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## Comparisons of CBO and OMB Baseline Projections August 28, 2009

The baseline estimates released earlier this week by the Congressional Budget Office (CBO) and the Office of Management and Budget (OMB) confirm the devastating effect of the recession on the nation's fiscal condition. While the current year deficit is less than the worst-case estimates based upon the administration's May budget proposal, baseline deficits in the next ten years are now projected to be higher than expected by OMB and CBO just a few months ago.

In the analysis below, we focus on a comparison between OMB and CBO baselines, deficit estimates, their drivers, and the bridge between CBO and OMB's numbers. (Note: These numbers analyze OMB's BEA baseline, not its budget proposals. For a bridge between the numbers, see the final section.)

### Deficits and Debt

For the current fiscal year, the CBO baseline estimates a deficit of \$1.587 trillion, \$38 billion larger than the OMB Budget Enforcement Act (BEA) baseline of \$1.549 trillion. These estimates, however, are not directly comparable because the CBO and OMB baselines differ in whether they treat Fannie Mae and Freddie Mac (GSEs) as government entities. In concluding that they should be considered federal operations, including them in the budget, and accounting for them on a present-value basis at the time of the government takeover, CBO sharply boosts its estimate of the current year deficit.

CBO indicates that if it accounted for the GSEs as nongovernmental agencies like the administration, its 2009 deficit would be \$1.409 trillion rather than \$1.587 trillion. On a comparable conceptual basis, therefore, OMB's estimate of the current year deficit is \$140 billion higher than CBO's. (The actual deficit is recorded as \$1.267 trillion for the first 10 months of the year. <http://www.fms.treas.gov/mts/mts0709.pdf>)

**Fig. 1: Comparison of BEA Baseline Deficits and Debt Held by the Public**

Fiscal year	<u>2008</u> <u>Actual</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2010-</u> <u>2014</u>	<u>2010-</u> <u>2019</u>
<b>In Billions of Dollars</b>									
<b>Deficits</b>									
CBO	459	1,587	1,381	921	590	538	558	3,988	7,137
OMB	<u>459</u>	<u>1,549</u>	<u>1,426</u>	<u>945</u>	<u>625</u>	<u>564</u>	<u>522</u>	<u>4,081</u>	<u>6,259</u>
CBO less OMB	0	38	-45	-24	-35	-26	36	-93	878
<b>Debt Held by the Public</b>									
CBO	5,803	7,612	8,868	9,782	10,382	10,870	11,439	na	na
OMB	<u>5,803</u>	<u>7,825</u>	<u>9,468</u>	<u>10,305</u>	<u>10,987</u>	<u>11,614</u>	<u>12,203</u>	<u>na</u>	<u>na</u>
CBO less OMB	0	-213	-600	-523	-605	-744	-764	na	na
<b>As a Percentage of GDP</b>									
<b>Deficits</b>									
CBO	3.2	11.2	9.6	6.1	3.7	3.2	3.2	5.0	4.0
OMB	<u>3.2</u>	<u>11.0</u>	<u>9.9</u>	<u>6.2</u>	<u>3.9</u>	<u>3.3</u>	<u>2.9</u>	<u>5.1</u>	<u>3.4</u>
CBO less OMB	0.0	0.2	-0.3	-0.1	-0.2	-0.1	0.3	-0.1	0.6
<b>Debt Held by the Public</b>									
CBO	40.8	53.8	61.4	65.2	65.9	65.5	66.0	na	na
OMB	<u>40.8</u>	<u>55.4</u>	<u>65.6</u>	<u>68.1</u>	<u>68.6</u>	<u>68.3</u>	<u>67.8</u>	<u>na</u>	<u>na</u>
CBO less OMB	0.0	-1.6	-4.2	-2.9	-2.7	-2.8	-1.8	na	na
<b>Memorandum: Gross Domestic Product</b>									
CBO	14,222	14,140	14,439	14,993	15,754	16,598	17,319	79,103	176,828
OMB	<u>14,222</u>	<u>14,116</u>	<u>14,442</u>	<u>15,123</u>	<u>16,021</u>	<u>16,997</u>	<u>18,011</u>	<u>80,594</u>	<u>185,284</u>
CBO less OMB	0	24	-3	-130	-267	-399	-692	-1,491	-8,456

For the next five years, the differences in the baseline deficit estimates are reasonably small. For 2010, CBO estimates that the baseline deficit will be \$45 billion below OMB's estimate; for 2010-2014, CBO expects deficits to be \$93 billion below OMB's estimate, with \$31 billion of that difference accounted for by the difference in the budgetary treatment of the GSEs. As a percentage of GDP, the differences look slightly more striking, but are still relatively minor.

Both agencies estimate a deficit of about \$1.4 trillion, or about 10 percent of GDP, for fiscal year 2010. Spending for the Troubled Asset Relief Program (TARP) goes down but is partially replaced by more rapid spending of stimulus funds. Receipts also are expected to increase at a rapid rate as the economy rebounds.

The deficit is expected to decrease in fiscal years after 2010. The assumed expiration of the 2001 and 2003 tax cuts will add an extra boost to revenues beginning in 2011, and spending from the American Recovery and Reinvestment Act (ARRA) will be generally completed in that year. Each of these factors provides relief to the bottom line before

baseline deficits begin to settle at a range of \$500 - \$600 billion (about 3.2 percent of GDP) in 2013 and 2014.

Over the full ten years covered by the projections, there are substantial differences in the baseline deficit estimates of the two agencies. For 2010-2019, CBO estimates that deficits are expected to total \$7.137 trillion, including \$48 billion from treating the GSEs as government entities. While OMB projects higher deficits in the first five years of the projections, it expects deficits in the second five years (2015-2019) to be around \$1 trillion lower than CBO's estimates.

Large deficits beget large increases in debt held by the public. OMB's estimates of debt held by the public are above CBO's because of expected increases in the government's holdings of financial assets. This result follows from the OMB's treatment of Fannie Mae and Freddie Mac, which treats the government's contributions to their solvency as the purchase of financial assets. The OMB projections include the net purchase of \$603 billion in financial assets above CBO's estimates over 2010-2014, which increases to \$913 billion in purchases over 10 years.

For FY 2009, debt held by the public is expected to increase by about one-third—from \$5.8 trillion at the end of fiscal 2008 to \$7.6 trillion at the end of fiscal 2009 under CBO estimates, and \$7.8 trillion under OMB's. Debt in the baseline scenario is expected to increase steadily in both dollar terms and as a share of the economy under CBO's projections, but will decline slightly as a share of GDP under OMB's. CBO expects debt to reach \$11.4 trillion (66 percent of GDP) in 2014, increasing to \$14.3 trillion (67.8 percent of the economy) in 2019. Under OMB's treatment of GSE's, debt held by the public would reach \$12.2 trillion (67.8 percent of GDP in 2014 and \$14.7 trillion (64.2 percent of GDP) in 2019.

## **Revenues and Mandatory Spending**

Key drivers in the future path of the baseline deficit are revenues and mandatory spending. Revenues are expected to fall by 17 percent in the current fiscal year while mandatory spending is expected to increase by 40 percent. Tax receipts as a share of the economy are expected to be around 15 percent for 2009, while entitlement spending alone is expected to be about 16 percent of GDP.

Receipts are expected to rebound in FY 2010, reflecting the passing of the worst of the recession. CBO expects revenues will grow by 7.8 percent next year, while OMB expects growth of 10.5 percent. In 2011 receipts would be boosted by the expiration of the 2001 and 2003 tax cuts and increase year-over-year by 20 percent in both agencies' estimates. For years after 2011, OMB assumes the rate of growth in receipts is about one percentage point above CBO's assumptions.

The resulting cumulative difference in the two agencies' revenue estimates is not trivial. From 2010-2014, OMB expects revenues to total \$36.6 trillion, on average about 20.5 percent of GDP. CBO, in contrast, projects revenues will total \$34.2 trillion, or 19.3 percent of GDP. This difference in revenues accounts for the bulk of the difference in the baseline deficit projections.

It is likely that actual receipts will be lower than shown in these projections since the traditional baseline assumes that the AMT will not be indexed for inflation in future years, but the AMT patch has been enacted by Congress without offsets for several years now. In addition, the baseline assumes that the 2001/2003 tax cuts will expire after 2010. The President and Congress have endorsed the continuation of most of those tax cuts, which will add to the deficit.

**Fig. 2: Comparison of Receipts and Mandatory Spending in BEA Baseline**

Fiscal year	<u>2008</u> <u>Actual</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2010-2014</u>	<u>2010-2019</u>
<b>In Billions of Dollars</b>									
<b>Receipts</b>									
CBO	2,524	2,100	2,264	2,717	3,010	3,221	3,403	14,614	34,177
OMB	<u>2,524</u>	<u>2,102</u>	<u>2,322</u>	<u>2,785</u>	<u>3,114</u>	<u>3,354</u>	<u>3,586</u>	<u>15,161</u>	<u>36,584</u>
CBO less OMB	0	-2	-58	-68	-104	-133	-183	-547	-2,407
<b>Mandatory Spending</b>									
CBO	1,595	2,270	2,070	2,027	1,961	2,038	2,127	10,222	22,630
OMB	<u>1,595</u>	<u>2,213</u>	<u>2,116</u>	<u>2,056</u>	<u>2,006</u>	<u>2,113</u>	<u>2,236</u>	<u>10,527</u>	<u>23,742</u>
CBO less OMB	0	57	-46	-29	-45	-75	-109	-305	-1,112
<b>As a Percentage of GDP</b>									
<b>Receipts</b>									
CBO	17.7	14.9	15.7	18.1	19.1	19.4	19.6	18.5	19.3
OMB	<u>17.7</u>	<u>14.9</u>	<u>16.1</u>	<u>18.4</u>	<u>19.4</u>	<u>19.7</u>	<u>19.9</u>	<u>18.8</u>	<u>19.7</u>
CBO less OMB	0.0	0.0	-0.4	-0.3	-0.3	-0.3	-0.3	-0.3	-0.4
<b>Mandatory Spending</b>									
CBO	11.2	16.1	14.3	13.5	12.4	12.3	12.3	12.9	12.8
OMB	<u>11.2</u>	<u>15.7</u>	<u>14.7</u>	<u>13.6</u>	<u>12.5</u>	<u>12.4</u>	<u>12.4</u>	na	na
CBO less OMB	0.0	0.4	-0.4	-0.1	-0.1	-0.1	-0.1	na	na

After the effects of the TARP and the stimulus make their way through the system, mandatory spending is expected to continue its inexorable rise. Entitlements are expected to decline from 16 percent of GDP in the current fiscal year to about 12 percent in 2015, before beginning to increase as a share of the economy for the remainder of the projection period and thereafter.

Over the projection period, OMB expects mandatory spending will be \$1.1 trillion above the \$22.6 trillion estimated by CBO. Differences in estimates of health care spending account for \$361 billion of the total \$1.1 trillion difference.

Medicare spending is expected to grow at an average annual rate of 6.9 percent for 2010-2014 under both agencies' estimates. For 2015-2019, CBO expects that growth will moderate to 6.4 percent while OMB projects that growth will increase to 7.2 percent. This accounts for \$78 billion in higher spending over 10 years.

The difference in average annual growth rates is even starker for Medicaid. Over 2010-2014, CBO expects Medicaid growth of 3.7 percent, while OMB expects 5.0 percent. (Those rates are lower than expected because of the effects of the increased federal match rate in 2010.) Over 2015-2019, CBO projects baseline Medicaid growth of 7.1 percent, and OMB estimates 7.8 percent. Over 10 years, OMB expects Medicaid spending will be \$283 billion above CBO's estimate.

## **Economic Projections**

The economic forecasts that serve as the foundation for the CBO and OMB revenue and spending projections show somewhat different paths for the US economy. Both expect that the economy will begin to grow again in calendar year 2010. On average, they expect that the level of nominal GDP will grow by 3.1 percent in calendar 2010, and that real GDP will grow by 1.9 percent.

Both agencies expect economic growth will peak in calendar year 2012 before settling back to trend growth. In that year, CBO expects nominal GDP to increase at a 5.4 percent rate, with real GDP growing at 5.0 percent. OMB sees real GDP reaching its peak in 2012 at 4.3 percent and staying there through 2013 while nominal GDP reaching its peak growth of 6.1 percent in calendar 2013.

CBO and OMB differ somewhat substantially on where the economy settles after the current recession passes. CBO expects the economy will settle at a much lower growth rate in the second five years of the projection period. For 2015-2019, CBO projects average real GDP growth of 2.4 percent while OMB projects 3.0 percent.

Despite expecting stronger growth in the real economy and higher inflation and therefore nominal GDP, OMB expects the unemployment rate to be persistently high. While CBO's peak annual average unemployment rate of 10.2 percent is above OMB's 9.8 percent, CBO expects that rate to decline fairly rapidly to 4.8 percent in 2015. OMB, in contrast, never expects the unemployment rate to drop below 5.2 percent, which is achieved in 2019. On average, OMB estimates the unemployment rate will be 5.4 percent for the second five years of the projection period, 0.6 percentage points above CBO's estimate of 4.8 percent.

Fig. 3: Comparison of Economic Forecasts

	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>Annual Average</u>	
	<u>Actual</u>							<u>2010-2014</u>	<u>2015-2019</u>
<b>Nominal GDP Growth (Calendar year over calendar year)</b>									
CBO	3.3	-0.7	2.9	4.0	5.4	5.2	4.1	4.3	4.0
OMB	<u>3.3</u>	<u>-1.0</u>	<u>3.3</u>	<u>5.1</u>	<u>6.0</u>	<u>6.1</u>	<u>5.9</u>	<u>5.3</u>	<u>4.8</u>
CBO less OMB	0.0	0.3	-0.4	-1.1	-0.6	-0.9	-1.8	-1.0	-0.8
<b>Real GDP Growth (Calendar year over calendar year)</b>									
CBO	1.1	-2.5	1.7	3.5	5.0	4.5	3.0	3.5	2.4
OMB	<u>1.1</u>	<u>-2.8</u>	<u>2.0</u>	<u>3.8</u>	<u>4.3</u>	<u>4.3</u>	<u>4.1</u>	<u>3.7</u>	<u>3.0</u>
CBO less OMB	0.0	0.3	-0.3	-0.3	0.7	0.2	-1.1	-0.2	-0.6
<b>Unemployment Rate (Annual averages, percent)</b>									
CBO	5.8	9.3	10.2	9.1	7.2	5.6	4.9	7.4	4.8
OMB	<u>5.8</u>	<u>9.3</u>	<u>9.8</u>	<u>8.6</u>	<u>7.7</u>	<u>6.8</u>	<u>5.9</u>	<u>7.8</u>	<u>5.4</u>
CBO less OMB	0.0	0.0	0.4	0.5	-0.5	-1.2	-1.0	-0.4	-0.6

### Bridge to OMB's Policy Estimates

The deficit figures discussed above are quite different than the \$9.1 trillion 10-year deficit figures that were mentioned in most recent press reports on the latest projections. The \$9.1 trillion figure is a post-policy estimate, which means that it assumes wholesale enactment of the President's recommended budget. It is based on OMB's economic and technical assumptions; CBO does not re-estimate the effects of the administration's policies with its August baseline update. The table below provides a bridge between CBO's baseline and OMB's policy figures. If one assumes that CBO's estimates of the effects of the President's policies were identical, the CBO would estimate the 10-year deficits under the President's policies to be about \$9.9 trillion.

Fig. 4: Bridge Between CBO's Baseline Estimate and OMB's Policy Estimate (Effect on the deficit, in billions of dollars)

	Fiscal year	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2010-2014</u>	<u>2010-2019</u>
<b>CBO Baseline Deficit</b>		<b>1,587</b>	<b>1,381</b>	<b>921</b>	<b>590</b>	<b>538</b>	<b>558</b>	<b>3,988</b>	<b>7,137</b>
Difference in Concepts (GSEs)		-178	-1	-4	-8	-13	-5	-31	-47
Economic and Technical		140	46	28	43	39	-31	125	-830
<b>OMB BEA Baseline Deficit</b>		<b>1,549</b>	<b>1,426</b>	<b>945</b>	<b>625</b>	<b>564</b>	<b>522</b>	<b>4,081</b>	<b>6,259</b>
Continue 2001 and 2003 tax cuts		*	4	137	232	262	293	928	2,682
Index AMT			13	65	32	37	44	192	546
Medicare 'Doc Fix'			12	22	28	37	39	137	311
Other Program Adjustments		2	-6	0	6	7	8	17	78
Debt Service		*	*	4	15	32	49	100	679
<b>OMB Current Policy Baseline Deficit</b>		<b>1,552</b>	<b>1,449</b>	<b>1,173</b>	<b>939</b>	<b>938</b>	<b>955</b>	<b>5,454</b>	<b>10,555</b>
Net Revenue Policies		28	41	-8	-95	-106	-116	-284	-902
Net Discretionary Policies			15	-44	-69	-72	-71	-241	-603
Net Mandatory Policies			-2	3	24	23	26	74	216
Debt Service		*	*	*	-4	-9	-15	-28	-217
<b>OMB Budget Policy Deficit</b>		<b>1,580</b>	<b>1,502</b>	<b>1,123</b>	<b>796</b>	<b>775</b>	<b>778</b>	<b>4,974</b>	<b>9,051</b>

\*--\$500 million or less.