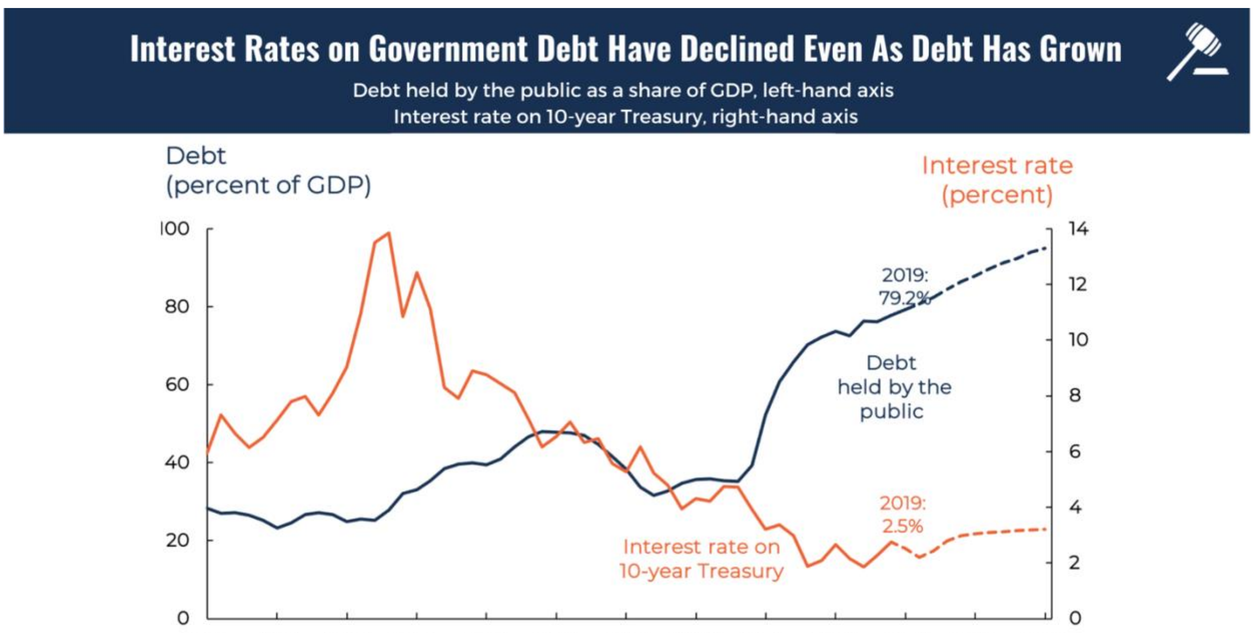
February 25, 2020

The Fiscal Outlook Has Deteriorated Under President Trump

In a recent hearing, Congressional Budget Office (CBO) Director Phillip Swagel presented the agency's updated Budget and Economic Outlook. The report shows a darkening fiscal future, with trillion-dollar deficits and near-record debt levels persisting through the next decade. Improving our fiscal outlook over the coming decades will require a fair tax system and responsible investments that reflect our nation's values and promote a stronger economy.

Our Fiscal Challenge Is Long Term

CBO projects that debt held by the public will rise from 81 percent of GDP in 2020 to 98 percent of GDP by 2030, higher than any point since just after World War II. However, interest rates have steadily declined to historical lows over the last several decades, a trend CBO expects to continue through the next decade. This reality has led mainstream economic experts toward a more nuanced understanding of our fiscal state. With interest rates low, Congress has the space to address our fiscal trajectory gradually. As Director Swagel argued, this is "a problem that's decades in the making and decades in the solving."



Source: Congressional Budget Office

Note: Data for both series are fiscal year. Values starting from 2020 are projected.

"It is not an emergency, but it is a long-term challenge"— Director Swagel stressed throughout the hearing that our fiscal outlook does not constitute a crisis. "When interest rates are low as they are today, the cost of not acting is pretty modest," he said. This does not mean that we can avoid acting, but it does mean "that we have the ability to do this over time...That it doesn't have to be a wrenching change, whether on the spending side or on the revenue side." Ultimately, Director Swagel explained, "the challenge is getting a start on addressing the situation over time. It doesn't have to be done this second."

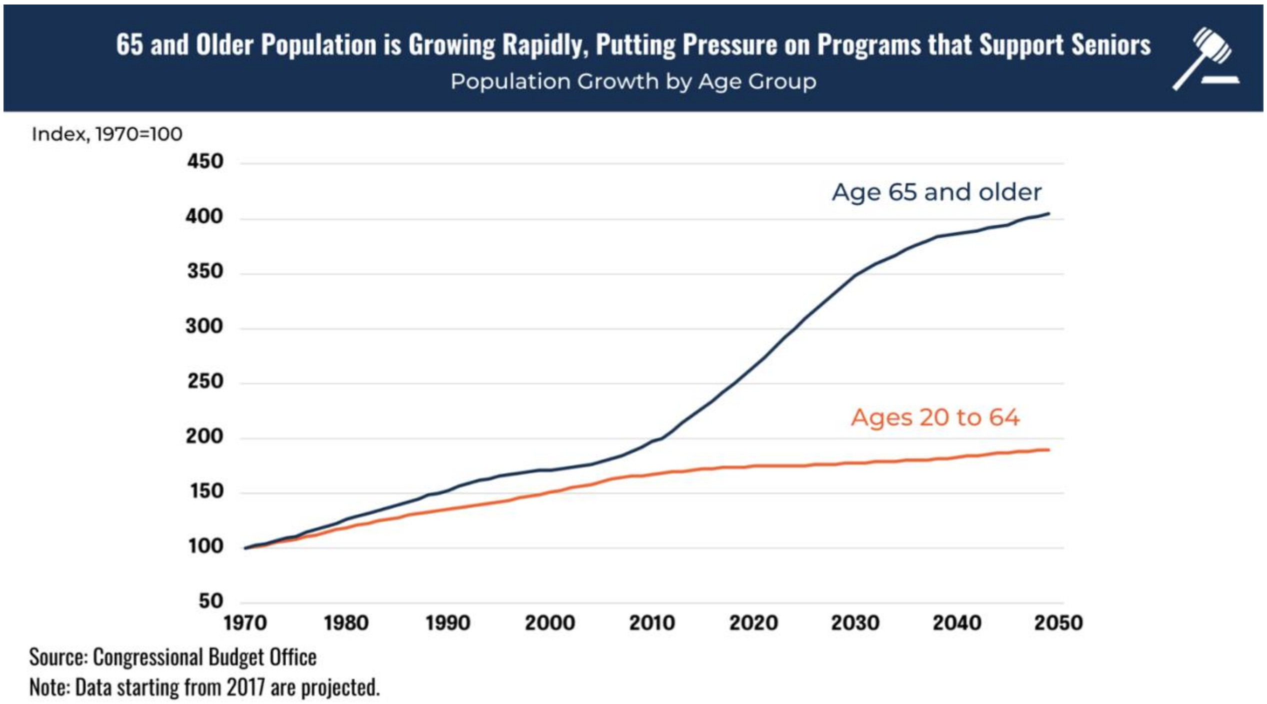
Fiscal sustainability "does not require a balanced budget"— Echoing a position Federal Reserve Chair Jerome Powell shared with the Committee last year, Director Swagel clarified that putting the federal budget on a sustainable path does not mean deficits must be eliminated entirely. Instead, it "means bringing the deficit down low enough so that the debt level does not continue to rise. And that does not require a balanced budget because as long as GDP is growing, we can run a deficit without increasing the debt-to-GDP level…That is the best measure for capacity."

"**The United States has the ability to undertake fiscal policy today for whatever purpose**" — Director Swagel noted that CBO lowered its projection of interest rates in its latest forecast, a reflection of the fact that "markets today are not concerned" about the sustainability of our debt. With interest rates expected to remain low going forward, "the budget challenge is there, but it is not immediate, and Congress has the ability to undertake initiatives" – including to repair our infrastructure, promote affordable housing, bolster workforce training programs, and invest in our environmental resilience. Director Swagel also emphasized that Congress has the fiscal space to counteract the next economic downturn, or any other crisis we face: "if there is some problem today, whether it is economic or national security, we have the fiscal ability, if the Congress chooses, to respond."

Our Fiscal Challenge Cannot Be Solved on the Backs of Seniors

With more than 1-in-5 Americans expected to be aged 65 and older by 2030, more people will rely on Social Security, Medicare, and Medicaid for their retirement and health security. The aging of the U.S. population, combined with the long-term trend of rising health-care costs, suggests that keeping our commitments to our nation's seniors in the years to come will require more resources than in the past. As Chairman John Yarmuth noted, "it's not simple, saying we are going to do something about mandatory spending in this country, because it is an essential part of the economy and the life of many of our citizens."

"Those two trends, aging and health care costs, affect Social Security and Medicare in particular. And we see those trends persisting beyond the 10-year budget horizon" — CBO projects that mandatory spending will increase from 12.9 percent of GDP this year to 15.2 percent by 2030. This increase is driven entirely by higher spending on Social Security and health care, while spending on other mandatory programs – such as for income security and veterans – is projected to fall. As Director Swagel noted, this is a predictable trend in an aging society. Mandatory spending as a share of GDP has more than doubled over the last 50 years, coincident with a near-tripling of the 65-and-older population over the same period. With this population projected to grow six times faster than the working-age population over the next 30 years, and with per-beneficiary health care costs expected to grow faster than the economy, spending on programs that ensure seniors' health and economic security will continue to grow over the coming decades.

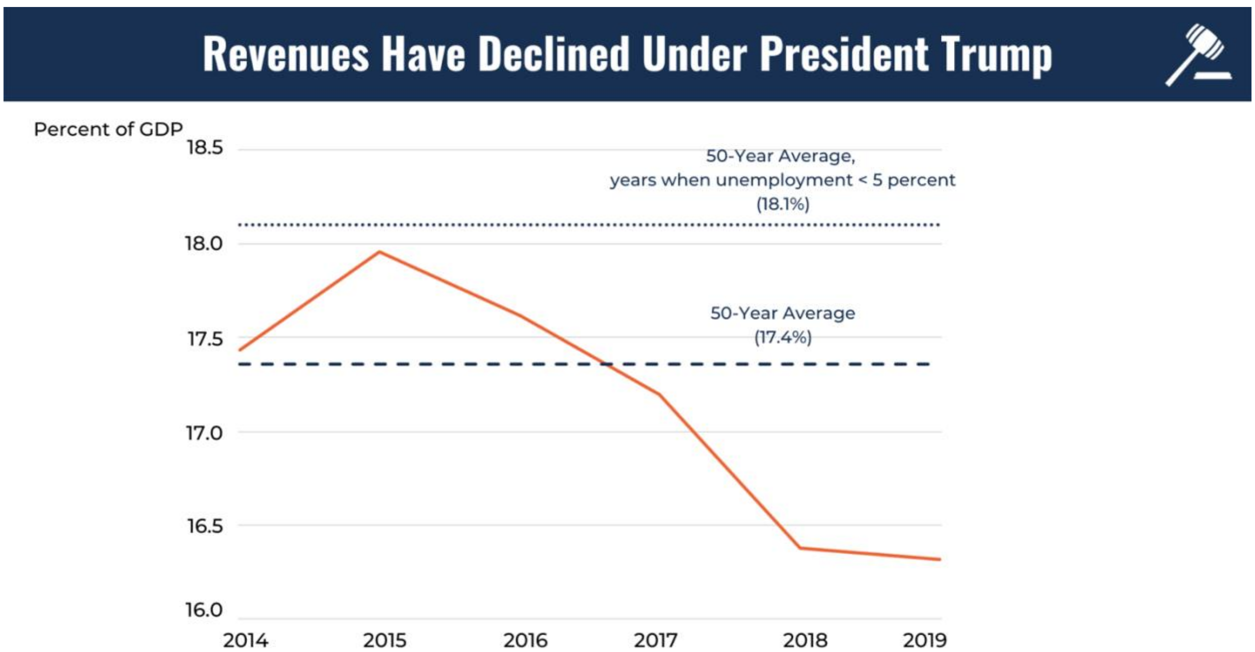


"The challenge is that spending is projected to grow more than revenues, widening the gap between spending and revenues" — Director Swagel characterized the driver of our long-term fiscal challenge as the *gap* between spending and revenues, rather than the absolute level of either spending or revenue by itself. CBO projects that total federal spending as a share of the economy will be 3 percentage points higher than its 50-year average in 2030. Revenue as a share of the economy, however, will be only 0.6 percentage points higher than its historical average – despite the fact the senior citizen population will be significantly larger than any point in the last half century.

The 2017 GOP tax law – which primarily benefits the wealthy and corporations – added $1.9 trillion to the debt, but Committee Republicans suggested that does not matter because deficits would still be high without the tax law. Instead, they repeatedly and systematically ignore the revenue side of the equation – insisting that Congress can only address deficits by cutting spending from the very programs that are so vital to seniors' well-being. By focusing solely on mandatory spending, Republicans deny the reality that we will need additional revenues to keep our promises to America's seniors. As Representative Dan Kildee (MI-5) pointed out: "to take the President's proposal to cut Medicare and the President's proposal to cut Social Security and call that reform by placing it on the backs of the people who can least afford it, but happily celebrate and throw parties and parades for tax policy that gave the wealthiest people in this country massive breaks at the cost of everyone else and then say 'well it only added to 14 percent of our fiscal problem' is not a very good argument."

We Have a Revenue Problem

Measured in nominal dollars, revenues *always* increase when the economy is growing, so the fact that nominal revenues were higher last year than the year before tells us nothing useful about whether current tax policy is bringing in enough revenue to meet our needs. More meaningful measures, however, clearly show that no matter how you cut it, revenues are low.



Source: Congressional Budget Office

- **As a share of GDP**: Revenues as a share of GDP were 16.3 percent in 2019 – more than a percentage point below the 50-year average (17.4 percent) and the lowest they have been in the past half century except in the aftermaths of the past two recessions.

- **As a share of GDP in good economic times**: In years in which the unemployment rate was at or below 5 percent – which has been the case since 2016 and which CBO expects will continue through the next decade – revenues have averaged 18.1 percent over the last half century. This is nearly *2* percentage points above our current level.

- **Nominal year-over-year growth**: Nominal revenues grew by 4 percent between 2018 and 2019 and are projected to increase by 4.9 percent in 2020. Over the last 50 years, year-over-year nominal revenue growth has averaged more than 6 percent.

- **Compared with pre-tax law baseline:** In the summer before the 2017 tax law was enacted, CBO projected revenue in 2019 would be 17.8 percent of GDP – 1.5 percentage points higher than it actually was.

- **Compared with other developed countries:** In 2018, total tax revenue for all levels of government in the United States was 24.3 percent of GDP, 10 percentage points below the Organization for Economic Cooperation and Development (OECD) average.

- **Compared to our needs:** Though the nation's 65-and-older population is nearly three times larger today than it was 50 years ago, we are taking in less revenue as a share of the economy now than we were then.

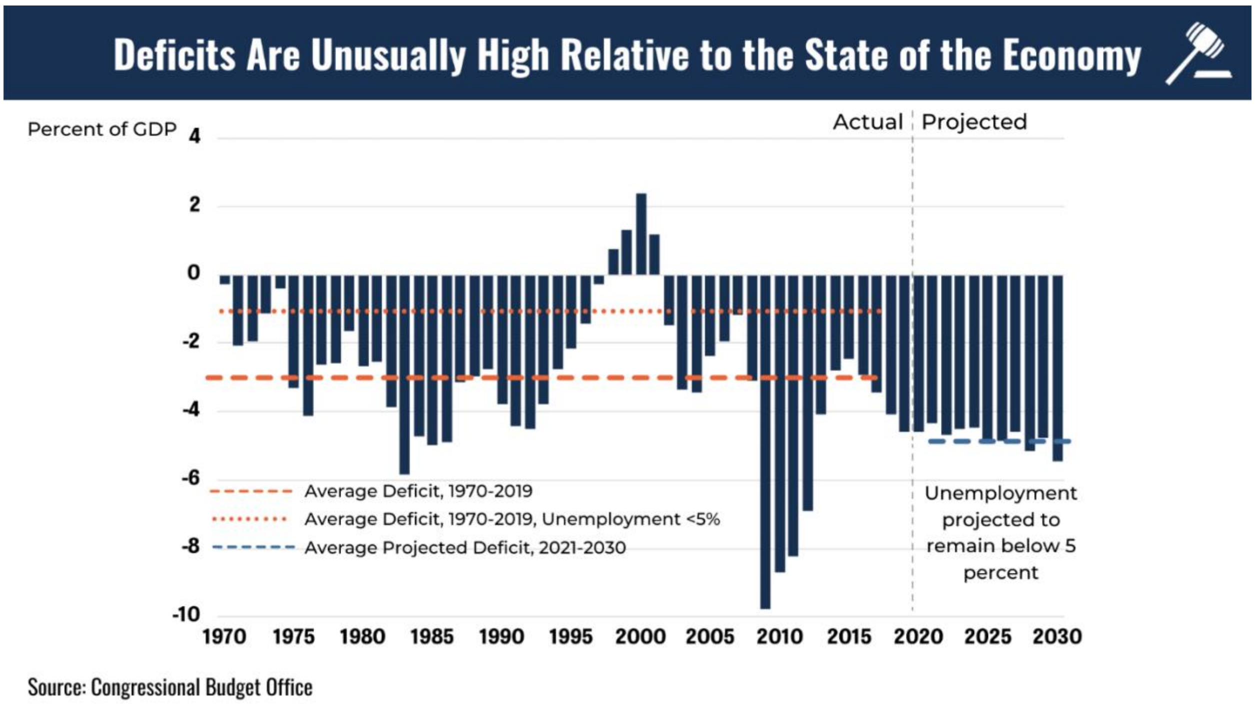
GOP Tax Law Exacerbated Our Fiscal Challenge

The GOP tax law worsened the gap between revenues and spending, further straining our budget while providing little in return. Director Swagel's testimony confirmed that the tax law is not anywhere close to paying for itself, despite the Trump Administration's insistence otherwise, and may even cost more than CBO's initial projections – helping to push deficits to unprecedented heights.

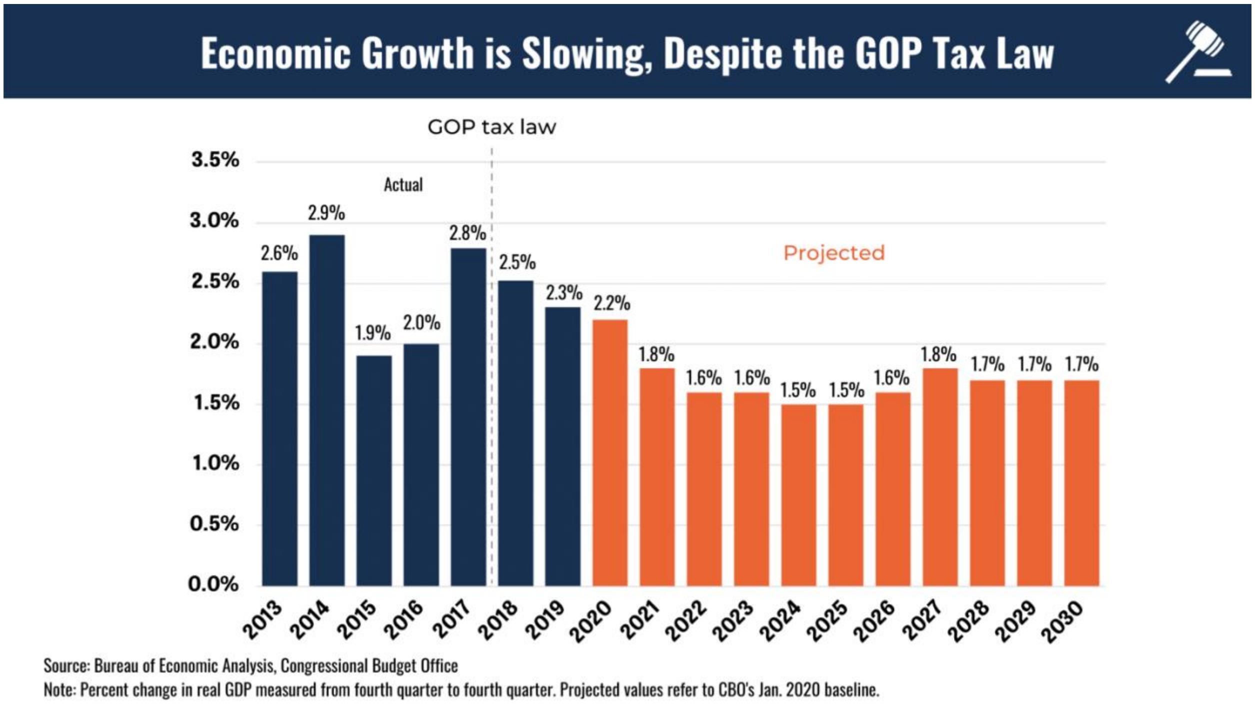
"We don't see the tax cut as for paying for itself" — Director Swagel stood by CBO's initial 2018 estimate that the GOP tax law would add $1.9 trillion to deficits over a decade, noting that it "is adding about one percentage point of GDP to the deficit" each year. In 2020, CBO estimates it will account for 1.2 percentage points – more than one quarter – of our 4.6 percent of GDP deficit. When asked by Vice Chair Seth Moulton (MA-06) "what single law signed by President Trump is the single largest contributor to the deficit and debt growth over a 10-year period," Director Swagel was unequivocal: "that would be the December 2017 tax act."

Director Swagel also described CBO's updated estimates which show that implementation of the tax law *further* reduced revenues by $110 billion – suggesting it could cost even more than the $1.9 trillion initially estimated. As CBO's outlook states, corporate revenues will be 3.2 percent lower than expected, in part due to the Trump Administration's regulations pertaining to the law's international provisions. In fact, since the GOP tax law was enacted, CBO forecasts have lowered projected corporate revenues by almost $800 billion, more than the double the $320 billion cost initially forecasted for the law's business and international provisions. This worse-than-expected drop in corporate revenues will exacerbate our fiscal challenge.

“The noteworthy thing about the economic and budget situation today is that the deficit is wide and the debt is rising when the economy is this strong” — CBO’s latest outlook shows that the Trump Administration’s economy has made history, but not in the way it hoped. As Director Swagel noted in the opening of his testimony, “Not since World War II has the country seen deficits during times of low unemployment that are as large as those that we project—nor, in the past century, has it experienced large deficits for as long as we project.” Between 1969 and 2018, deficits averaged 0.7 percent of GDP in years when the unemployment rate was below 5 percent. By contrast, the deficit in 2019 was 4.6 percent of GDP – driven in part by lost revenue due to the GOP tax law – and is expected to average 4.8 percent over the next decade. This “is unusual and it makes the challenge we face yet larger,” Director Swagel said.



“In our projection, GDP growth goes down” — In response to questions about whether the GOP tax law spurred annual economic growth of 3-4 percent as many Republicans promised, Director Swagel said “we don’t see that happening,” adding “I should say our GDP projection is well within the range of other forecasters” (though, notably, not the Trump Administration). CBO projects economic growth will average 1.7 percent over the next decade, “lower than the historical average because of long-term demographic trends,” he explained. What’s more, CBO now projects *lower* average economic growth over the 2021-2027 period than it did in June 2017, before the tax law was enacted.

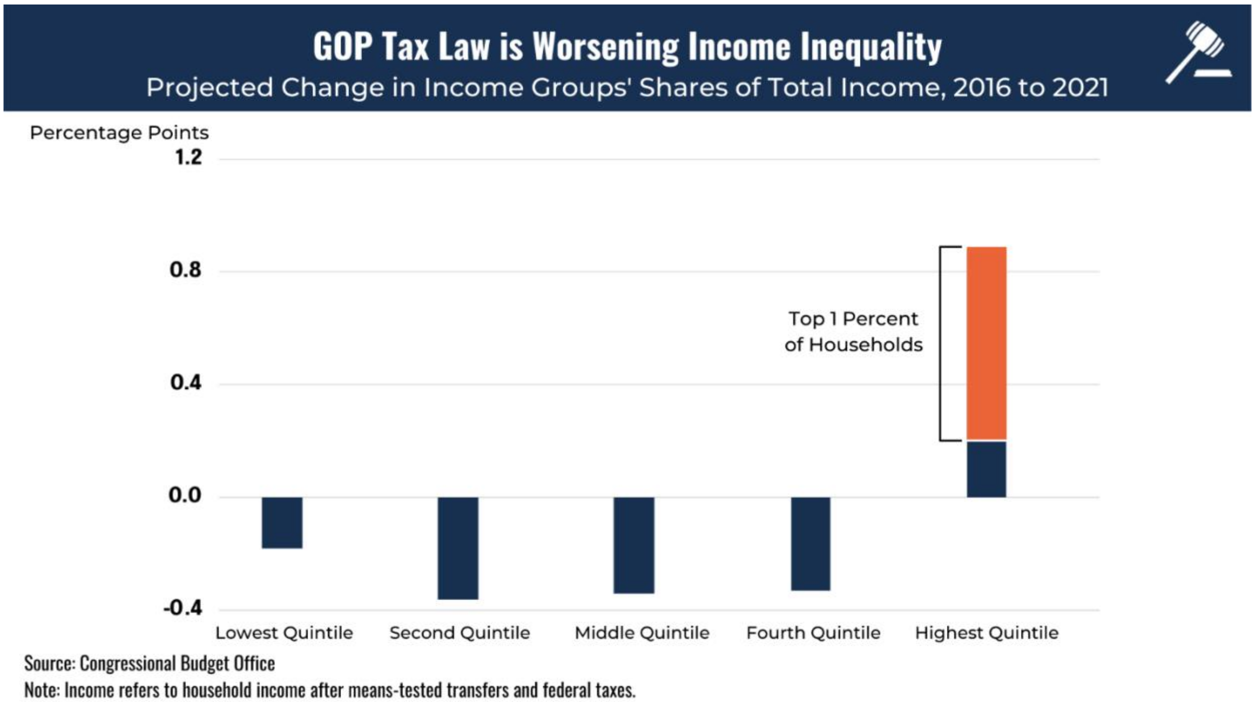


Income Inequality is Getting Worse

In response to several Member questions, Director Swagel summarized key findings from another recent CBO report, which forecasts changes to the distribution of real household income between 2016 and 2021. The report projects that income inequality will worsen over this period, with incomes – before and, especially, after taxes and means-tested transfers – growing fastest for households at the top of the distribution. Of the policies that have occurred or are projected to occur over this period, CBO's report states that "the change affecting the distribution of household income most significantly is the implementation of the 2017 tax act."

"**We show greater inequality in 2021**" — CBO projects that the share of income (after taxes and transfers) received by households in the top 1 percent will increase by nearly a percentage point between 2016 and 2021, from 12.5 to 13.4 percent. By contrast, the share of income received by the bottom 80 percent of American households will decline over this period. While our tax and transfer systems generally reduce inequality, Director Swagel noted that "our projection is that they will do less to attenuate inequality" in 2021 than they did in 2016 – "and this is characteristic of the 2017 tax act." If Congress wanted to address this projected rise in inequality, "more could be done in the short term with either taxes or transfers," he suggested.

"**We know that inequality doesn't have just these short-term effects, but over time it means a weaker economy and a weaker society**" — Director Swagel explained that rising inequality has long-run economic consequences that pose a "key challenge for the nation." As he noted, "the children of families at the bottom have more difficult situations and worse trajectories...that in some sense is an intergenerational transmission of inequality and of poverty." Mitigating these impacts and promoting greater economic mobility would require addressing the challenges that families at the bottom of the income distribution face most acutely, including accessing high-quality education, housing, transportation, childcare, and elder care – "all the things that would make it possible for people at the bottom to work and to have a rising wage profile."

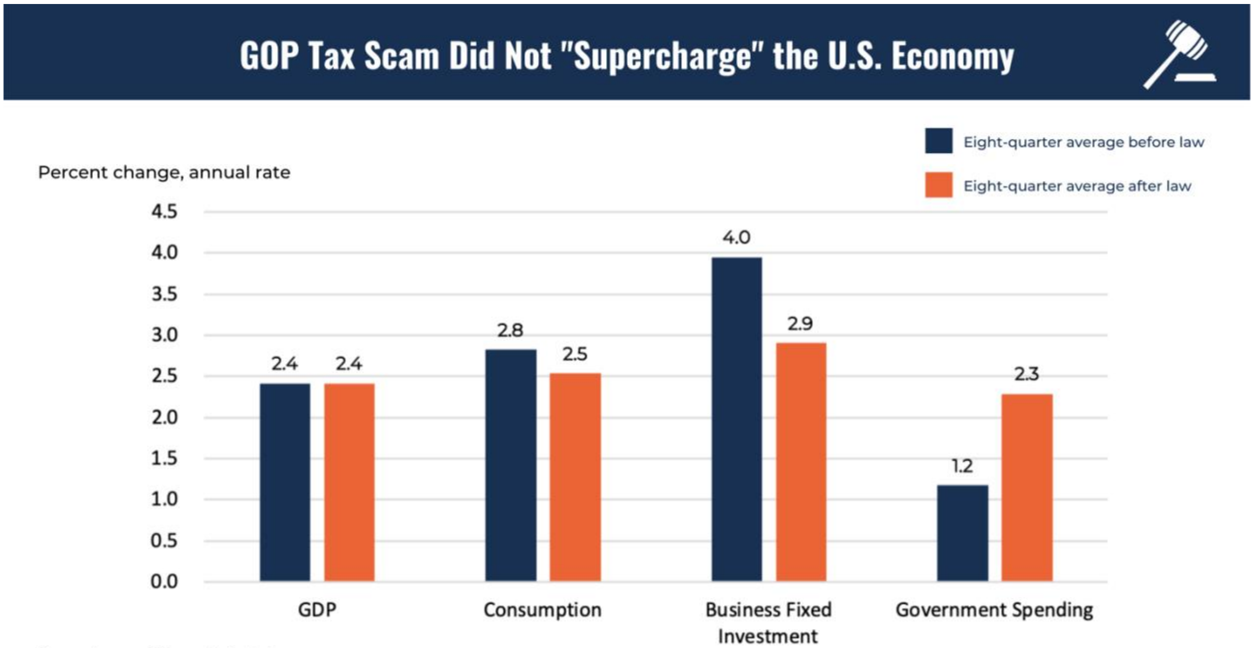


Director Swagel added that "the striking thing about the economic situation today" is that even with low unemployment, there are millions of Americans on the sidelines who face barriers to work. "We know these challenges of homelessness and addiction. These issues with opioids, mental illness. There [are] a lot of challenges that affect the bottom of the distribution."

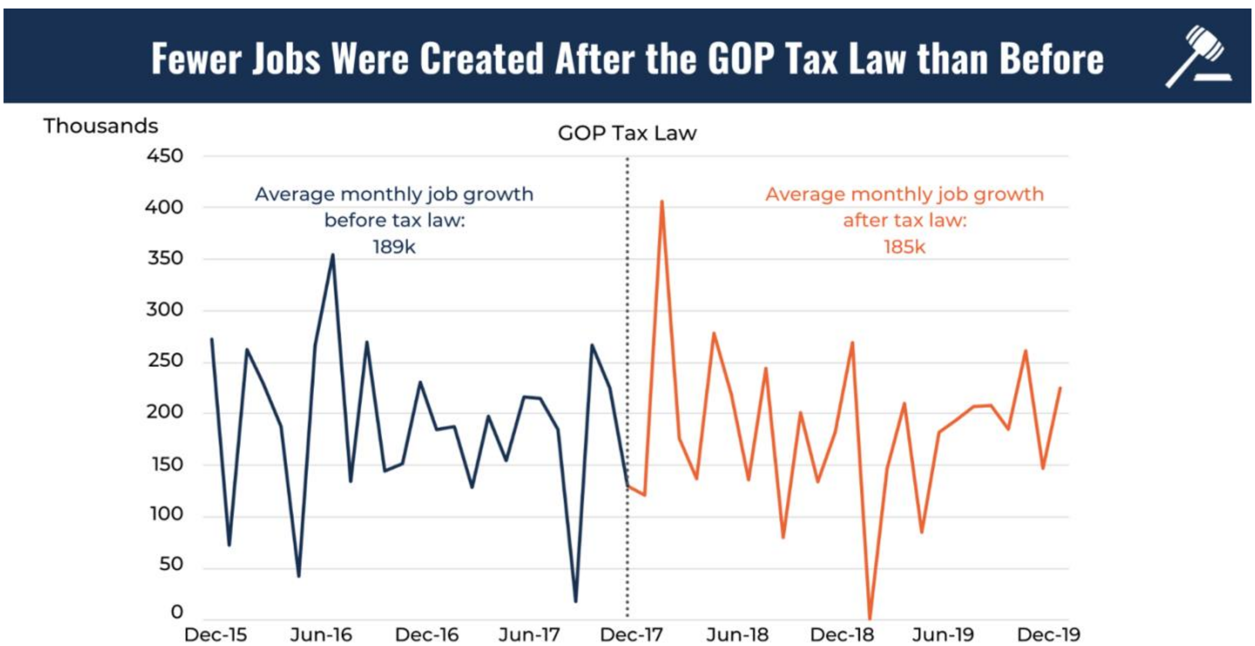
GOP Tax Law Was a Squandered Opportunity

Director Swagel reminded Members that a policy's effect on deficits is "not the only standard" by which we should evaluate fiscal policies. While infrastructure projects and other investments can yield economic returns that exceed their fiscal costs, other policies may be necessary and worthwhile even if they do not: "if it costs money," he noted, "sometimes it is worth it."

There is little evidence the tax law has had a meaningful or sustained economic impact beyond aggravating inequality. Economic growth in the eight quarters since the law was enacted averaged 2.4 percent – the same growth rate in the eight quarters before the law. And there has been little change in the pace of job growth; in fact, fewer jobs were created in the two years after the tax law than in the two years before it. The idea that tax cuts primarily for the wealthy and corporations would unleash an economic miracle and grow us out of debt – one of the most enduring and destructive conservative myths – has again proven incorrect.



Source: Bureau of Economic Analysis
Pre-tax law period reflects 2015: Q4 to 2017: Q4; post-tax law period reflects 2017:Q4 to 2019: Q4.



Source: Bureau of Labor Statistics
Note: Monthly change in nonfarm employment. Averages refer to the 25 months before and after the tax law was enacted.

Thus, the tax law was a squandered opportunity to invest in our families, nation, and future. As Representative Lloyd Doggett (TX-35) put it, "the same people that told us we can't afford more medical research. We can't afford better schools. We can't provide health care for more Americans. We can't meet our infrastructure needs with our crumbling roads. When it came to helping the very rich in this country and multinational corporations, they could not do enough."

Conclusion

CBO's latest baseline makes clear that we must use our nation's resources more wisely going forward. This means prioritizing policies that will help more American families get ahead in this economy, prepare our communities for the opportunities of the future, and improve the well-being of current and future generations.