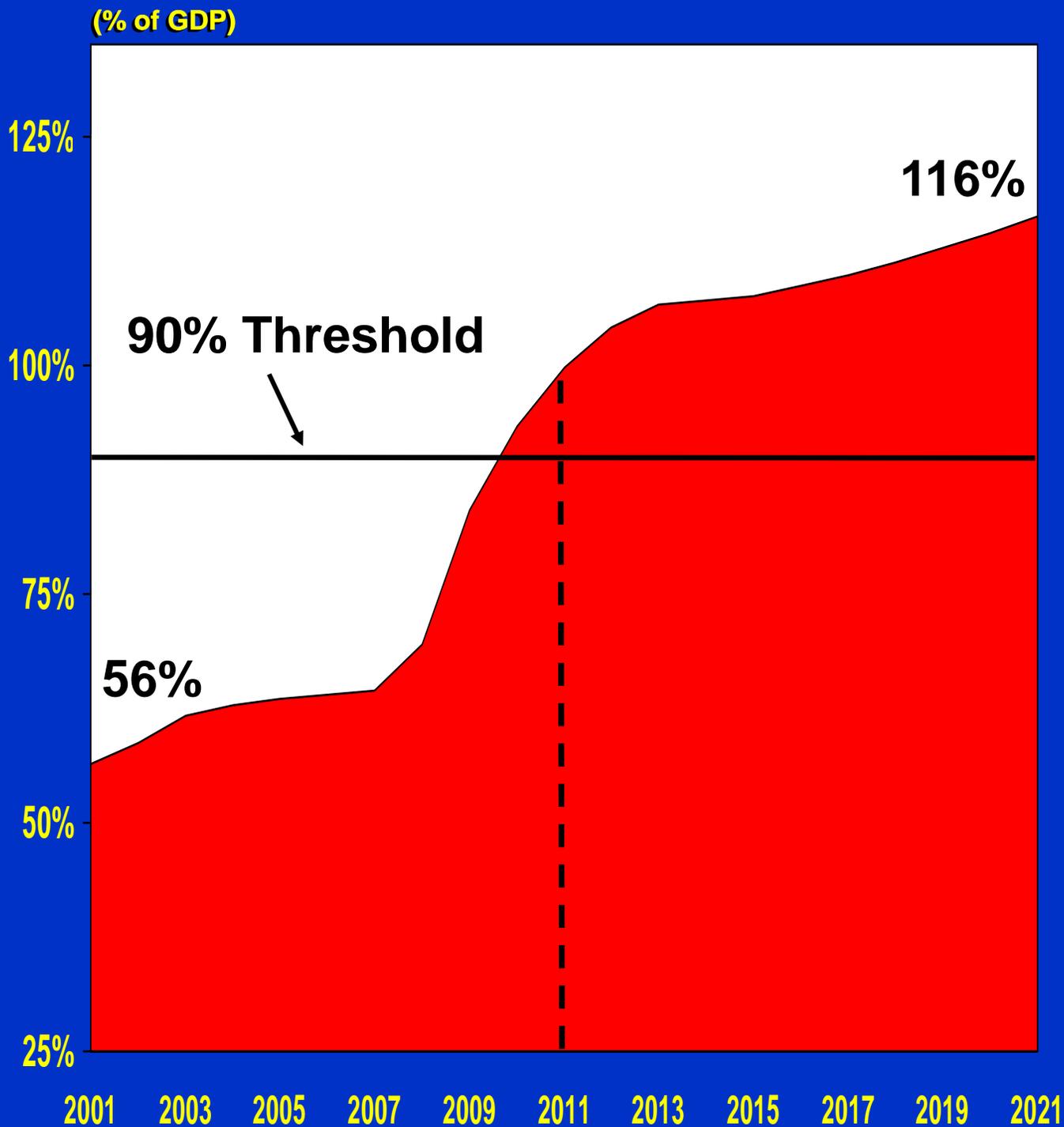
Sources: OMB, CBO

Admiral Mullen on Debt Threat

**“Our national debt is
our biggest national
security threat.”**

**–Admiral Mike Mullen, Chairman of
the Joint Chiefs of Staff
“Tribute to the Troops” Breakfast
June 24, 2010**

Gross Debt as Percent of GDP



Source: OMB, CBO

Note: 2011-2021 reflects CBO March 2011 baseline adjusted for extension of middle-class tax cuts, estate tax at 2009 levels, AMT relief, Doc fix extended, and CBO drawdown scenario.

Economists Reinhart and Rogoff on Danger of Gross Debt Above 90 Percent of GDP Threshold

“We examine the experience of 44 countries spanning up to two centuries of data on central government debt, inflation and growth. Our main finding is that across both advanced countries and emerging markets, high debt / GDP levels (90 percent and above) are associated with notably lower growth outcomes.”

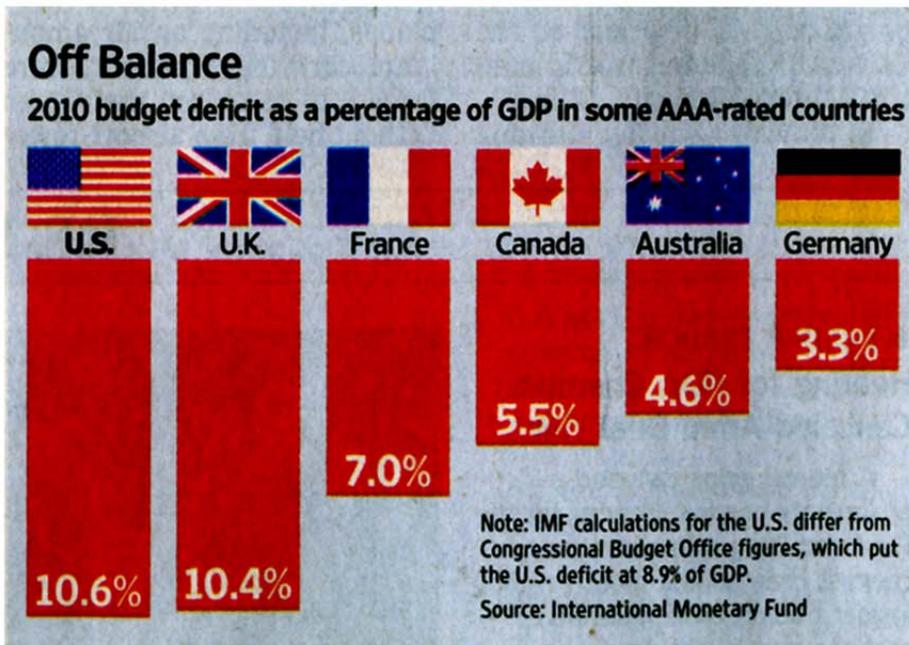
**– Carmen M. Reinhart and Kenneth S. Rogoff
“Growth in a Time of Debt,” American
Economic Review: Papers & Proceedings
May 2010**

THE WALL STREET JOURNAL.

TUESDAY, APRIL 19, 2011

U.S. Warned on Debt Load

S&P Signals Top Credit Rating Is in Danger, Stoking Political Battle on Deficit



BY DAMIAN PALETTA
AND E.S. BROWNING

A blunt warning Monday from a credit-rating firm about the U.S. government's mounting debt pushed stock markets lower and intensified political divisions in Washington about how best to tackle growing deficits.

Both the Obama administration and House Republicans scrambled to gain leverage from Standard & Poor's changing its outlook on U.S. Treasury securities to "negative" from "stable."

S&P didn't lower its top-notch AAA-bond rating for U.S. government Treasury securities, and

their prices initially fell but later rebounded amid optimism that the report could serve as a catalyst to force both sides in Washington to compromise.

The Dow Jones Industrial Average fell 140.24 points, or 1.14%, to 12201.59, its biggest decline in a month, after earlier tumbling

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Deficit Attention

- Capital Journal: Dueling narratives on the debt..... A7
- The Intelligent Investor: Markets should recover..... A7
- Dow falls 140.24 points..... C1

**Every one percentage
point increase in
interest rates adds
\$1.3 T to deficits
over ten years.**

Source: CBO

Note: Increase in interest rates above current baseline levels.

Unsustainable Budget Threatens Nation

By: 10 Ex-Chairs of the President's Council of Economic Advisers
March 24, 2011

Repeated battles over the 2011 budget are taking attention from a more dire problem—the long-run budget deficit.

Divided government is no excuse for inaction. The bipartisan National Commission on Fiscal Responsibility and Reform, under co-chairmen Erskine Bowles and Alan Simpson, issued a report on the problem in December supported by 11 Democrats and Republicans — a clear majority of the panel's 18 members.

As former chairmen and chairwomen of the Council of Economic Advisers, who have served in Republican and Democratic administrations, we urge that the Bowles-Simpson report, "The Moment of Truth," be the starting point of an active legislative process that involves intense negotiations between both parties.

There are many issues on which we don't agree. Yet we find ourselves in remarkable unanimity about the long-run federal budget deficit: It is a severe threat that calls for serious and prompt attention.

While the actual deficit is likely to shrink over the next few years as the economy continues to recover, the aging of the baby-boom generation and rapidly rising health care costs are likely to create a large and growing gap between spending and revenue. These deficits will take a toll on private investment and economic growth that could dwarf 2008.

"The Moment of Truth" could be fixed by just

The commission has well as tax increases

The commission's sp Everything is on the

It also urges significant broaden the tax base help encourage great

The commission's re are incomplete. It pro a number of concrete insurance.

To be sure, we don't already have. Many

Yet we all strongly su well-being. Further s

There are many issues on which we don't agree. Yet we find ourselves in remarkable unanimity about the long-run federal budget deficit: It is a severe threat that calls for serious and prompt attention.... We all strongly support prompt consideration of the Fiscal Commission's proposals. The unsustainable long-run budget outlook is a growing threat to our well-being. Further stalemate and inaction would be irresponsible.

We know the measures to deal with the long-run deficit are politically difficult. The only way to accomplish them is for members of both parties to accept the political risks together. That is what the Republicans and Democrats on the commission who voted for the bipartisan proposal did.

We urge Congress and the president to do the same.

Martin N. Baily, a senior fellow at the Brookings Institution, served as the chairman of the Council of Economic Advisers in the Clinton administration, 1999-2001.

Martin S. Feldstein, an economics professor at Harvard University, served as chairman in the Reagan administration, 1982-4.

R. Glenn Hubbard, dean of the Columbia University Graduate School of Business, served as chairman in the Bush administration, 2001-3.

Edward P. Lazear, economics professor at Stanford University's Graduate School of Business, served as chairman in the Bush administration, 2006-9.

N. Gregory Mankiw, an economics professor at Harvard University and influential blogger, served as chairman in the Bush administration, 2003-5.

Christina D. Romer, economics professor at the University of California, Berkeley, served as the chairwoman in the Obama administration, 2009-10.

Harvey S. Rosen, an economics professor at Princeton University, served as chairman in the Bush administration, 2005.

Charles L. Schultze, a senior fellow emeritus at the Brookings Institution, served as chairman in the Carter administration, 1977-81.

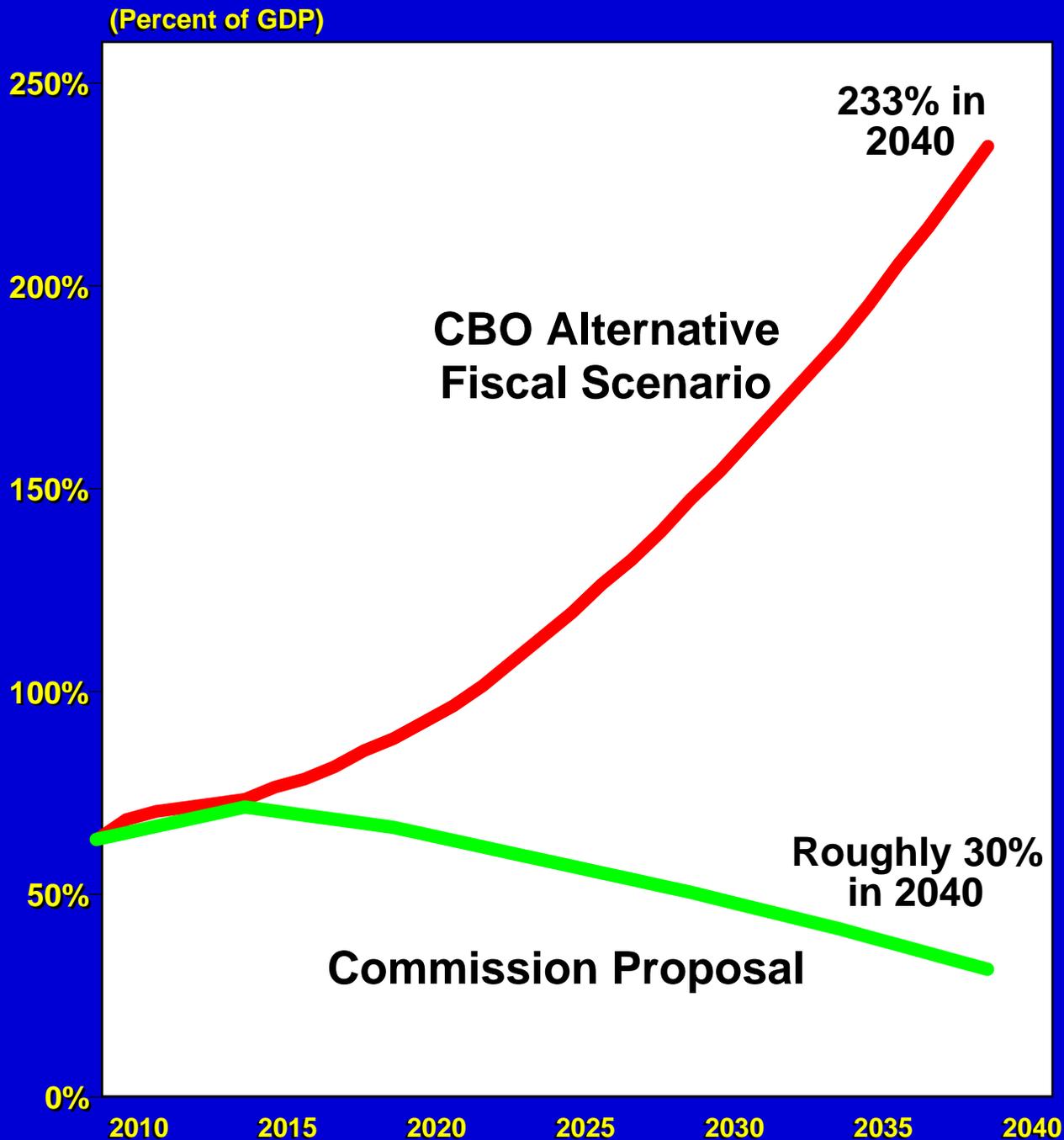
Laura D. Tyson, a professor at the Haas School of Business of the University of California, Berkeley, served as chairwoman in the Clinton administration, 1993-95.

Murray L. Weidenbaum, honorary chairman of the Murray Weidenbaum Center on the Economy, Government and Public Policy at Washington University in St. Louis, served as chairman in the Reagan administration, 1981-82.

Groups Proposing Roughly \$4 T in Deficit Reduction Over Ten Years

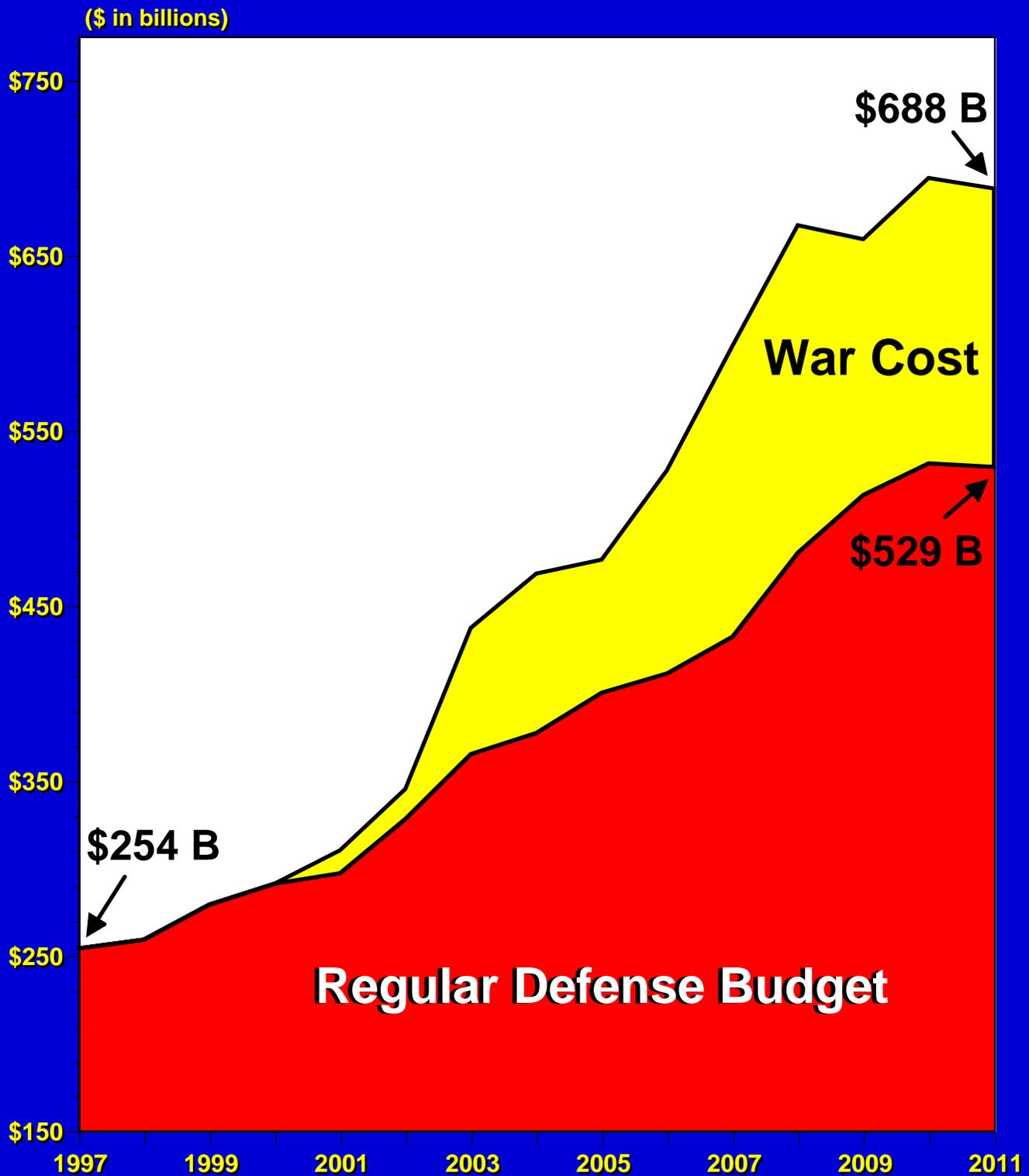
- **Fiscal Commission**
- **Bipartisan Policy Center**
- **American Enterprise Institute**
- **Center for American Progress**
- **Heritage Foundation**
- **Roosevelt Institute**

Debt as Percent of GDP Under Commission Proposal



Source: CBO Long-Term Budget Outlook, June 2010; Report of the National Commission on Fiscal Responsibility and Reform, December 2010

Defense Budget Growth



Source: OMB, CBO

Defense Secretary Gates on Defense Funding

“...[T]he budget of the Pentagon almost doubled during the last decade. But our capabilities didn't particularly expand. A lot of that money went into infrastructure and overhead and, frankly, I think a culture that had an open checkbook.”

–Secretary of Defense Robert Gates
Interview on CBS's *60 Minutes*
May 15, 2011

On the way to a surplus, a \$12 trillion U.S. detour

In 2001, the nation looked to be debt-free in a decade. In 2011, it's anything but.

BY LORI MONTGOMERY

The nation's unnerving descent into debt began a decade ago with a choice, not a crisis.

In January 2001, with the budget balanced and clear sailing ahead, the Congressional Budget Office forecast ever-larger annual surpluses indefinitely. The outlook was so rosy, the CBO said, that Washington would have enough money by the end of the decade to pay off everything it owed.

Voices of caution were swept aside in the rush to take advantage of the apparent bounty. Political leaders chose to cut taxes, jack up spending and, for the first time in U.S. history, wage two wars solely with borrowed funds. "In the end, the floodgates opened," said former senator Pete

Big-ticket spending initiated by the Bush administration accounts for 12 percent of the shift. The Iraq and Afghanistan wars have added \$1.3 trillion in new borrowing. A new prescription drug benefit for Medicare recipients contributed \$272 billion. The Troubled Assets Relief Program bank bailout, which infuriated voters and led to the defeat of several legislators in 2010, added just \$16 billion — and may eventually cost nothing as financial institutions repay the Treasury.

Obama's 2009 economic stimulus, a favorite target of Republi-

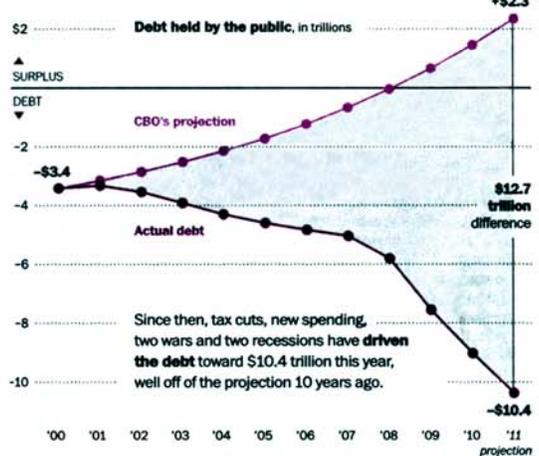
The biggest culprit, by far, has been an erosion of tax revenue triggered largely by two recessions and multiple rounds of tax cuts. Together, the economy and the tax bills enacted under former president George W. Bush, and to a lesser extent by President Obama, wiped out \$6.3 trillion in anticipated revenue. That's nearly half of the \$12.7 trillion swing from projected surpluses to real debt. Federal tax collections now stand at their lowest level as a percentage of the economy in 60 years.

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debt — and of the difficulty of re-balancing the budget without new tax revenue.

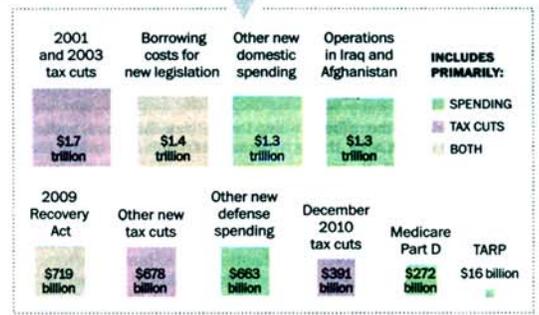
From surplus to debt

In 2000, the United States had \$3.4 trillion in debt held by the public. Based on policies in place at the time, the Congressional Budget Office projected in 2001 that the country could pay off its debt by the year 2008 and by 2011 have a \$2.3 trillion surplus.



How we got here

The difference between the surplus projected for 2011 and the actual debt level is approaching \$12.7 trillion. New legislation, made up of spending as well as tax cuts, contributed to most of this difference.



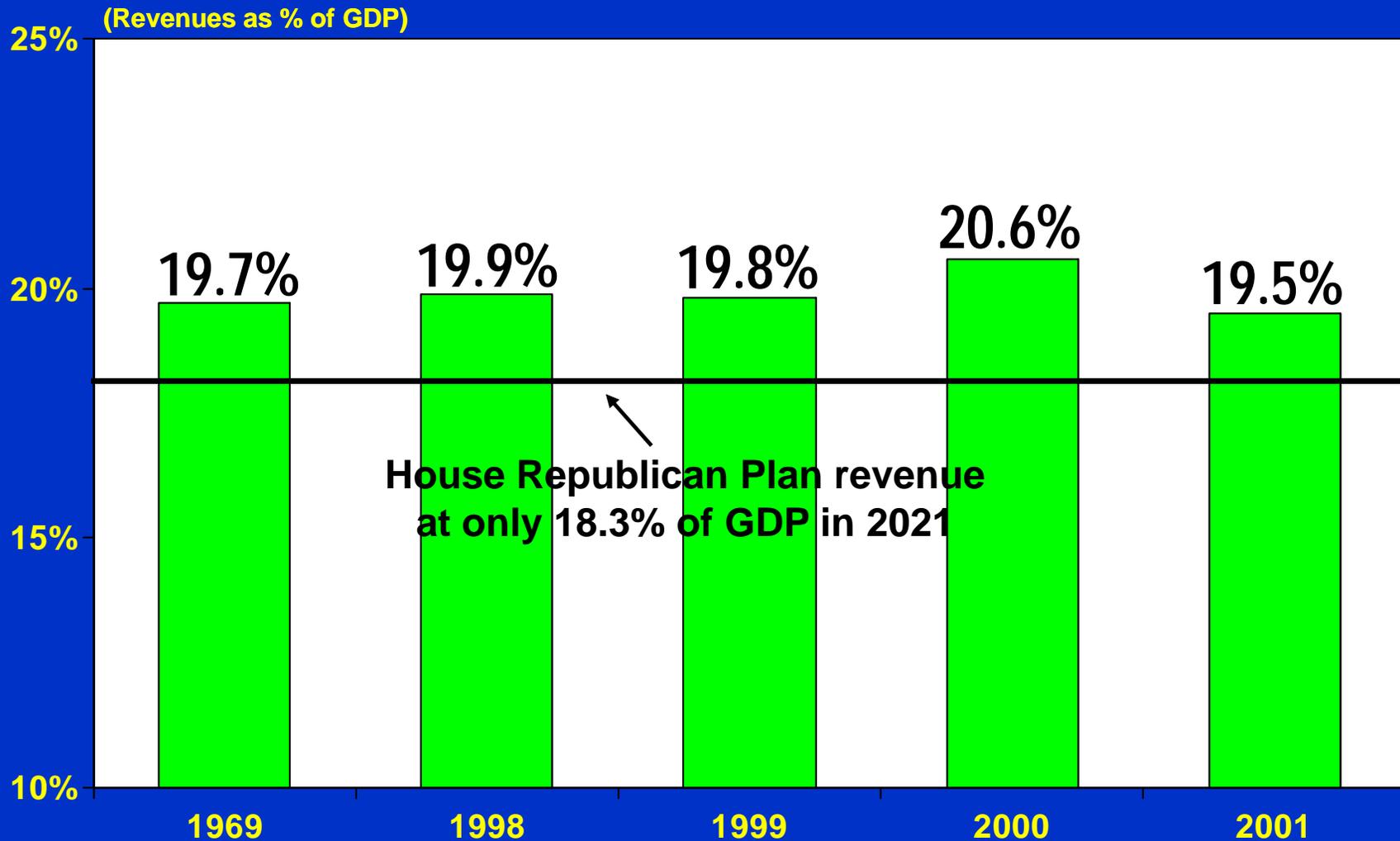
SOURCE: Pew Fiscal Analysis Initiative analysis of CBO data ALICIA PARLAPIANO/THE WASHINGTON POST

document of fiscal discipline in the wake of the surpluses clearly didn't help. "Nobody pushed for paying for this stuff," he said. Not even after "it became very clear in

the middle of 2003 that the line had turned on us. And the surpluses as far as the eye could see were no longer there."

montgomery@washpost.com

Last Five Times Budget in Surplus, Revenues Near 20% of GDP



Source: OMB

Economist Feldstein on Need to Reduce Tax Expenditures

“Cutting tax expenditures is really the best way to reduce government spending.... [E]liminating tax expenditures does not increase marginal tax rates or reduce the reward for saving, investment or risk-taking. It would also increase overall economic efficiency by removing incentives that distort private spending decisions. And eliminating or consolidating the large number of overlapping tax-based subsidies would also greatly simplify tax filing. In short, cutting tax expenditures is not at all like other ways of raising revenue.”

**– Martin Feldstein
Professor of Economics at Harvard University
Chairman of Council of Economic Advisers under President Reagan
“The ‘Tax Expenditure’ Solution for Our National Debt,”
Wall Street Journal
July 20, 2010**

Fed Chairman Bernanke on Economic Benefit of Acting Now to Address Long-Term Debt

“Acting now to develop a credible program to reduce future deficits would not only enhance economic growth and stability in the long run, but could also yield substantial near-term benefits in terms of lower long-term interest rates and increased consumer and business confidence.”

**– Federal Reserve Chairman Ben S. Bernanke
Testimony before House Budget Committee
February 9, 2011**