

INFORMED BUDGETEER

CBO ECONOMIC AND BUDGET OUTLOOK

| CBO BASELINE SURPLUS/DEFICITS<br>January 1998 (\$ in Billions, - Deficit) |                   |                    |                     |                               |
|---------------------------------------------------------------------------|-------------------|--------------------|---------------------|-------------------------------|
|                                                                           | Unified<br>Budget | Social<br>Security | Budget <sup>A</sup> | Freeze<br>Budget <sup>B</sup> |
| 1999                                                                      | -2                | 113                | -115                | -115                          |
| 2000                                                                      | -3                | 123                | -126                | -126                          |
| 2001                                                                      | 14                | 130                | -116                | -116                          |
| 2002                                                                      | 69                | 139                | -70                 | -70                           |
| 2003                                                                      | 54                | 148                | -94                 | -78                           |
| 2004                                                                      | 71                | 158                | -87                 | -53                           |
| 2005                                                                      | 75                | 170                | -95                 | -42                           |
| 2006                                                                      | 115               | 179                | -64                 | 9                             |
| 2007                                                                      | 129               | 189                | -60                 | 35                            |
| 2008                                                                      | 138               | 197                | -59                 | 59                            |
| 1999-2003                                                                 | 132               | 653                | -521                | -505                          |
| 1999-2008                                                                 | 660               | 1546               | -886                | -497                          |

<sup>A</sup>Excluding Social Security Trust Fund balances. <sup>B</sup>Excludes Social Security Trust Fund balances and assumes discretionary spending is frozen at 2002 level through 2008.

SOURCE: CBO Economic and Budget Outlook, January 1998.

TIGHT CAPS

- The Balanced Budget Act of 1997 (BBA) sets limits on discretionary spending and provides for across-the-board cuts if annual appropriations exceed those limits.
- The statutory caps -- first enacted in 1990 -- are in effect through 2002. For 1998 and 1999 the law splits the caps into three categories: defense, nondefense, and violent crime. For years 2000 through 2002, the categories are collapsed into total discretionary pot.

| CBO BASELINE: BBA DISCRETIONARY CAPS<br>(\$ Billions) |    |       |       |       |       |       |        |
|-------------------------------------------------------|----|-------|-------|-------|-------|-------|--------|
|                                                       |    | 1998  | 1999  | 2000  | 2001  | 2002  | Total  |
| <b>BBA Discretionary</b>                              |    |       |       |       |       |       |        |
| Defense                                               | BA | 269.0 | 271.5 | 275.4 | 281.8 | 289.6 | 1387.3 |
|                                                       | OT | 267.1 | 266.6 | 269.0 | 270.7 | 273.1 | 1346.4 |
| Nondefense                                            | BA | 259.0 | 261.5 | 261.8 | 260.2 | 261.5 | 1304.0 |
|                                                       | OT | 290.5 | 294.5 | 295.3 | 293.7 | 287.7 | 1461.8 |
| TOTAL                                                 | BA | 528.0 | 533.0 | 537.2 | 542.0 | 551.1 | 2691.3 |
|                                                       | OT | 557.6 | 561.1 | 564.3 | 564.4 | 560.8 | 2808.2 |
| <b>CBO Baseline Freeze</b>                            |    |       |       |       |       |       |        |
| Defense                                               | BA | 268.5 | 268.5 | 268.5 | 268.5 | 268.5 | 1342.3 |
|                                                       | OT | 268.8 | 268.1 | 269.7 | 264.1 | 266.6 | 1337.3 |
| Nondefense                                            | BA | 258.9 | 261.2 | 261.2 | 261.1 | 261.2 | 1303.7 |
|                                                       | OT | 288.4 | 296.5 | 298.0 | 295.7 | 294.4 | 1473.1 |
| TOTAL                                                 | BA | 527.4 | 529.7 | 529.7 | 529.5 | 529.7 | 2646.0 |
|                                                       | OT | 557.2 | 564.6 | 567.7 | 559.8 | 561.0 | 2810.4 |
| <b>BBA vs. Freeze</b>                                 |    |       |       |       |       |       |        |
| Defense                                               | BA | 0.5   | 3.0   | 6.9   | 13.4  | 21.2  | 45.0   |
|                                                       | OT | -1.7  | -1.5  | -0.7  | 6.6   | 6.5   | 9.2    |
| Nondefense                                            | BA | 0.1   | 0.3   | 0.6   | -0.9  | 0.2   | 0.3    |
|                                                       | OT | 2.1   | -2.0  | -2.7  | -2.0  | -6.7  | -11.3  |
| TOTAL                                                 | BA | 0.6   | 3.3   | 7.5   | 12.5  | 21.4  | 45.3   |
|                                                       | OT | 0.4   | -3.5  | -3.4  | 4.6   | -0.2  | -2.2   |

NOTE: Non-defense category includes crime trust fund spending. Source: SBC Majority Staff.

- A budget resolution that assumed an increase in spending above these caps would be subject to a 60 vote point of order. Further, even if the point of order were waived and subsequent appropriations passed that exceeded the spending caps, unless underlying statutory law were changed (requiring the waiver of another 60 vote point of order), an automatic across the board spending cut would be triggered to bring spending back to the cap level.
- The table above summarizes the spending caps for defense and non-defense in 1998 and 1999, and the aggregate spending caps for 2000 through 2002. For 2000 through 2002, the table allocates the aggregate cap to defense and nondefense as was

assumed in the BBA -- however they are not binding.

- For the upcoming 1999 appropriation cycle and beyond, the table indicates very tight caps. **If every program received the same appropriation in 1999 at the levels they received in 1998 (CBO Baseline Freeze), the outlay spending caps would be exceeded by \$3.5 billion.**

SOMETIMES YOU GET THE BEAR,  
SOMETIMES IT GETS YOU

- While much of the surprising drop in the 1997 deficit resulted from higher than expected revenues, outlays fell short of the amount estimated by \$20 billion. This compounded the beneficial effects of the additional revenues, thereby cheering the economy but puzzling estimators.
- What caused the \$20 billion drop?
- For the half a trillion dollars that is the discretionary part of the budget, the law of offsetting errors worked as one hopes. While defense and international affairs spending exceeded assumptions by \$5 billion, all other discretionary programs spent \$5 billion less than estimated, producing no net error. See the table below.

| ACTUAL OUTLAYS FALL SHORT OF BUDGET<br>RESOLUTION ASSUMPTIONS FOR 1997<br>(\$ in Billions) |                      |                 |              |   |           |
|--------------------------------------------------------------------------------------------|----------------------|-----------------|--------------|---|-----------|
| Budget Function                                                                            | Budget<br>Resolution | 1997<br>Actuals | Difference   |   |           |
|                                                                                            |                      |                 | Amount       | % |           |
| <b>Discretionary:</b>                                                                      |                      |                 |              |   |           |
| Defense                                                                                    | 267.5                | 271.9           | 4.4          |   | 2         |
| International Affairs                                                                      | 19.2                 | 19.8            | 0.6          |   | 3         |
| <u>All Others</u>                                                                          | <u>261.8</u>         | <u>256.9</u>    | <u>-5.0</u>  |   | <u>-2</u> |
| TOTAL Discretionary                                                                        | 548.5                | 548.5           | --           |   | --        |
| <b>Mandatory:</b>                                                                          |                      |                 |              |   |           |
| Natural Resources                                                                          | 0.8                  | 0.2             | -0.6         |   | -175      |
| Agriculture                                                                                | 5.8                  | 4.9             | -0.8         |   | -14       |
| Commerce                                                                                   | -12.4                | -16.4           | -4.0         |   | 32        |
| Education                                                                                  | 10.0                 | 13.6            | 3.7          |   | 37        |
| Health                                                                                     | 103.6                | 100.5           | -3.1         |   | -3        |
| Medicare                                                                                   | 188.6                | 187.4           | -1.2         |   | -1        |
| Income Security                                                                            | 197.0                | 191.4           | -5.6         |   | -3        |
| General Government                                                                         | 2.0                  | 0.7             | -1.3         |   | -66       |
| Interest                                                                                   | 247.7                | 245.4           | -2.3         |   | -1        |
| Off. Receipts                                                                              | -47.4                | -50.0           | -2.6         |   | 5         |
| <u>All Other Mandatory</u>                                                                 | <u>377.9</u>         | <u>375.3</u>    | <u>-2.6</u>  |   | <u>-1</u> |
| TOTAL Mandatory                                                                            | 1073.4               | 1053.1          | -20.4        |   | -2        |
| <b>Total:</b>                                                                              |                      |                 |              |   |           |
| Discretionary                                                                              | 548.5                | 548.5           | --           |   |           |
| <u>Mandatory</u>                                                                           | <u>1073.4</u>        | <u>1053.1</u>   | <u>-20.4</u> |   |           |
| TOTAL                                                                                      | 1621.9               | 1601.6          | -20.4        |   |           |

SOURCE: SBC Majority Staff

- For the mandatory side of spending (\$1.1 trillion), most of the differences between actual outlays and amounts assumed in the budget resolution were in the same direction--producing net outlays that fell \$20.4 billion short of the amount assumed.
- While that is only a 2 percent error, some of the programs that contributed to that shortfall had larger percentage errors. For example, Postal Service profits that exceeded expectations by \$1.1 billion, increases in deposit insurance fund recoveries of \$1.9 billion, and increased collections by the Federal Housing Administration of \$0.9 billion all contributed to the decrease in outlays in the Commerce function.
- In Income Security, outlays slowed primarily in unemployment insurance (by \$2.1 billion) and in family support payments (by \$3.2 billion). Medicaid outlays, likely subject to similar forces, also proved lower than expected by \$3.1 billion.

BUDGET 101: OMB PROPOSED CONCEPT CHANGE  
FOR TRANSPORTATION

- The Office of Management and Budget has proposed to redefine the obligation limitations placed on transportation programs by the Appropriations Committee as discretionary budget authority. Most of the time, OMB changes in budget definitions and concepts are not controversial. This proposed change is one of the few exceptions.
- Currently, budget authority for highway, mass transit, highway safety, and the Airport Improvement Program (AIP) is provided in the form of contract authority from the authorizing committees. Spending on these programs is controlled by the Appropriations Committee when they set obligation limitations on these programs. The obligation limitation determines the annual amount of spending for these programs.
- The purpose of this change is to provide a uniform treatment for all programs subject to obligation limitations. This change would also eliminate the large gap that appears to exist between the discretionary BA and outlay caps.
- Under current budget enforcement rules, OMB is required to adjust the discretionary spending caps for this and other conceptual changes. Making these obligation limitations discretionary BA would require the BA cap to be raised by approximately \$28 billion in 1998 and 1999, rising to \$30 billion in 2002.
- The authorizing committees for these transportation programs have voiced their opposition to this change, stating this action would lead to the elimination of contract authority from their committees and prevent long-term planning and certainty in transportation. OMB denies this would be the result of this change.
- At this time, the Budget Committee is withholding comment on this issue until the President’s budget is released, along with the accompanying Preview Report.

ECONOMICS

BUDGET COMMITTEE LEARNS ABOUT EMU

- Chairman Domenici recently led a group of Budget Committee Senators to Europe to learn more about the upcoming European Monetary Union (EMU). EMU will begin January 1, 1999, when up to 11 members of the EU will adopt the single “euro” currency. The Senators met with senior European political and monetary officials, reviewing the existing preparations for EMU and the challenges that lay ahead.
- EMU holds many prospective benefits for Europe and the global economy. It will reduce hedging needs and will increase transparency, since cross border prices will more comparable. This should lead to increased competition within the EMU zone and a harmonization of tax and regulatory policy toward the level of least burden .
- EMU has already yielded benefits - EMU’s strict entrance requirements have induced countries to pursue credible fiscal and monetary policies. Prospective entrants now have low inflation and fiscal deficits at or below 3 percent of GDP-- this contrasts with Italy’s and France’s 1993 fiscal deficits of 10% and 6% of GDP respectively.
- Despite this progress, the Senators learned that EMU still faces challenges. Europe’s labor market rigidities and the lack of a supranational fiscal authority will make it harder for any one country to recover from a localized recession. Similarly, Europe’s escalating pension costs will make it difficult to uphold EMU’s fiscal deficit limits without significant reforms. European officials of all parties acknowledge these challenges. However, they believe EMU may make it easier to enact unpopular reforms given the presence of an outside mandate.

- The main risk for the US is likely if EMU disappoints, for this might cause Europe to turn inward. Thus, the Senators believe the US is best served if EMU succeeds.
- After meeting with various US Chambers of Commerce, it appears that large US multinationals and exporters will be ready for the euro’s launch in 1999. It is important to ensure that small US businesses are equally prepared. There are some issues that may still need to be resolved in the U.S. The appropriate legislative committees of jurisdiction will want to review -- questions as to whether the euro conversion is a taxable event and whether investments related to the conversion can be expensed.

CALENDAR

February 2: Release of the President’s FY 1999 Budget.

February 2: Chairman Domenici and Chairman Kasich will hold a press conference to discuss the President’s FY 1999 Budget submission. Radio/TV Gallery, 3pm. (For credentialed press only).

Senate Budget Committee Hearing Schedule

February 3: The President's FY1999 Budget. Witnesses: Treasury Secretary Robert Rubin, accompanied by Jack Lew, Deputy OMB Director. Dirksen 608, 10:00 am

February 4: The President’s FY1999 Budget. Witnesses: Office of Management and Budget Director Franklin Raines. Dirksen 608, 10:00 am.

February 9: Education Task Force Field Hearing: State & Local Initiatives: Engines for Change. Witnesses: Lamar Alexander, Former U.S. Secretary of Education; Jane Walters, Commissioner, Tennessee Department of Education; Judy Beasley, Vice-President, Tennessee Education Association; Dr. Susan Gendrich-Cameron, Principal, Cason Lane Academy; Dr. James Guthrie, Director, Peabody Center for Education, Vanderbilt University; Mr. Randle Richardson, President & CEO, Community Education Partners. Location: Middle Tennessee State University, Murfreesboro, TN, 9:30-11:30 am.

February 10: Causes of recent unexpected revenue growth. Witnesses: David Wyss, Chief Economist, Standard & Poor's DRI; James Glassman, Vice President, Chase Securities, Inc.; John G. Wilkins, National Director, Tax Policy Economics, Coopers and Lybrand. Dirksen 608, 10:00 am.

February 11: Federalism & Funding Issues. Witnesses: Ray Scheppach, Director, National Governor’s Association; William Pound, Director, National Conference of State Legislatures, Larry Naake, Director, National Association of Counties; and National League of Cities. Dirksen 608, 10:00 am.

February 11: Education Task Force Meeting. Dirksen 608, 2:00 pm

February 12: Unfunded Mandates Task Force Meeting. Dirksen 608..