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# CBO's updated budget and economic outlook paints a bleak long-term fiscal picture

The latest annual projections from the nonpartisan Congressional Budget Office (CBO) assessing the state of the US budget and economy for the next decade show a large and growing mismatch between federal revenues and spending even as the agency sees certain economic factors returning to more normal levels in the coming years.

**Revenue, spending projections**

CBO's *Budget and Economic Outlook: 2022 to 2032*, which was released on May 25, predicts budget deficits will average 5.1 percent of gross domestic product (GDP) over the next decade—almost one-and-a-half times higher than the average 3.5 percent of GDP deficit registered over the past 50 years.
**URL:** https://www.cbo.gov/publication/58147

Although the deficit is projected to fall to about $1 trillion—or 4.2 percent of GDP—in the current fiscal year (fiscal 2022) from almost $2.8 trillion last year, demographic pressures and other factors will push deficits steadily higher in later years.

**Revenues and spending:** CBO sees federal revenues reaching 19.6 percent of GDP this year—a two-decade high. However, over the course of the next 10 years, CBO projects revenues will hover within a relatively narrow band and average 18.1 percent of GDP, a bit north of the 17.3 percent of GDP average over the past five decades.

Although revenues have been marked up slightly compared to CBO's prior projections last year, that increase is due mainly to changes in economic and technical factors that underpin the budget baseline.

"Most of that [revenue] increase stems from changes in CBO's economic forecast, primarily its projections of GDP and the types of income that make up GDP, such as wages and salaries, corporate profits, and proprietor's income," the report states.

Meanwhile, federal spending—which has fallen sharply from its pandemic-era highs—is expected to resume its steady climb due to pre-existing demographic trends that are projected to increase the ranks of Social Security and Medicare beneficiaries and thus push up spending within those programs. By 2032, outlays would exceed 24 percent of the economy.

Over the past 50 years, spending has averaged about 20.8 percent of GDP.

**Publicly held debt:** In its January 2020 long-term outlook (published before the pandemic), CBO had projected that debt held by the public—that is, federal debt not held in intragovernmental accounts such as Social Security and Medicare Trust funds—would not reach 100 percent of GDP until the early 2030s.


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This week's analysis, however, shows that dubious milestone will be reached by 2027, and that publicly held debt will climb to 107 percent of the economy by the end of the 10-year budget window. (Actually, debt briefly crossed 100 percent of the economy by the end of fiscal year 2020, but then fell again as pandemic-related pressures began to wane).

**Inflation, interest rates, GDP:** On the economic front, CBO forecasts that currently elevated levels of inflation will normalize at about 2.3 percent annual price growth—as measured by the Consumer Price Index—after 2023, while annual economic growth (adjusted for inflation) will settle in at about 1.7 percent over the same time span. Inherent in these projections is an assumption that the Federal Reserve's current campaign to raise the Federal Funds Rate will result in a so-called "soft landing" that blunts annual price growth without triggering a recession.

Those short-term interest rate increases, however, will also serve to push up longer-term rates as well as the government's debt service costs. According to CBO, the average rate on 10-year Treasury bonds will rise from about 2.7 percent this year to 3.8 percent over the latter half of the budget window. As a result, interest payments on the national debt are projected to average 2.6 percent of GDP over the next decade, up from a 1.9 percent of GDP average in last year's report—a roughly 37 percent increase.

**'Current law' caveat**

It is important to note that, by law, CBO is generally required to make its projections on the basis of "current law," or laws as they are currently in effect. (One exception is excise taxes dedicated to trust funds—for example, highway taxes—which are assumed to be continued beyond any scheduled expiration).

That means this week's analysis does not account for the budget impact—which could be significant—of any potential "Build Back Better" legislation that is currently being pursued by congressional Democrats and President Biden. Although the prospects for any deal on this front remain highly uncertain, recent statements from key senators such as Joe Manchin, D-W.Va., suggest that any Build Back Better package that could secure the support of all 50 Senate Democrats—and thus win passage in the chamber under fast-track budget reconciliation rules—may reduce deficits, on net, by several hundred billion dollars over the next decade. (For prior coverage, see *Tax News & Views*, Vol. 23, No. 15, Apr. 29, 2022.)
**URL:** https://dhub.blob.core.windows.net/dhub/Newsletters/Tax/2022/TNV/220429_1.html

In comments to reporters on May 26, Manchin once again insisted that a portion of revenue raised from tax increases in a potential reconciliation bill must be applied to deficit reduction.

"Reconciliation is for getting your financial house in order, OK? So you have to have a tax adjustment to do that," he said.

On the flip side, also inherent in CBO's projections is an assumption that the temporary tax provisions scheduled to expire over the budget window—including nearly all of the individual tax changes and the passthrough deduction under section 199A that were enacted in the Tax Cuts and Jobs Act of 2017 (TCJA, P.L.


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115-97) and are set to lapse after 2025—will not be renewed, and revenues will be higher as a result. That assumption similarly applies to certain other TCJA provisions—affecting bonus depreciation, the business interest deduction limitation under section 163(j), the timing of research expenditure deductions, and the minimum tax on US multinationals known as the global intangible low-taxed income regime—that, if left untouched by lawmakers, will have the effect of raising revenue under current law later in the budget window. (A list of all the temporary tax provisions that expired in 2021 or are scheduled to expire through 2031 is available from the Joint Committee on Taxation staff.)
**URL:** https://www.jct.gov/publications/2022/jcx-1-22/

Thus, if additional stimulus legislation is enacted into law, or if temporary tax provisions are instead made permanent or otherwise extended beyond their scheduled expiration, future deficits may be higher than this week's CBO projections, while passage of a deficit-reducing reconciliation package could have the opposite effect.

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