Committee on the Budget
United States Senate
Hearing on "Reforming the Federal Budget Process: The Need for Action"
October 21, 2015

Statement of Michael A. Peterson
President and CEO, Peter G. Peterson Foundation

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Good morning Chairman Enzi, Ranking Member Sanders, and members of the Committee.

Thank you for the opportunity to appear before you today to discuss how budget process reform can help secure a brighter fiscal and economic future for our nation.

The Peterson Foundation is a non-partisan organization. Our mission is to increase awareness and accelerate action on America's long-term fiscal challenges, because we believe that our unsustainable fiscal outlook is a serious threat to our future. Our Foundation works with policy experts from across the political spectrum to educate and engage Americans, and build support for solutions.

Today's hearing is important because the current budget process hinders our ability to address these challenges. While process alone is not responsible for our growing debt, the current federal budget process keeps policy focused on the short-term, reinforces the tendency to go from crisis to crisis, and diverts attention from the key drivers of the budget over the long term.

Let me begin by providing some context. Current annual deficits are down from $1.4 trillion at the height of the great recession, to $440 billion today. Even though that's still a large deficit, that's a significant improvement.

The more significant problem is the trajectory of debt over the long term. The Congressional Budget Office projects that within 25 years, debt held by the public could climb to more than 100% of GDP under current law, and to a staggering 175% of GDP under less optimistic assumptions. By any definition, the fiscal path we are on is unsustainable and dangerous.

We need a more effective, forward-looking budget process, because there are severe consequences of our current fiscal path.

Most directly, interest costs will consume a huge amount of the federal budget. Over the next ten years alone, CBO projects that interest costs will be more than $5 trillion under current law. Under CBO's alternative fiscal scenario, interest costs will become the third largest category of the budget in 2023, the second largest category in 2032, and the single largest category by 2040. With our many important budget priorities, none of us wants interest to become the largest government program.

Higher interest costs would crowd out important public investments that can fuel economic growth. Discretionary spending is already on a path to fall to well below historical averages. A nation saddled with debt will have even less to invest in its own future.

In addition, growing federal debt reduces the amount of private capital for investments, which hurts economic growth and wages.

Furthermore, this fiscal path would lower income levels. CBO projects that our debt will reduce incomes by $6,000 per person in 2040. We are all very concerned about the lack of growth in low and median incomes, and the growing disparities in income and wealth. At the very least, the federal government should not let its own budget imbalances contribute to these very harmful trends.

In addition, on our current path, we are at greater risk for a fiscal crisis. And it leaves us with much less fiscal flexibility to deal with future economic crises. If we faced another major recession like 2008, we may not be as able to work our way out.

Lastly, and in many ways most importantly, this high level of debt imperils the safety net and the most vulnerable in our society. If our government does not have the resources and the stability of a sustainable budget, these essential programs, and those who need them most, are put in jeopardy. We can't let that happen.

On the other hand, a strong fiscal outlook is a foundation for a growing, thriving economy. Putting our nation on a sustainable fiscal path creates a positive environment for growth, opportunity and prosperity. With a strong fiscal foundation, the nation will have increased access to capital, more resources for private and public investments in our future, improved consumer and business confidence, and a stronger safety net.

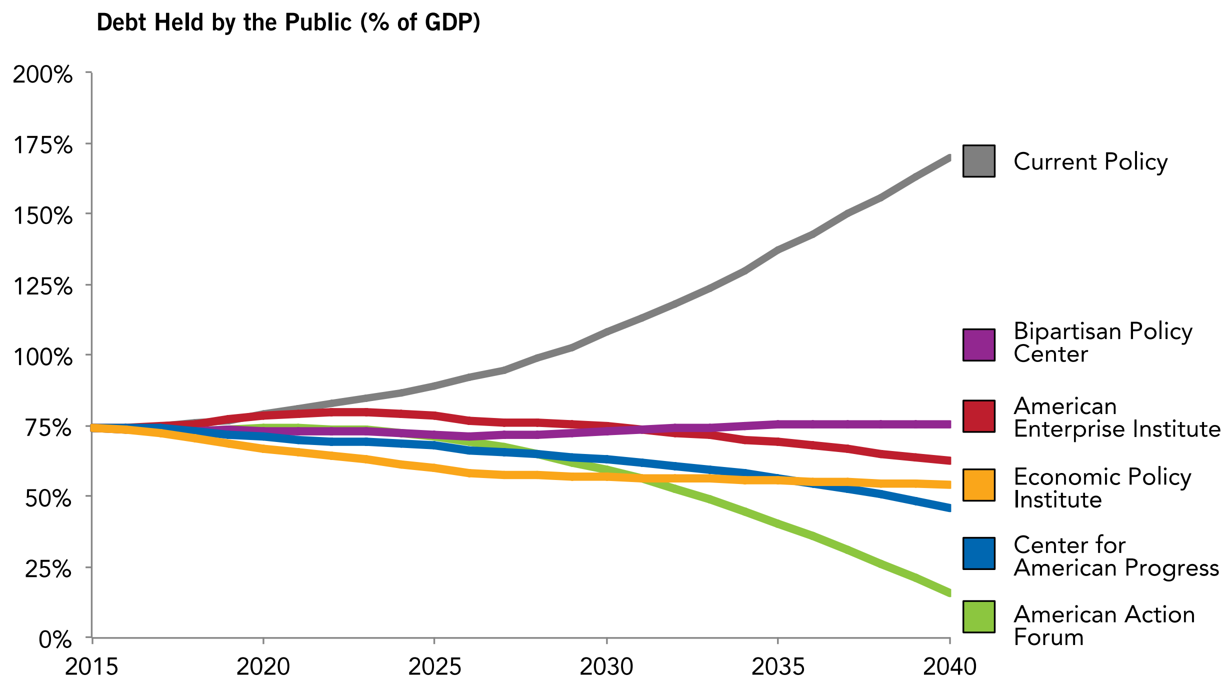
Our long-term debt problem stems from a structural mismatch between spending and revenue. The primary drivers of long-term spending are relatively simple: first, the nearly 80 million Baby Boomers are beginning to retire; second, older Americans are living much longer and therefore will spend more years in retirement; and third, the cost of healthcare in the U.S. is very high and (despite some recent improvements) is still growing faster than the economy. These structural factors are combined with a tax system that is inadequate, broken, and unfair, and fails to generate sufficient revenue to fund these programs. Put these facts together, and it leaves the United States on a dangerous long-term fiscal and economic path.

The good news is that there are plenty of solutions to choose from. One of the Peterson Foundation's most important projects is the Solutions Initiative, which brings together policy organizations from across the political spectrum to develop long-term fiscal plans.

Experts from five leading think tanks participated: the American Action Forum, the American Enterprise Institute, the Bipartisan Policy Center, the Center for American Progress, and the Economic Policy Institute. Each of these organizations developed specific, "scoreable" proposals. And I'm very proud to report that all of them successfully stabilized debt as a share of the economy over the long term.

While these very different organizations have a wide range of priorities, their plans demonstrate that comprehensive solutions do exist.

Solutions do exist: PGPF Solutions Initiative plans from five think tanks show stable or declining federal debt through 2040



SOURCE: Peter G. Peterson Foundation, *Solutions Initiative III*, May 2015. See pgpf.org/solutions-initiative-iii for more details.
NOTE: Current policy is defined as the alternative fiscal scenario without economic feedback from CBO's *2014 Long-Term Budget Outlook*.

It's also very important that we get started soon on fiscal reforms. According to CBO's alternative fiscal scenario, the current fiscal gap is 3.2% of GDP, which means that, in order to stabilize our debt, we need spending cuts or revenue increases or a combination of both, that total 3.2% of GDP. If we wait just 5 years, the amount of reforms we need grows by 24%. If we wait 10 years, the amount of reforms we need grows by 66%. Like any debt problem, the sooner you start to tackle it, the easier it is to solve.

Finally, let me close with a brief discussion of budget process.

The current, flawed federal budget process diverts attention away from our critical long-term challenges, and has contributed to an unfortunate recent pattern of gridlock and government-by-crisis – with significant economic costs for our nation. Our foundation commissioned a study by Macroeconomic Advisers, which estimated that that the uncertainty created by fiscal brinksmanship from 2010 to 2013 increased the unemployment rate by 0.6%, the equivalent of 900,000 jobs.

While budget process reforms alone cannot solve our fiscal challenges, there are various changes that would better encourage long-term fiscal planning. Let me highlight three key principles for you to consider:

First: look further into the future. The current Congressional "budget window" looks out only 10 years. We would recommend increasing that to 25 years. If we don't look further out, then there's no meaningful discussion of long-term trends, there's no visible information about long-term effects, and there's no credit given for long-term improvement. This is perhaps the single most important change that would encourage better long-term budgeting.

Secondly, set goals. Requiring Congress and the president to set medium- and long-term fiscal goals, and then report on progress annually, would improve accountability and transparency.

Lastly, improve enforcement. Adding new or strengthening existing enforcement measures would help lawmakers meet budget targets. Of course, measures should be flexible enough to accommodate changing conditions, but they should be strong enough to reinforce the commitment to long-term fiscal sustainability.

In summary, we have a long-term fiscal challenge that could do great damage to our nation's economy and role in the world. We know the causes. And we know the range of solutions. All it takes is leadership, commitment, honesty and cooperation. The Peterson Foundation is committed to helping our nation, and both political parties, to address this challenge successfully.

Thank you for your invitation to participate in this important discussion. I would be happy to answer any questions you may have.

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Selected Charts for the Senate Budget Committee

October 21, 2015

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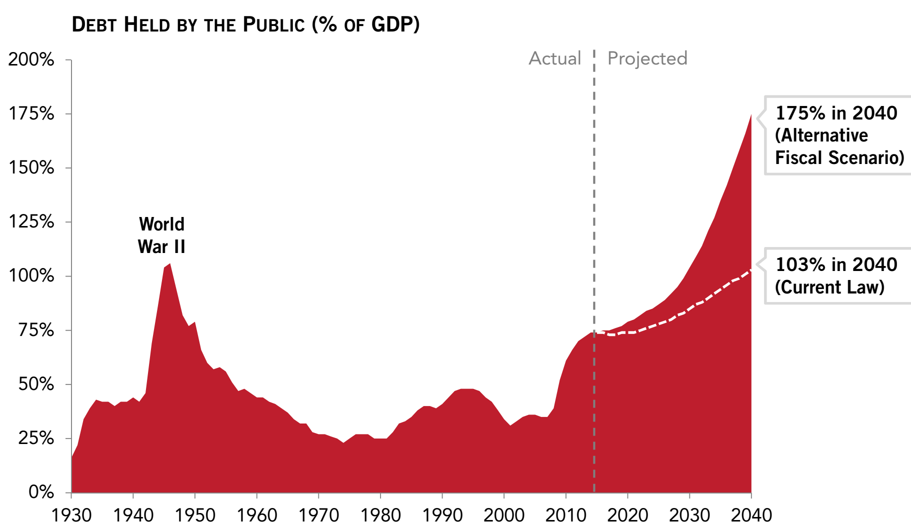
U.S. debt is on an unsustainable path



SOURCE: Congressional Budget Office, *The 2015 Long-Term Budget Outlook*, June 2015. Compiled by PGPF.
NOTE: Current law projections are from CBO's extended baseline scenario. Data for the alternative fiscal scenario include economic feedback.

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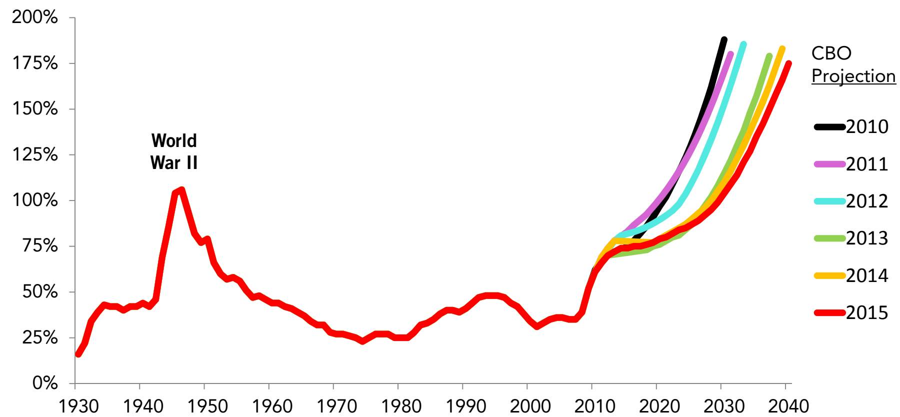
U.S. debt – Recent improvements have only delayed an unsustainable trajectory

DEBT HELD BY THE PUBLIC (% OF GDP)



SOURCE: Congressional Budget Office, *The 2015 Long-Term Budget Outlook* (June 2015), *The 2014 Long-Term Budget Outlook (July 2014), The 2013 Long-Term Budget Outlook (September 2013), The 2012 Long-Term Budget Outlook (June 2012), The 2011 Long-Term Budget Outlook (June 2011) , and The 2010 Long-Term Budget Outlook (June 2010).* Compiled by PGPF.
NOTE: Projections are based on CBO's alternative fiscal scenario with economic feedbacks. The projection use the midpoint of CBO's estimate of economic feedbacks.

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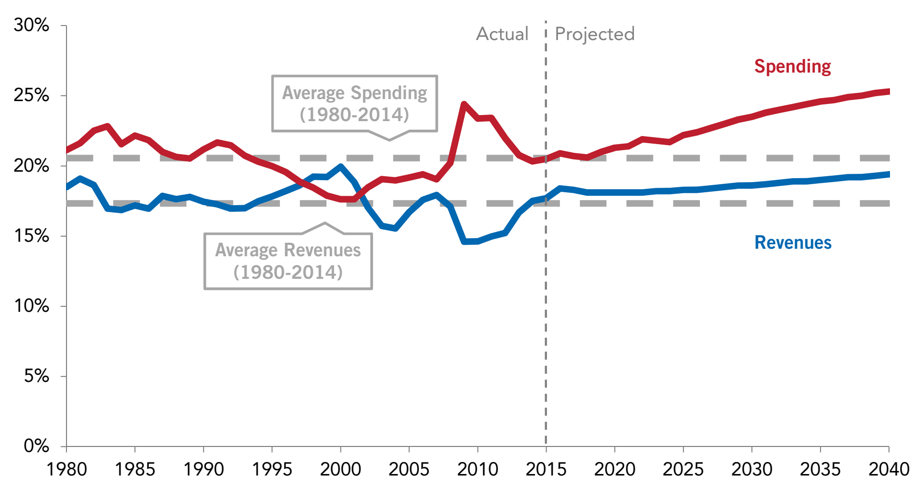
The growing debt is caused by a structural mismatch between spending and revenues

FEDERAL REVENUES AND SPENDING (% OF GDP)



SOURCE: Congressional Budget Office, *The 2015 Long-Term Budget Outlook*, June 2015, and *Updated Budget Projections: 2015 to 2025*, March 2015. Compiled by PGPF.
NOTE: Projections are from CBO's extended baseline scenario.

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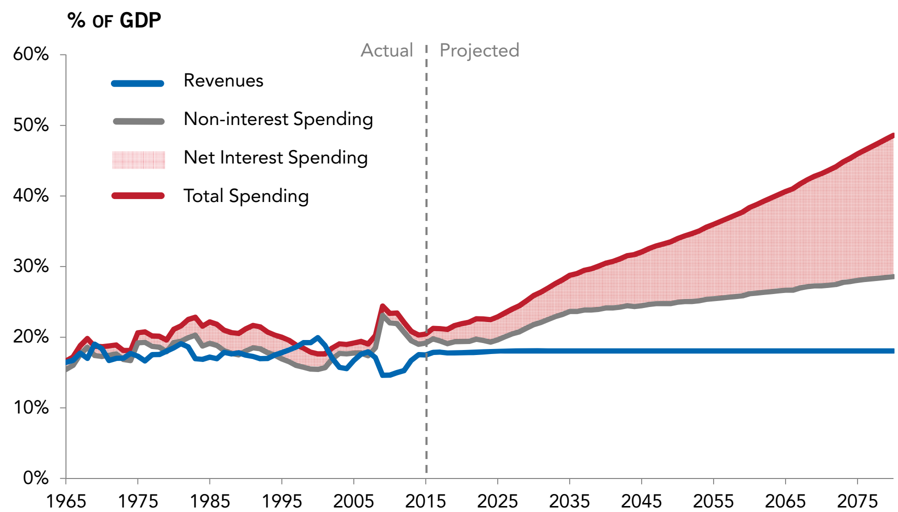
Interest costs are projected to grow to unsustainable levels if current policies aren't changed



SOURCE: Congressional Budget Office, *The 2015 Long-Term Budget Outlook*, June 2015; and Office of Management and Budget, *Budget of the United States Government, Fiscal Year 2016, Historical Tables*, February 2015. Calculated by PGPF.
NOTE: Projections are based on CBO's alternative fiscal scenario.

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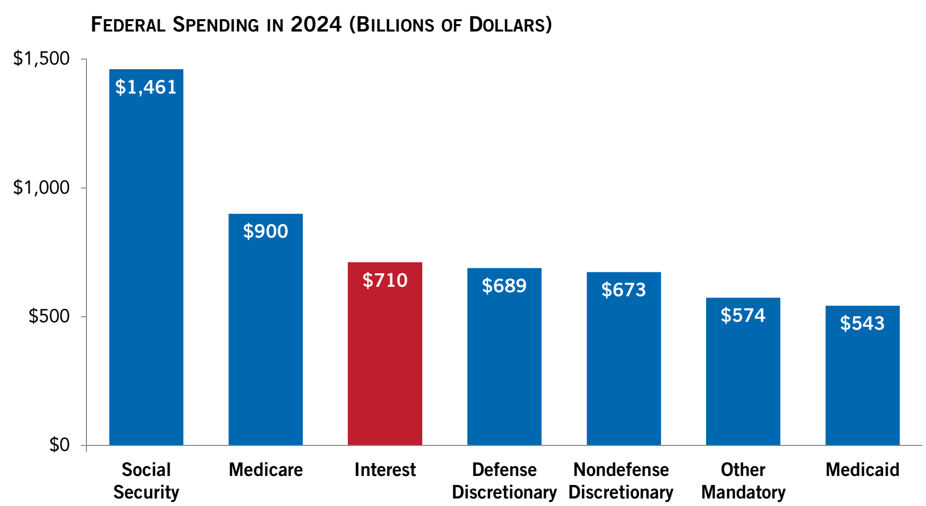
Interest costs will be the third largest category of the budget in 2024



SOURCE: Congressional Budget Office, *An Update to the Budget and Economic Outlook: 2015 to 2025*, August 2015. Compiled by PGPF.
NOTE: Medicare is net of offsetting receipts.

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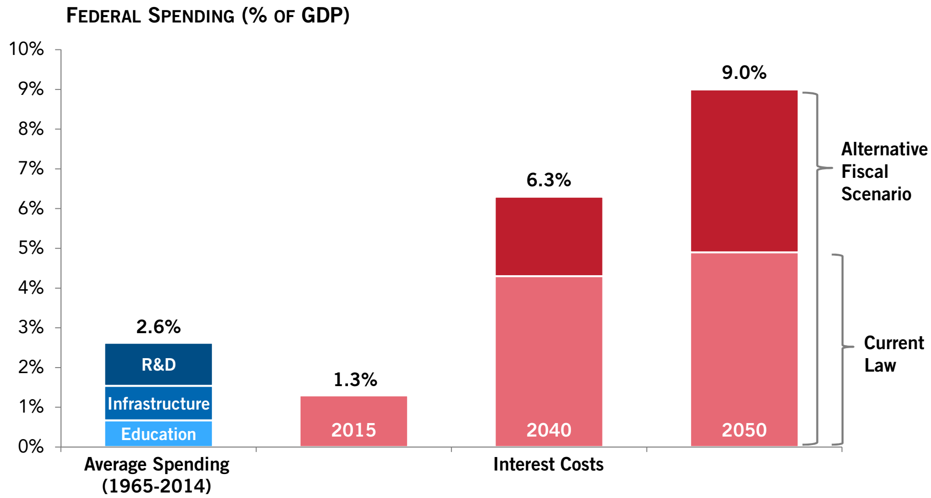
By 2050, interest costs are projected to be more than three times what the federal government has historically spent on R&D, infrastructure, and education combined



SOURCE: Congressional Budget Office, *The 2015 Long-Term Budget Outlook*, June 2015; and Office of Management and Budget, *Budget of the United States Government, Fiscal Year 2016*, February 2015. Compiled by PGPF.
NOTE: Infrastructure excludes defense. Current law projections are from CBO's extended baseline scenario. Data for the alternative fiscal scenario does not include economic feedback.

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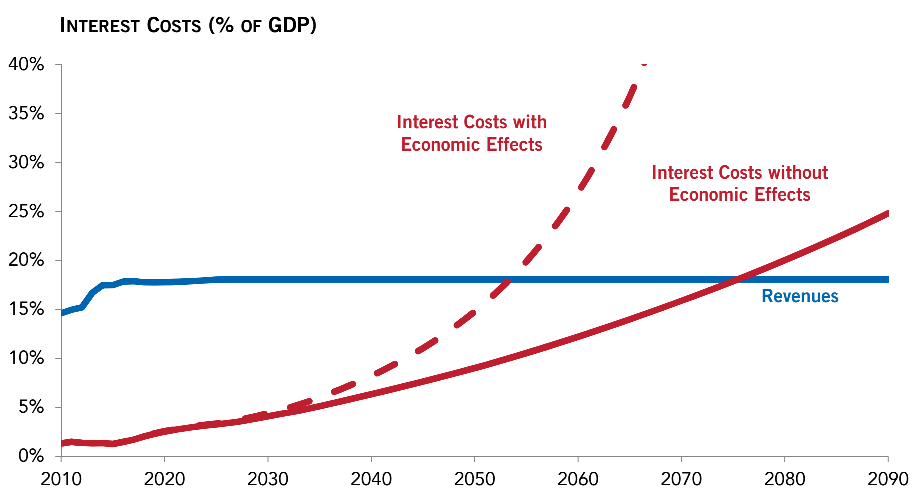
By 2076, interest costs on the federal debt will exceed federal revenues. If the economic effects of debt on interest rates are included, that date will occur in 2054.



SOURCE: Congressional Budget Office, *Updated Budget Projections: 2015 to 2025*, March 2015, and *The 2015 Long-Term Budget Outlook*, June 2015. Calculated by PGPF.
NOTE: Projections are based on CBO's alternative fiscal scenario and CBO's assumptions about the effects of high debt levels on interest rates. The effective interest rate on federal debt rises gradually until it is one percentage point higher in 2040 than in CBO's economic benchmark projections.

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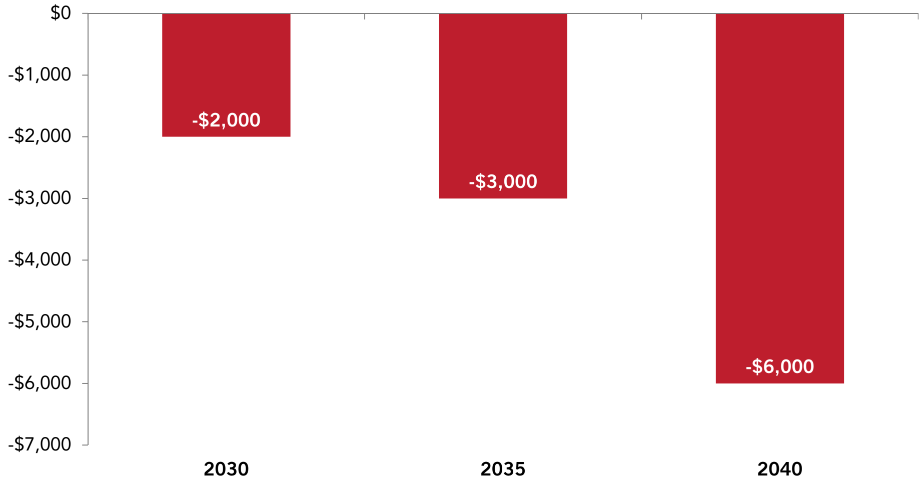
The growing federal debt is projected to reduce average income per person by as much as $6,000

AVERAGE INCOME LOSS PER CAPITA (2015 DOLLARS)



SOURCE: Congressional Budget Office, *The 2015 Long-Term Budget Outlook*, June 2015. Compiled by PGPF.
NOTE: Income is measured as real gross national product (GNP) per person. The income reduction is the difference between the level of income if debt rises as it does under the alternative fiscal scenario and the level of income if debt remains near its current share of GNP.

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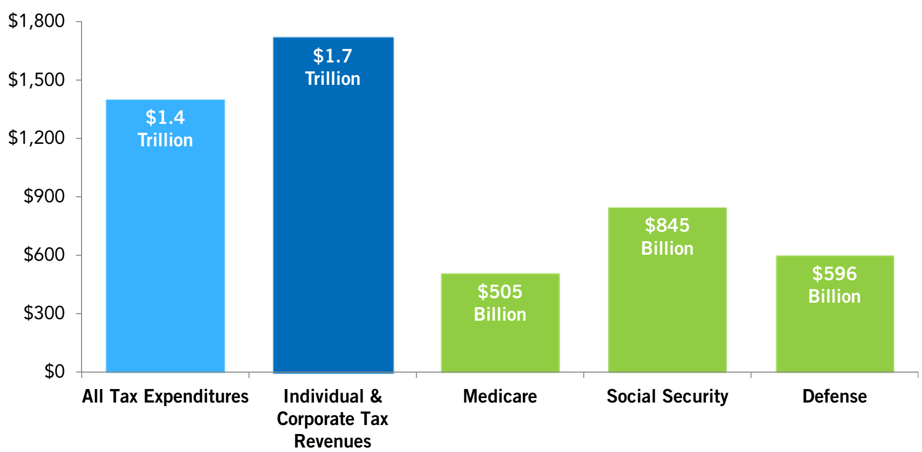
Corporate and individual tax expenditures are large in comparison to annual taxes collected, as well as to the government's major programs

BUDGETARY COST IN 2014 (BILLIONS OF DOLLARS)



SOURCE: Office of Management and Budget, *Budget of the United States Government, Fiscal Year 2016,* February 2015. Data are for 2014. Compiled by PGPF.
NOTE: Medicare spending is net of premiums and payments from the states. Those receipts were $95 billion in 2014. Defense represents discretionary defense spending. Income tax revenues includes both individual and corporate income tax receipts. Tax expenditures are deductions, credits, exclusions, and preferential rates. The estimates include effects on income, payroll, and excise tax revenues, as well as effects on outlays.

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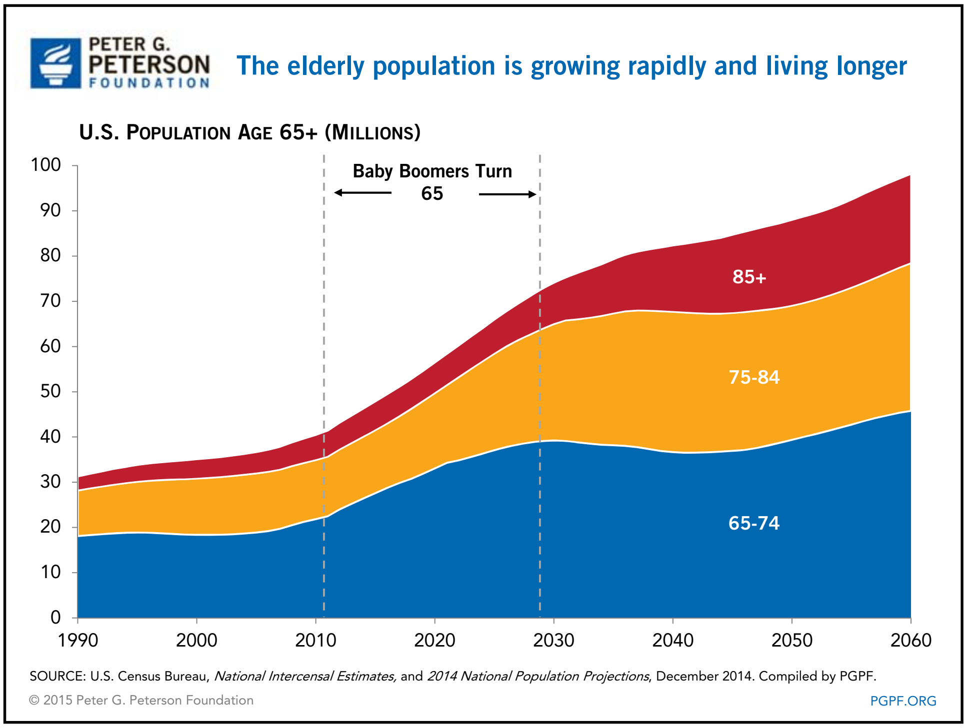
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The elderly population is growing rapidly and living longer
U.S. Population Age 65+ (Millions)
Baby Boomers Turn 65
85+
75-84
65-74
100
90
80
70
60
50
40
30
20
10
0
1990
2000
2010
2020
2030
2040
2050
2060
SOURCE: U.S. Census Bureau, National Intercensal Estimates, and 2014 National Population Projections, December 2014. Compiled by PGPF.
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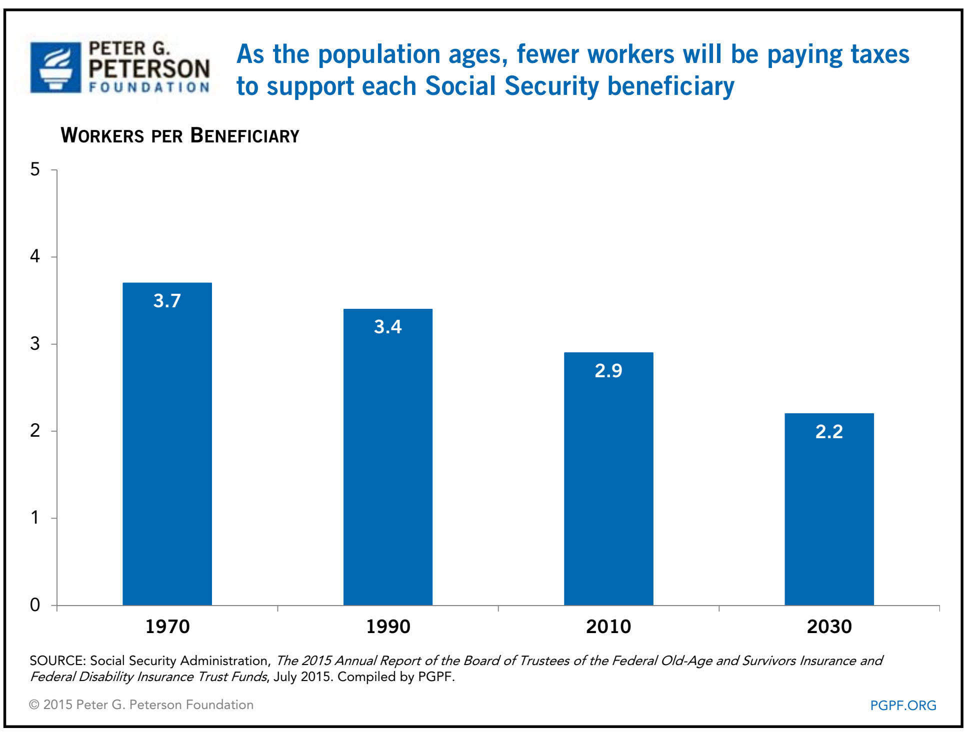
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As the population ages, fewer workers will be paying taxes to support each Social Security beneficiary
Workers per Beneficiary
5
4
3
2
1
0
3.7
3.4
2.9
2.2
1970
1990
2010
2030
SOURCE: Social Security Administration, The 2015 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds, July 2015. Compiled by PGPF.
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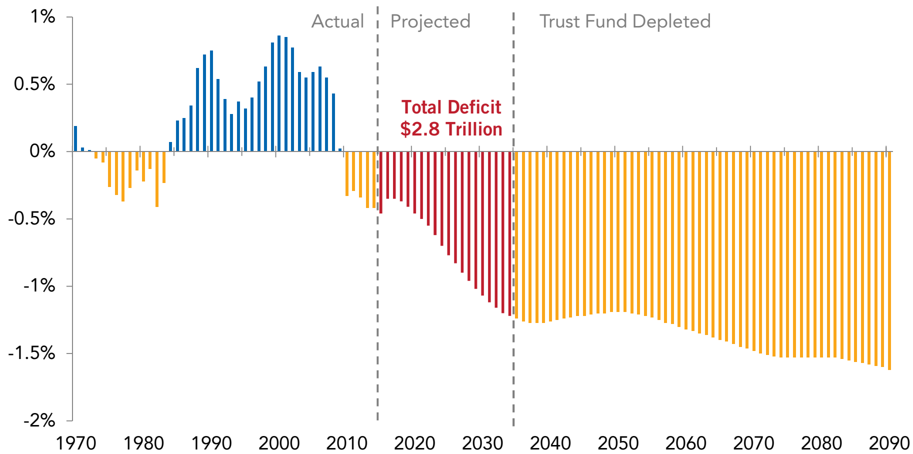
Social Security will run a cumulative cash deficit of $2.8 trillion between now and 2034

SOCIAL SECURITY SURPLUSES/DEFICITS (% OF GDP)



SOURCE: Social Security Administration, *The 2015 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds*, July 2015. Compiled by PGPF.
NOTE: Surplus/deficit numbers exclude interest income. The total deficit of $2.8 trillion is the present value of the cash deficits between 2015 and 2034.

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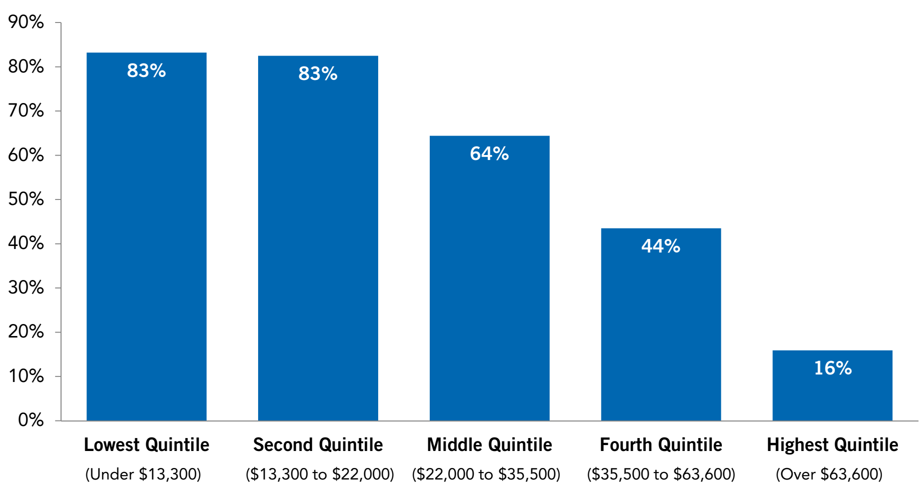
Low-income seniors rely on Social Security benefits for a major share of their retirement income

SOCIAL SECURITY BENEFITS (% OF TOTAL INCOME)



SOURCE: Social Security Administration, *Income of the Population 55 or Older, 2012,* April 2014. Compiled by PGPF.
NOTE: A quintile is one fifth of the distribution. The lowest quintile is the 20% of the 65+ population with the lowest income.

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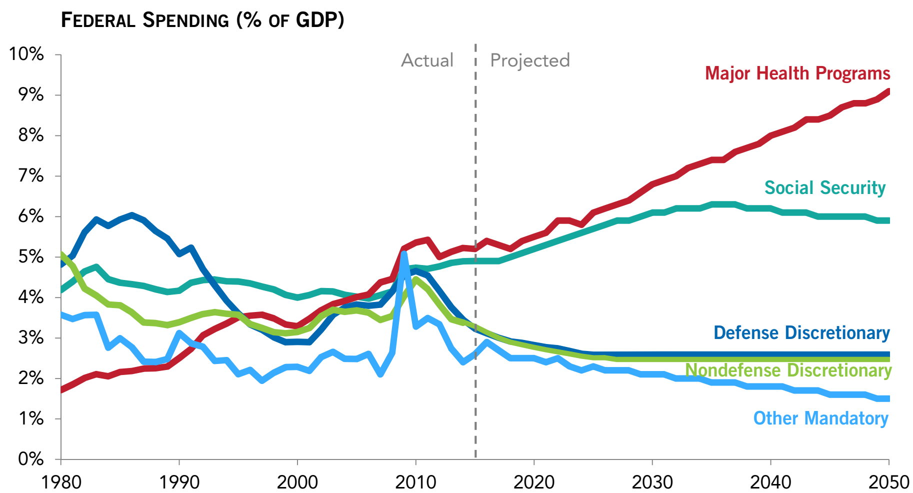
Healthcare is the major driver of the projected growth in federal spending over the long term



SOURCE: Congressional Budget Office, *Historical Budget Data*, January 2015, and *The 2015 Long-Term Budget Outlook,* June 2015; and PGPF projections based on CBO data. Calculated by PGPF.
NOTE: Projections are from the extended baseline scenario. Major health programs include Medicare, Medicaid, Children's Health Insurance Program (CHIP), and the health exchanges.

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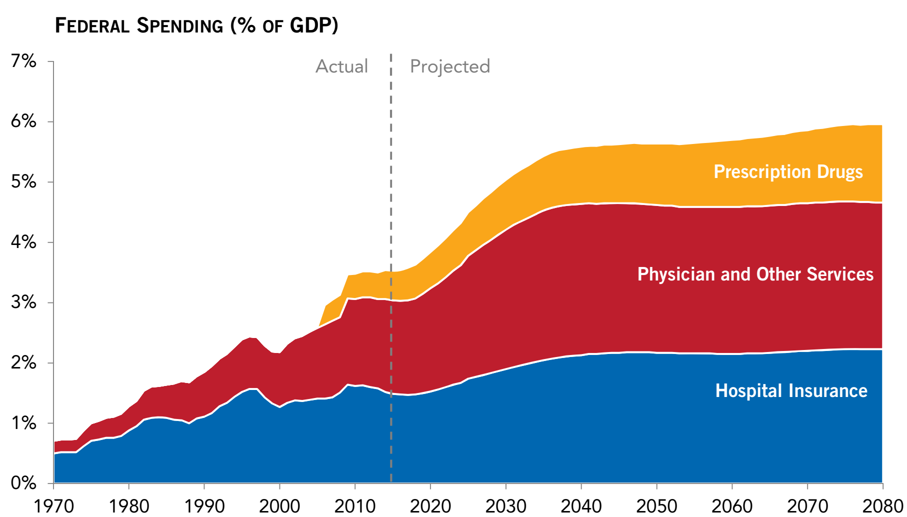
Medicare spending as a share of GDP is projected to rise by more than 50 percent within 25 years



SOURCE: Centers for Medicare and Medicaid Services, *2015 Annual Report of the Boards of Trustees of the Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds*, July 2015. Compiled by PGPF.

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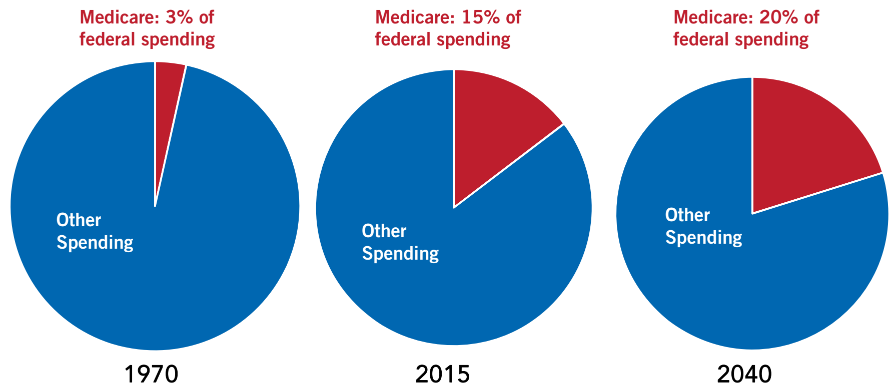
Medicare is a growing share of the federal budget



SOURCE: Office of Management and Budget, *Budget of the United States Government, Fiscal Year 2016*, February 2015; and Congressional Budget Office, *The 2015 Long-Term Budget Outlook*, June 2015. Compiled by PGPF.
NOTE: Pies represent total spending.

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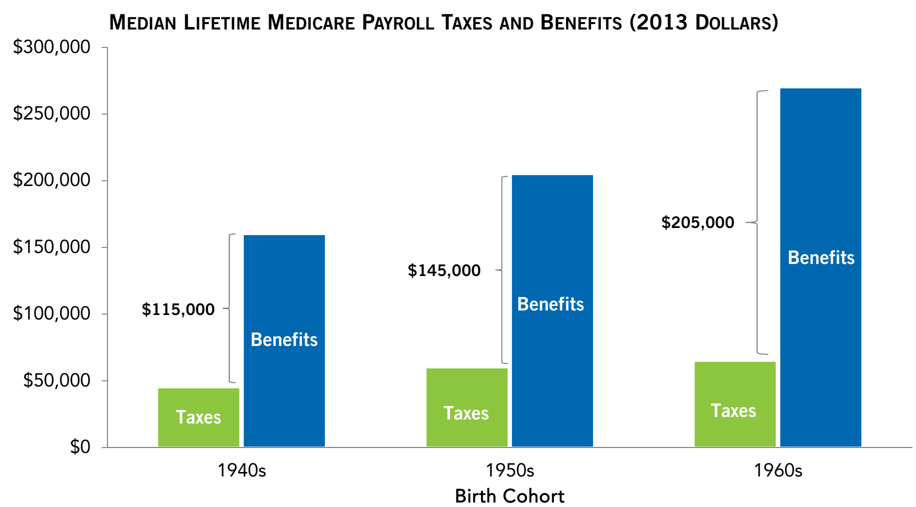
On average, Medicare benefits far exceed taxes over an individual's lifetime



SOURCE: Congressional Budget Office, *CBO 2013 Long-Term Budget Outlook*, September 2013. Compiled by PGPF.
NOTE: The amounts here are present values, calculated to adjust for inflation and discounted to the value for beneficiaries at age 65. Benefits are net of premiums paid by beneficiaries. Birth cohort refers to the decade in which beneficiaries were born.

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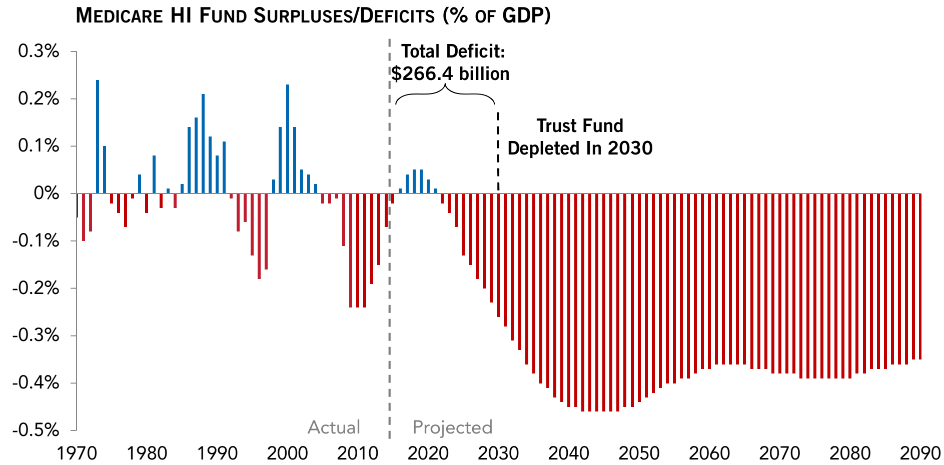
Medicare's Hospital Insurance will start running deficits in 2022 and its trust fund will be depleted in 2030



SOURCE: Social Security Administration, *The 2015 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds*, July 2015; and Centers for Medicare and Medicaid Services, *2015 Annual Report of the Boards of Trustees of the Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds*, July 2015. Compiled by PGPF.
NOTE: Data excludes interest income. The present value of the cumulative net deficit before insolvency is equal to the current value of the HI Trust Fund.

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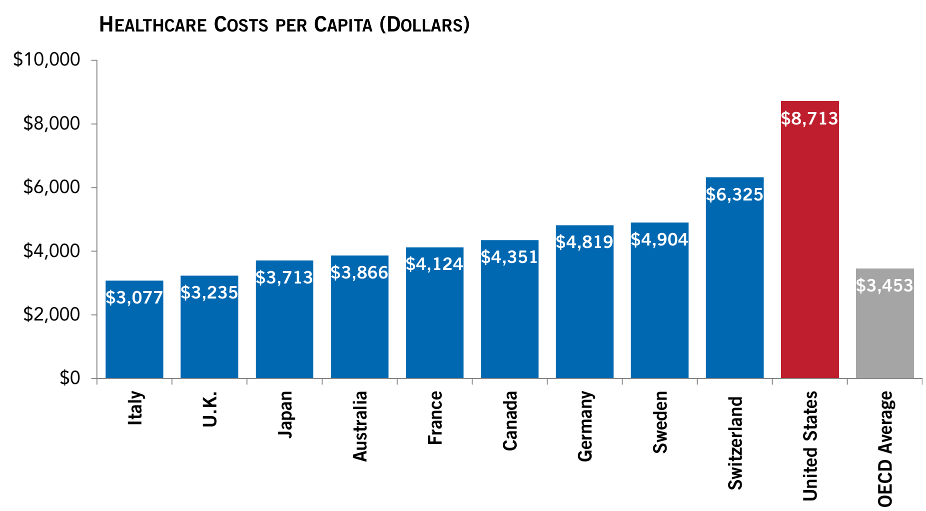
The United States spends more than twice as much per capita on healthcare as the average developed country does



SOURCE: Organization for Economic Cooperation and Development, *OECD Health Statistics 2015*, July 2015. Compiled by PGPF.
NOTE: Per capita health expenditures are for 2013, except Australia for which 2012 data are the latest available. Chart uses purchasing power parities to convert data into U.S. dollars.

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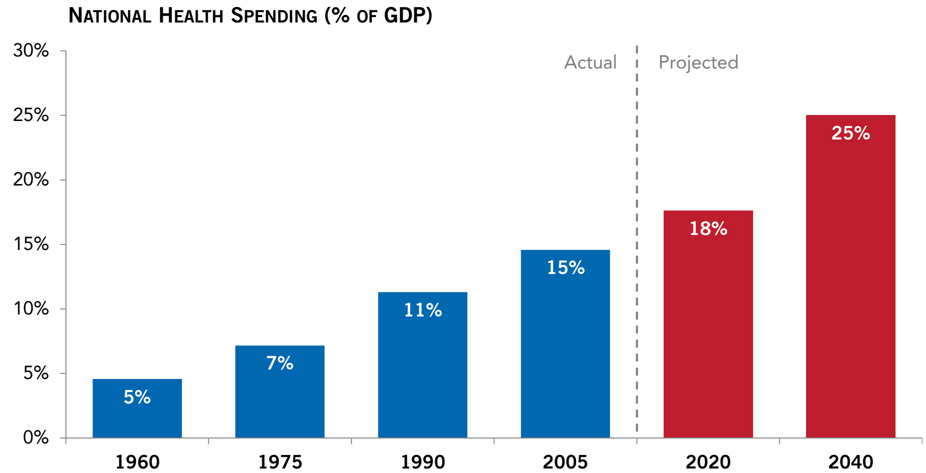
Total U.S. health expenditures (both public and private) are projected to rise to approximately one-quarter of the economy by 2040



SOURCE: Centers for Medicare and Medicaid Services, *National Health Expenditures*, July 2015; and the Congressional Budget Office, *The 2015 Long-Term Budget Outlook*, July 2015. Compiled by PGPF.
NOTE: CMS data are for 1960–2020. The 2040 figure is based on the latest projection from CBO. National spending on healthcare is health consumption expenditures as defined in the national health expenditure accounts and excludes spending on medical research, structures, and equipment.

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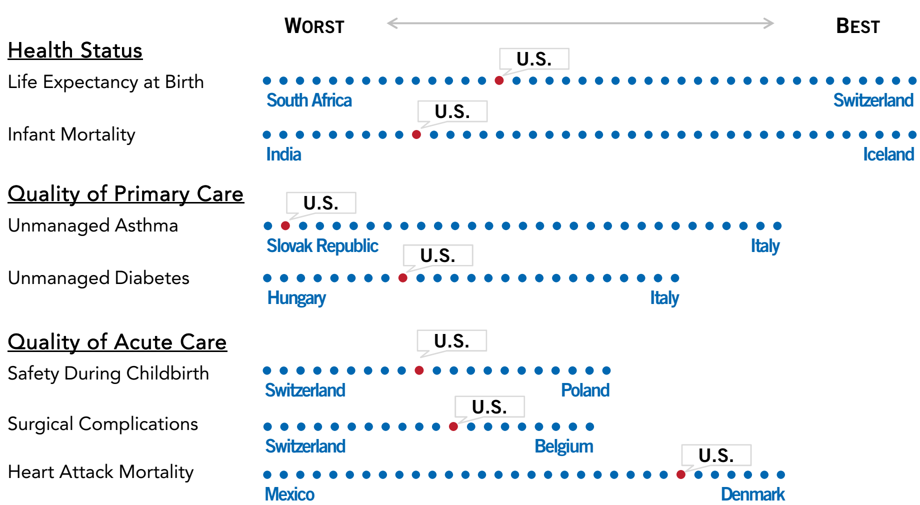
Although the United States spends more on healthcare than other developed countries, its health outcomes are generally no better



SOURCE: Organization for Economic Cooperation and Development, *Health at a Glance 2013: OECD Indicators*, March 2014. Compiled by PGPF.
NOTE: Data are not available for all countries for all metrics; all published data are shown. Data are for 2011 or latest available. Surgical complications is defined by a foreign body left in after a procedure. Childbirth safety is based on data for deliveries without instruments.

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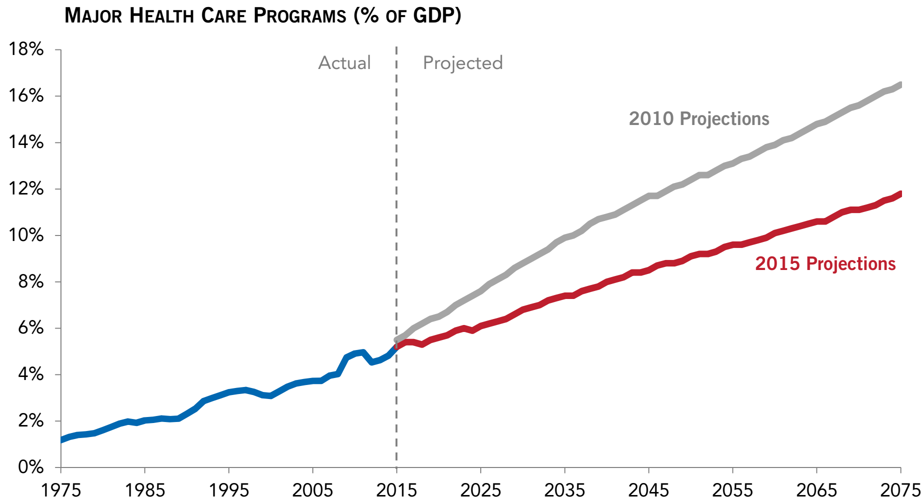
Projections of federal healthcare spending have improved but are still climbing as a share of the economy



SOURCE: Congressional Budget Office, *The Long-Term Budget Outlook*, June 2010, *Updated Budget Projections: 2015 to 2025*, January 2015, and *The 2015 Long-Term Budget Outlook*, June 2015. Compiled by PGPF.
NOTE: Federal spending on major health programs reflects CBO's alternate fiscal scenario and is net of Medicare premiums.

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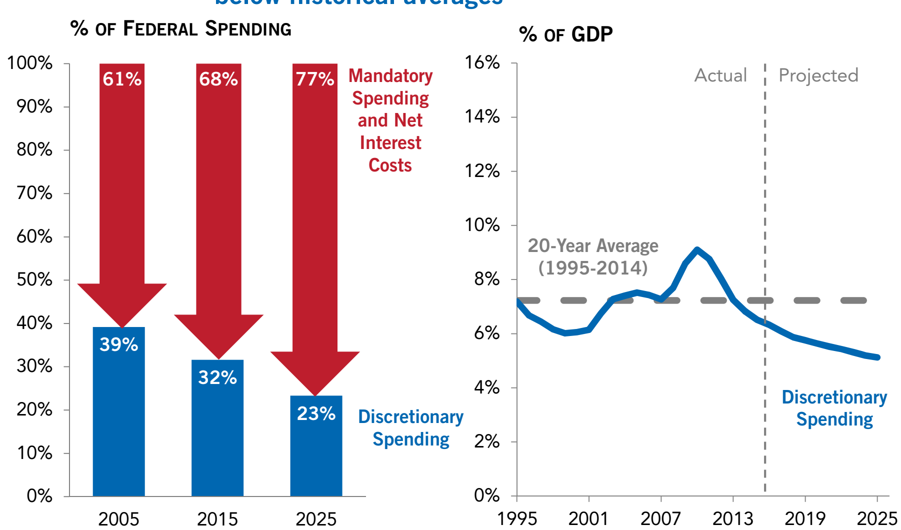
Mandatory spending and interest costs will climb significantly, while discretionary spending will fall to well below historical averages



SOURCE: Congressional Budget Office, *An Update to the Budget and Economic Outlook: 2015 to 2025*, August 2015. Compiled by PGPF.

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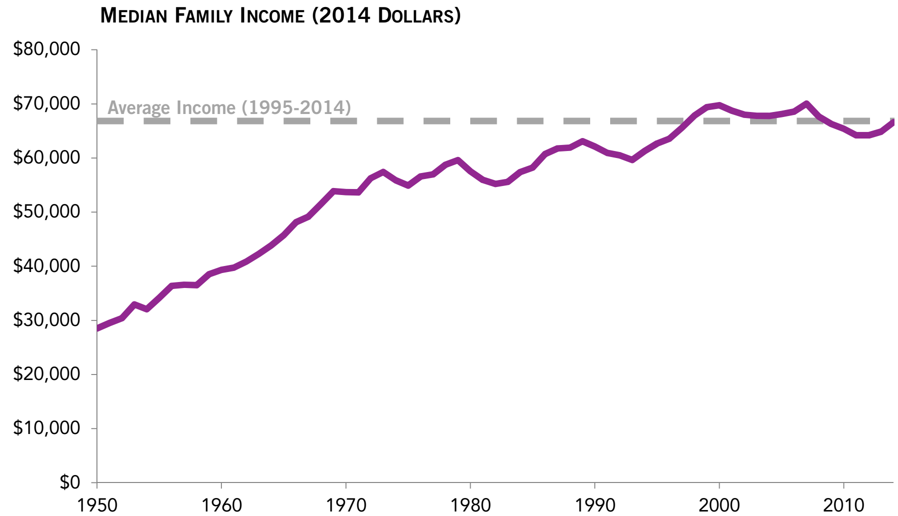
The median real income for families in the United States has been relatively stagnant for two decades



SOURCE: U.S. Census Bureau, *Historical Income Tables*, September 2015. Compiled by PGPF.

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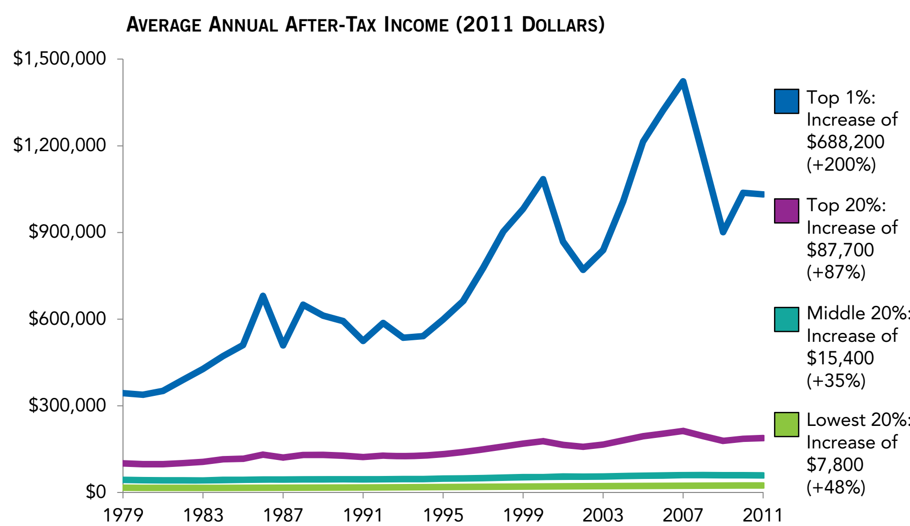
Although the incomes of the wealthy are volatile, they have grown much faster than the incomes of other groups



SOURCE: Congressional Budget Office, *The Distribution of Household Income and Federal Taxes, 2011,* November 2014. Compiled by PGPF.

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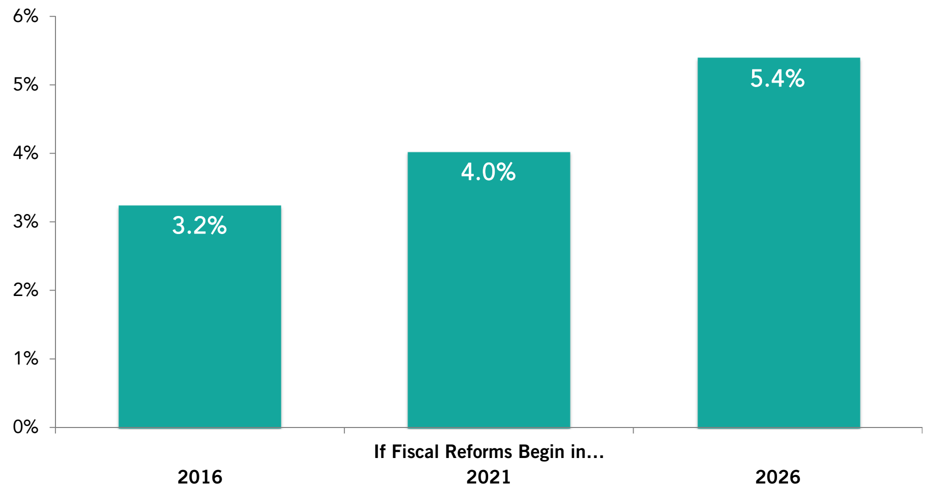
Delaying action raises the cost of stabilizing the debt in the long run

SIZE OF BUDGET CHANGES NEEDED TO STABILIZE THE DEBT (% OF GDP)



SOURCE: Congressional Budget Office, *The 2015 Long-Term Budget Outlook*, June 2015. Calculated by PGPF.
NOTE: Calculations are based on CBO's alternative fiscal scenario.

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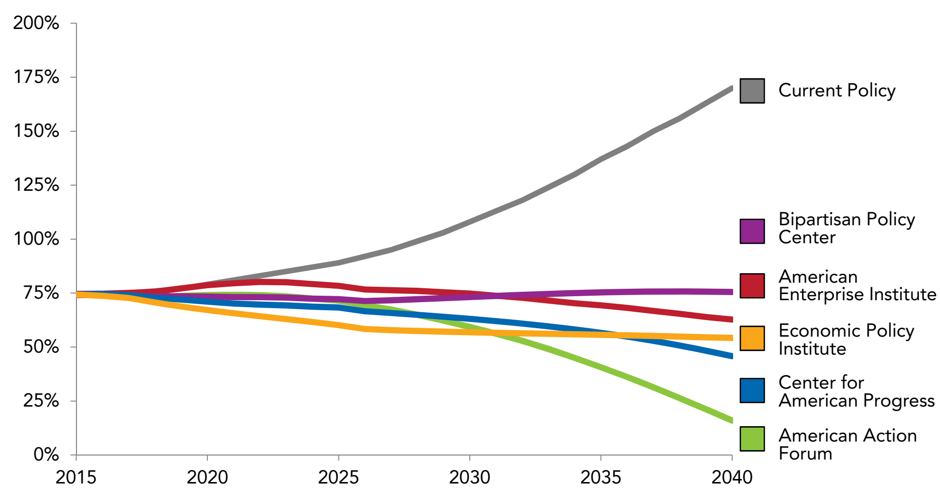
Solutions do exist: PGPF Solutions Initiative plans from five think tanks show stable or declining federal debt through 2040

DEBT HELD BY THE PUBLIC (% OF GDP)



SOURCE: Peter G. Peterson Foundation, *Solutions Initiative III*, May 2015. See pgpf.org/solutions-initiative-iii for more details.
NOTE: Current policy is defined as the alternative fiscal scenario without economic feedback from CBO's *2014 Long-Term Budget Outlook*.

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