

# The US Federal Budget and Debt

## ThinkTank Tuesday: Wine, Water, and Policy Whimsy

March 14, 2019

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*Executive Director*

*National Economic Education Delegation*



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## National Economic Education Delegation

### • Vision

- One day, the public discussion of policy issues will be grounded in an accurate perception of the underlying economic principles and data.

### • Mission

- NEED unites the skills and knowledge of a vast network of professional economists to promote understanding of the economics of policy issues in the United States.

### • NEED Presentations

- Are **nonpartisan** and intended to reflect the consensus of the economics profession.



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## Who Are We?

- **Honorary Board: 44 members**

- 2 Fed Chairs: Janet Yellen, Ben Bernanke
- 6 Chairs Council of Economic Advisers
  - o Furman (D), Rosen (R), Bernanke (R), Yellen (D), Tyson (D), Goolsbee (D)
- 3 Nobel Prize Winners
  - o Akerlof, Smith, Maskin

- **Delegates: 363 members**

- At all levels of academia and some in government service
- All have a Ph.D. in economics
- Crowdsource slide decks
- Give presentations

- **Global Partners: 42 Ph.D. Economists**

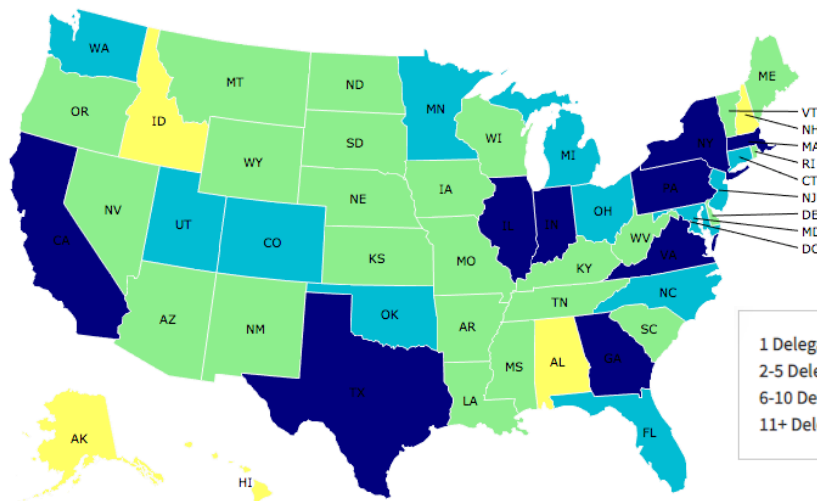
- Aid in slide deck development



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## Where Are We?



1 Delegate - Yellow  
 2-5 Delegates - Green  
 6-10 Delegates - Light Blue  
 11+ Delegates - Blue



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# Outline

- Government Spending
- Government Revenues
- Government Debt

# What Does the U.S. Gov't Budget Look Like?

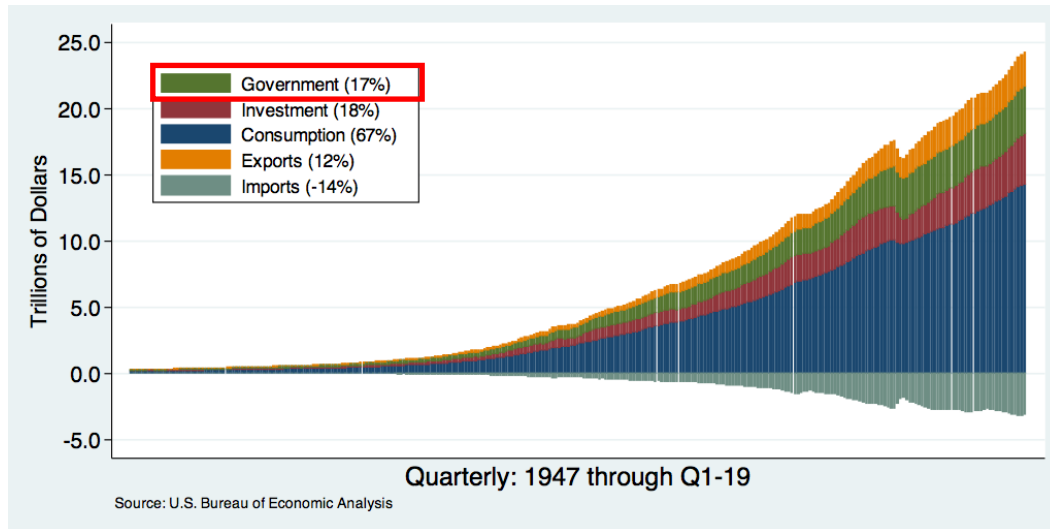
## 2018 Budget Summary

Revenue	Billions		Expenditures	Billions
Income Taxes	\$1,684		Mandatory	\$2,520
Payroll Taxes	\$1,171		Discretionary	\$1,263
Corporate Taxes	\$205		Interest	\$325
Other	\$270			
<b>Total</b>	<b>\$3,329</b>		<b>Total</b>	<b>\$4,108</b>

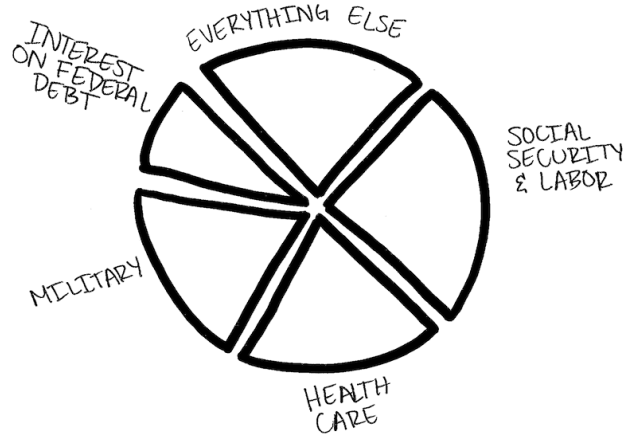
Budget Deficit **\$779 Billion**

# U.S. Government Spending

## Government Spending and the US Economy

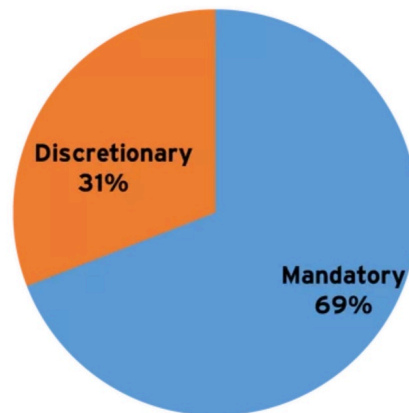


## Where Does the Money Go?



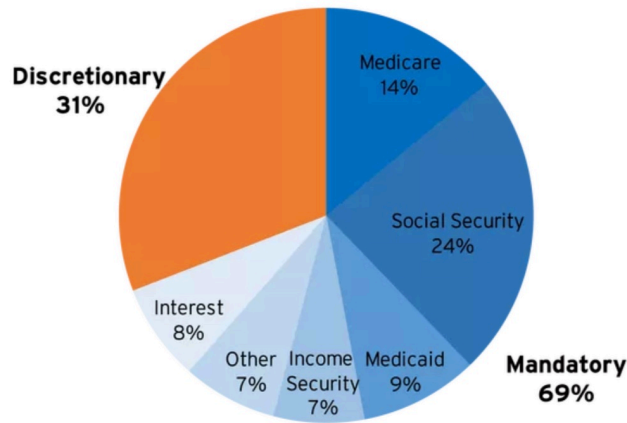
## On What is the Money Spent? Complicated

### COMPOSITION OF FEDERAL SPENDING (2018)



# What is Mandatory Spending?

COMPOSITION OF MANDATORY SPENDING (2018)

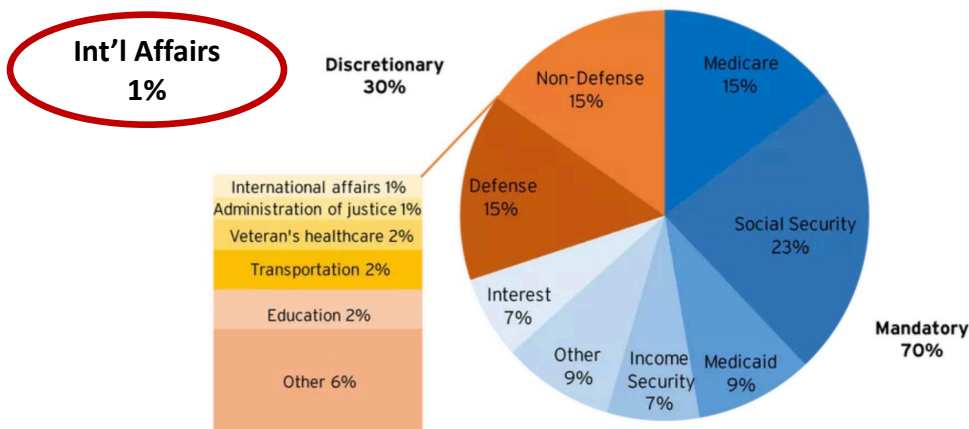


Source: Congressional Budget Office, Haver

Hutchins Center on Fiscal & Monetary Policy at BROOKINGS

# What is Discretionary Spending?

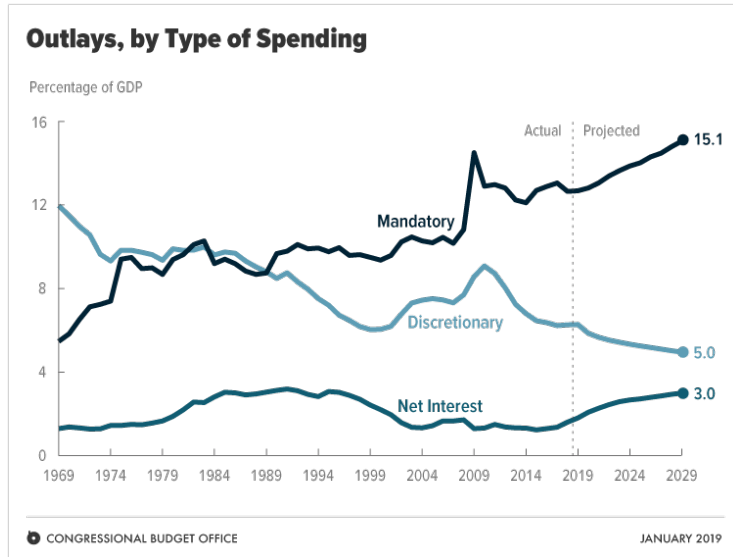
COMPOSITION OF DISCRETIONARY SPENDING (2017)



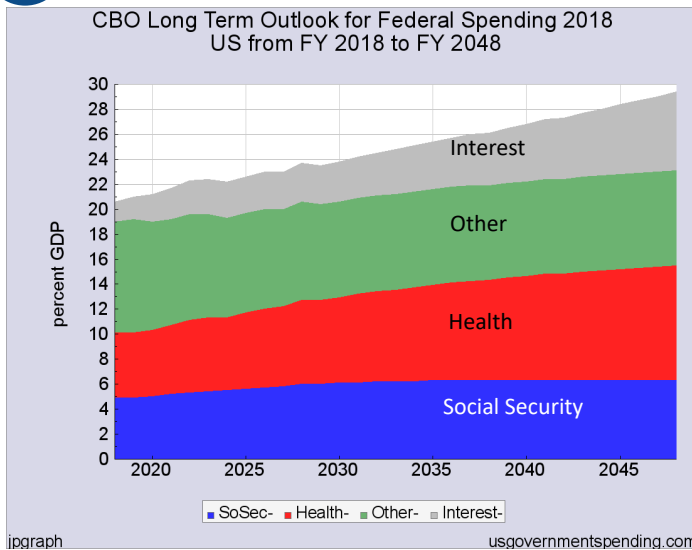
Source: Congressional Budget Office, Haver. Data are for 2017. Note: Numbers may not add up due to rounding.

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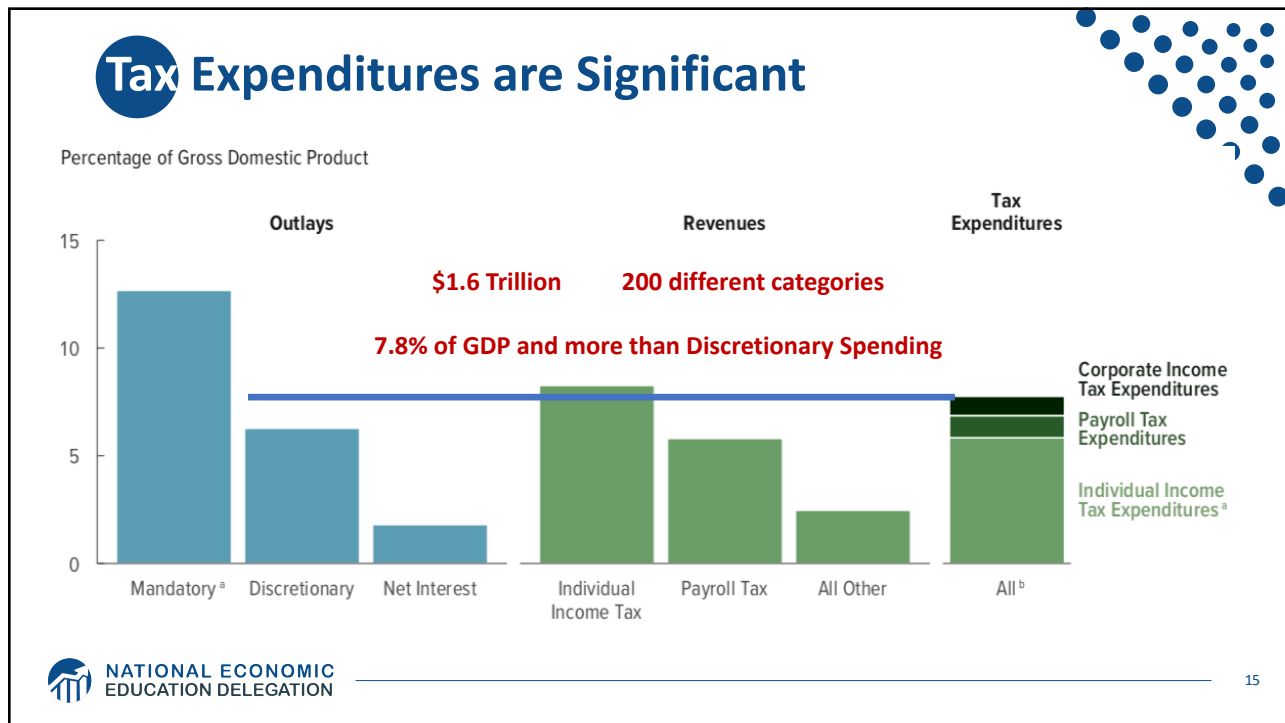
# Mandatory Spending Dominates Forecasts



# Forecast Spending



What trends do you see?



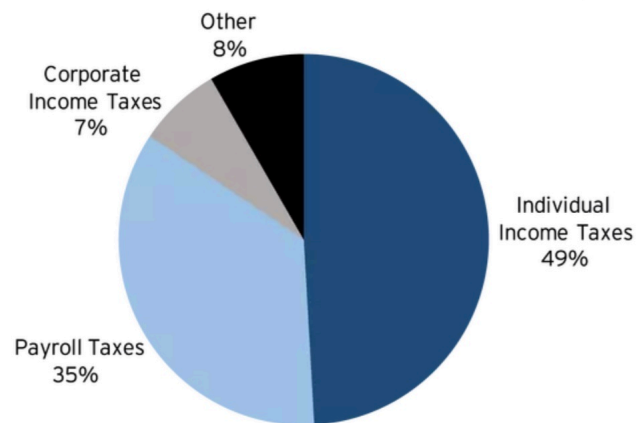
- ## Important things that people get from govt
- Roads and highways
  - Public education
  - Defense
  - Research and development
  - Space exploration
  - Income Security
  - Improved public health
    - Sanitation
  - Investments in communications
  - Energy
  - Many, many, inventions:
    - Microchips
    - GPS
    - Wind turbines
    - Tang
    - Touch screens
    - Internet
    - Bar Codes
    - Wii
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# US Government Revenues

## Where Do Government Revenues Come From?

COMPOSITION OF REVENUES (2018)

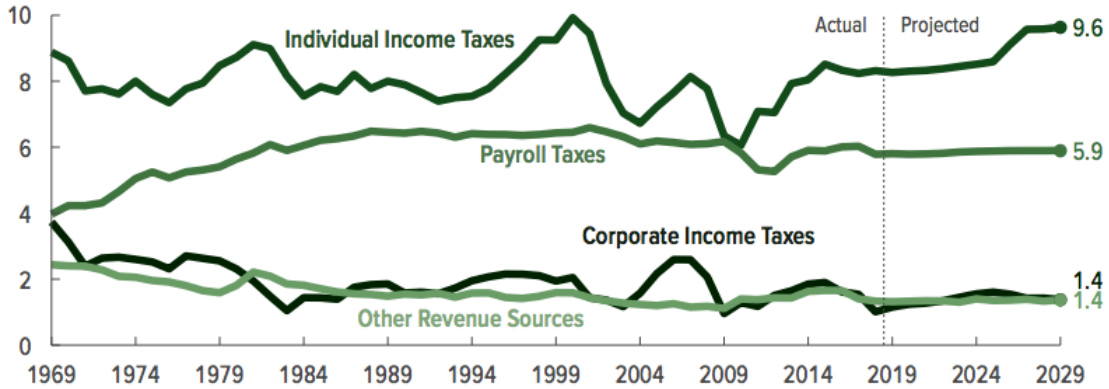


Source: Congressional Budget Office, Haver

Hutchins Center on Fiscal & Monetary Policy at BROOKINGS

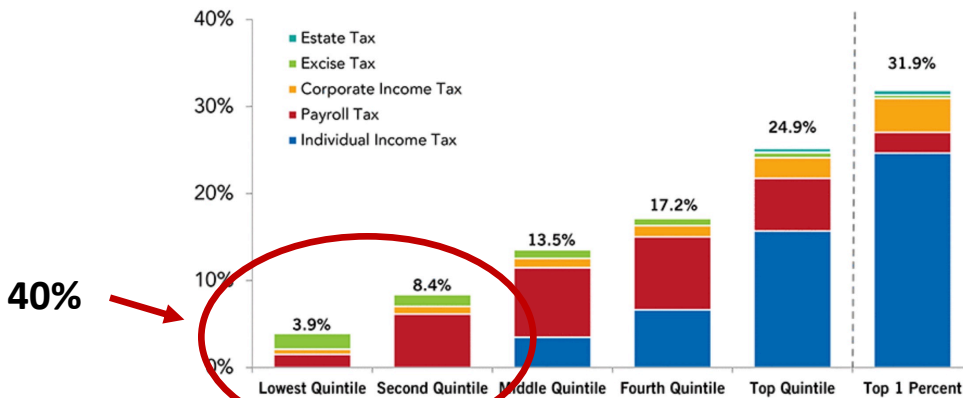
## Revenue Sources: Share of GDP over Time

Percentage of Gross Domestic Product



## The Bottom 40% Does Pay Other Taxes

EFFECTIVE FEDERAL TAX RATE (% OF CASH INCOME IN 2016)



SOURCE: Tax Policy Center, *Effective Federal Tax Rates by Expanded Cash Income Percentile*, March 2017. Data are for 2016. Compiled by PGPF.  
 NOTE: Individual income tax rates for the lowest and second lowest quintiles are negative and are netted against the payroll tax rate. A quintile is one fifth of the population. In 2017 dollars, the income breaks are: 20% \$24,600; 40% \$47,700; 60% \$84,300; 80% \$147,700; 99% \$717,900. Includes both filing and non-filing units but excludes those that are dependents of other tax units.

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## Summary: Slide 1

- **Total Spending: \$4.1 Trillion in 2018**
- **There is remarkably little discretion in each budget:**
  - Mandatory: 69%
  - Discretionary 31%
- **Fastest growing parts of the budget: Health Care and Interest**
- **By 2048:**
  - Debt is forecast to grow to 150% of GDP, from 80% today
  - Interest payments are forecast to grow from 8% to 22% of budget



## Summary: Slide 2

- **Categories that get a lot of attention are relatively small**
  - Foreign Aid: 1% of the budget
  - Income support/welfare: 8.7%
- **Or are not forecast to grow significantly**
  - Social security
  - Most other categories of spending
- **Tax Expenditures are Really Important**
  - Larger than all of discretionary spending.
  - Add 25% to spending.



# US Government Debt



## Of Debt, Deficits, and Surpluses

- **STOCK**

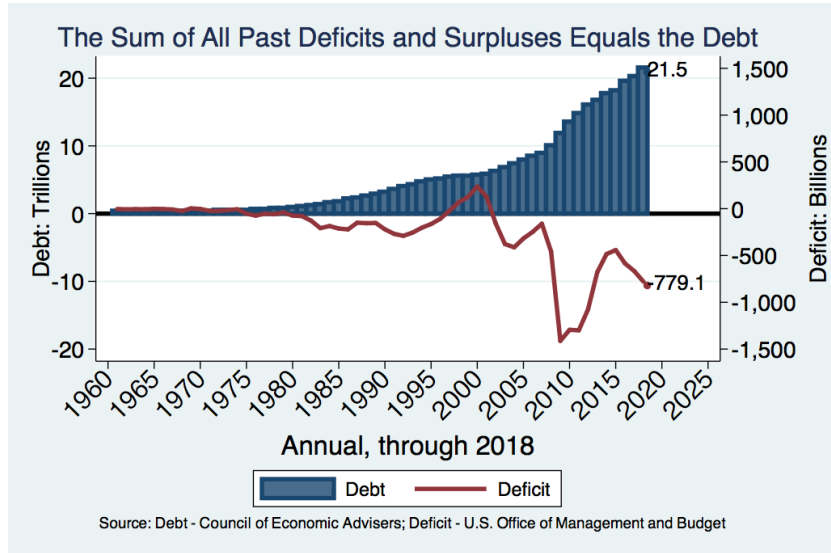
- **Debt**: The accumulation of debt over time.
  - The sum of all past debts and surpluses.

- **FLOW**

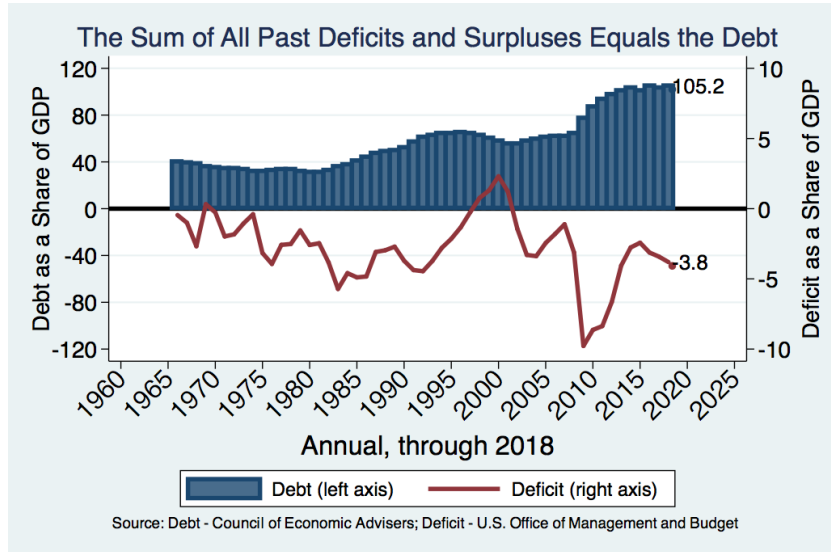
- **Deficit**: The amount of debt accrued in a single year.
- **Surplus**: The excess of revenues over expenses in a single year.



## Debt vs. Deficit



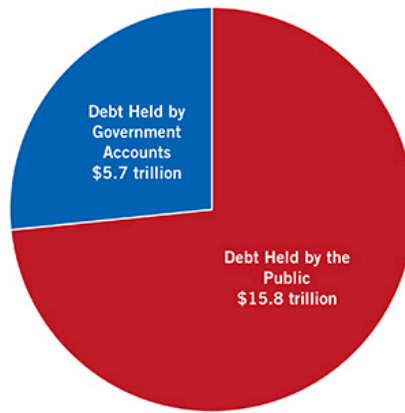
## Debt vs. Deficit: Share of GDP





### What makes up gross federal debt?

Gross Federal Debt at the End of Fiscal Year 2018:  
\$21.5 Trillion



SOURCE: Department of Treasury, *Monthly Treasury Statement*, issue for September 2018. Compiled by PGPF.  
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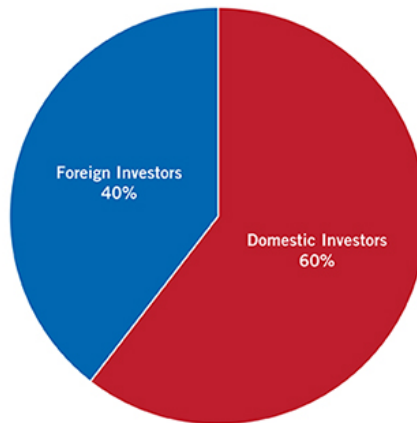
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### Foreign investors own over one-third of all U.S. public debt



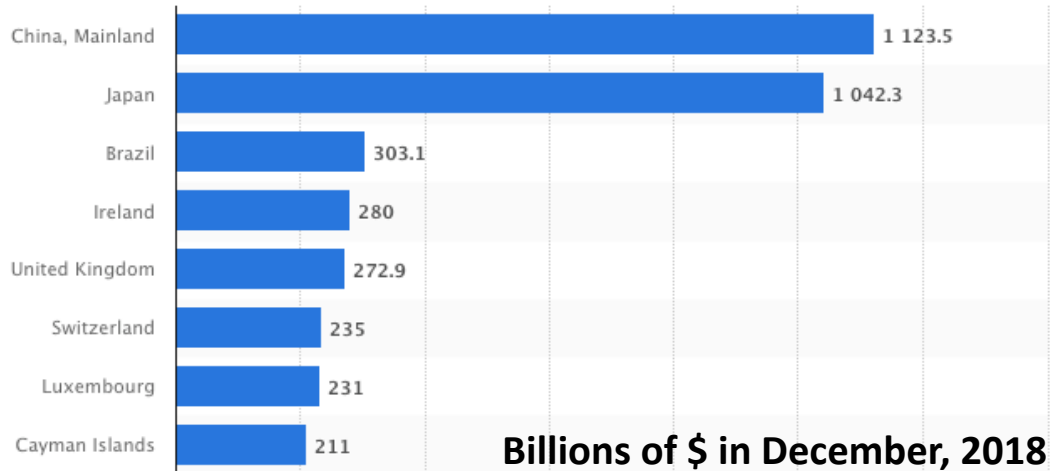
SOURCE: Department of the Treasury, *Monthly Treasury Statement*, issue for September 2018; and Department of Treasury, *Treasury Bulletin*, December 2018. Compiled by PGPF.  
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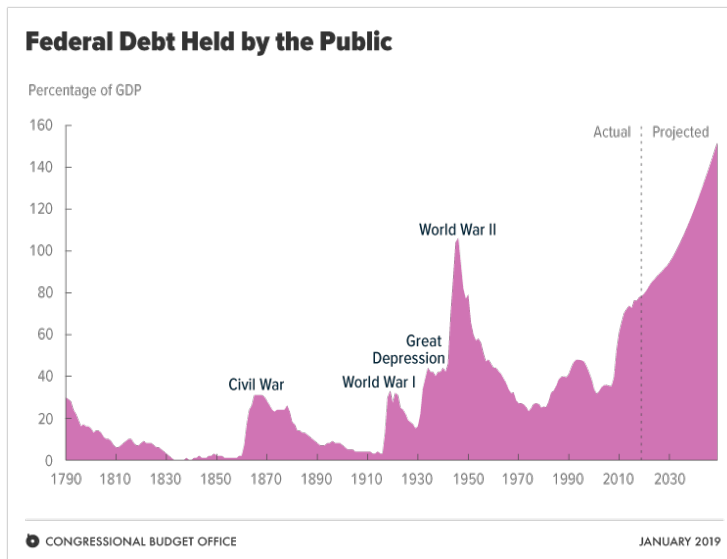


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## Who Holds Debt to Foreigners

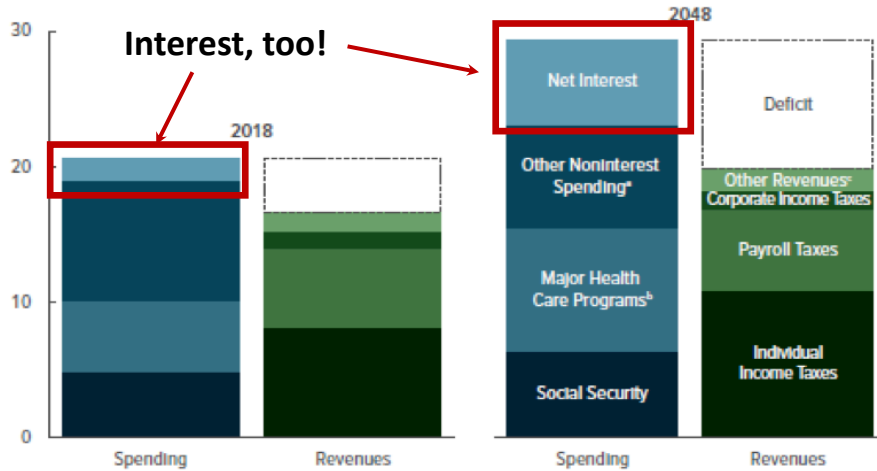


## Headed for Record Levels of Debt



## Deficit to Grow Much Faster than Revenues

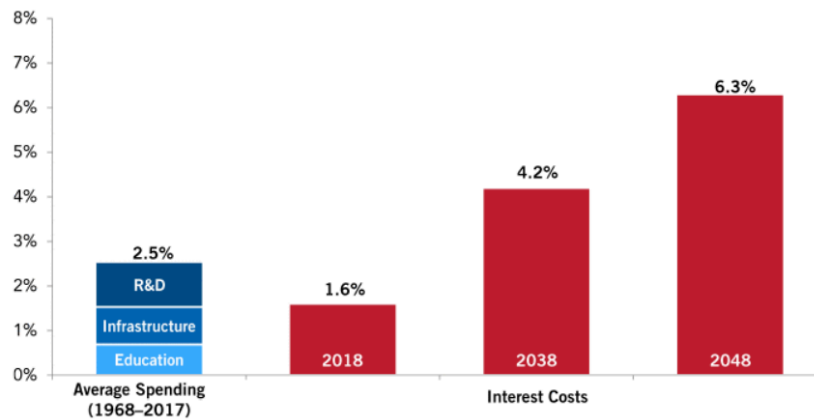
Percentage of Gross Domestic Product



Source: Congressional Budget Office.

## Interest Payments to Grow Significantly

FEDERAL SPENDING (% OF GDP)



SOURCE: Office of Management and Budget, *Budget of the United States Government, Fiscal Year 2019*, February 2018; Congressional Budget Office, *The 2018 Long-Term Budget Outlook*, June 2018. Compiled by PGPF.

NOTE: Infrastructure excludes defense.  
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## Perspectives on Increased Debt

- **Government borrowing CROWDS OUT private capital and investments.**
  - Weakened by ability to borrow from abroad.
- **Is it reasonable to borrow at low interest rates for investments?**
  - For example, infrastructure.
- **Does debt impose a burden on future generations?**
  - Does it inevitably have to be paid off?
- **In time, it may start to crowd out other government spending.**
  - Diminishing policy priorities in the budget.



## The Reason for Borrowing Matters

- **Two good reasons to borrow heavily:**
  - To support the economy during a recession – fiscal expansion.
  - Investments that will increase economic activity in the future.
- **Should not borrow for:**
  - Items consumed today
    - Government salaries
    - Retirement benefits
  - Tax breaks of uncertain benefit to the broader economy.



## Is the Debt a Problem Today?

- Currently borrow about \$100 Billion each month with little difficulty.
- Very little evidence of "crowding out".
- Interest rates are very low, less than 3% on 10-year notes.



## So, Why Worry About it?

- If debt gets too high:
  - There is the potential for investors to start questioning the *creditworthiness of the U.S. Government*.
    - Problem: Nobody knows how high might be too high?
  - It becomes more difficult to *borrow in times of crisis*.
    - War, severe recession
    - "Fiscal space" – impossible to measure how much we have, but clear that we have less now than back in 2007.
  - Could start to *crowd out* investments by consumers and businesses.
    - Not currently a problem. No idea if/when it might become one.
  - Could be inflationary.



## So, Why Worry About it?

- **If debt continues to grow:**

- **Interest payments** will grow with it.
  - 8% of spending in 2018.
  - 22% of spending in 2048.
  - Less room for using the budget for policy priorities.
  - 40% of payments go abroad.
- The longer we wait to address it, the **harder and more disruptive** it will be to address it.
- **Interest RATES** may increase.



## Are There Reasons to Wait?

- **Very little evidence of:**

- Crowding out
- Inflationary impact

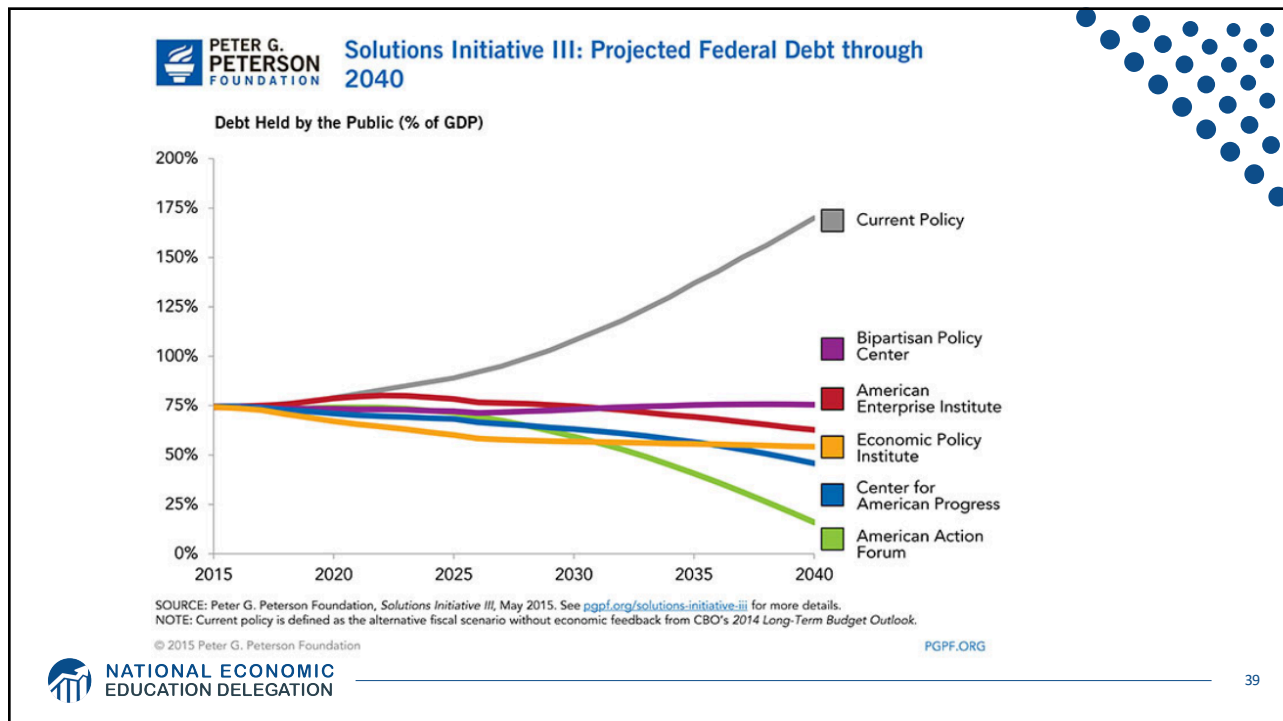
- **Uncertainty about the future**

- Economic growth may render action today unnecessary.

- **There are a great many investments to be made by the gov't.**

- Infrastructure
- Education
- Much, much more...





## Summary: The Debt

- The jury is (sort of) out on the debt.
- Conventional wisdom is being challenged:
  - Previously: inflationary and crowd out private investment
  - New assertion: these things don't matter for a country that can borrow in its own currency.
- Upshot?
  - This is a policy choice.
  - The cautious approach is to rein in the debt.
  - The cautious approach may lead to slower economic growth.

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## Bottom Line

- Question is not **WHETHER** the U.S. will have to act...  
...but **WHEN**.
- Some combination of the following **WILL** be necessary:
  - Raising taxes
  - Cutting spending
  - Reining in health care costs



Thank you!

## Any Questions?

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