CBO: Long-term budget outlook remains bleak

The nonpartisan Congressional Budget Office (CBO) on July 27 released its annual Long-Term Budget Outlook, which continues to paint a sobering picture of the nation's projected fiscal condition over the next 30 years.
URL: https://www.cbo.gov/system/files/2022-07/57971-LTBO.pdf

The report, which extrapolates CBO's typical 10-year current-law "baseline" projections through 2052, predicts the federal debt held by the public (that is, debt not held in intragovernmental accounts such as the Social Security trust fund) will reach 185 percent of gross domestic product (GDP) by the end of the 30-year window.

The largest debt-to-GDP level in recorded US history—106 percent—was reached in 1946 in the wake of World War II.

Those increasing debt levels are the product of large and growing annual budget deficits that would consistently rise from about 3.9 percent of GDP in the current fiscal year to more than 11 percent of GDP in 2052. Over the past five decades, budget deficits have averaged 3.5 percent annually.

Revenue and spending mismatch

As it has many times in recent years, CBO once again attributes those large and growing deficits to a fundamental mismatch between revenues and spending driven in part by the continuing retirement of the Baby Boom generation (which is resulting in a greater number of Medicare and Social Security beneficiaries), lower birth rates, and health care cost growth.

Revenues: In CBO's estimation, revenues will rise gradually over the next few decades—from about 18.1 percent of GDP in the most recently completed fiscal year (that is, fiscal year 2021) to 19.1 percent of GDP by 2052—as the economy recovers, temporary tax cuts expire, scheduled tax increases take effect, and more income is taxed at higher rates due to a concept called "bracket creep" (or the tendency of revenues to naturally rise over time as wage growth exceeds the inflation index to which the individual tax brackets are tied). Accelerating distributions from tax-deferred retirement plans by Baby Boomers exiting the workforce also plays a role.

Over the past five decades, revenues have averaged slightly more than 17 percent of the economy.

Spending and debt service: Another notable metric in this week's report—and a large contributor to future deficits, along with growing outlays on Social Security and Medicare due to the aging population and growing health care expenses—relates to the government's projected debt service costs. Though low interest rates—at least up until to the Federal Reserve's recent campaign to raise the Federal Funds Rate—have caused the CBO to significantly write down its estimates of what the government will spend on interest over the medium term, it does not see that trend continuing after 2030. Between 2030 and 2052, the agency projects the government's net interest costs will more than double from 3 percent of GDP to 7.2 percent of GDP.

Copyright © 2022 Deloitte Development LLC
All rights reserved.

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 potential budget impact of the Inflation Reduction Act of 2022—an unexpected deal struck Senate Majority Leader Charles Schumer, D-N.Y., and Sen. Joe Manchin, D-W.Va., and released late July 27 after months of negotiations—and which, according to a summary, could reduce budget deficits, on net, by roughly $300 billion over the next decade. (See related coverage in this issue for the latest news on Senate Democrats' apparent budget reconciliation deal and its prospects for passage in the coming days.)

On the flip side, also inherent in CBO's projections is an assumption that most expiring tax provisions—including, most notably, nearly all of the individual tax changes in the Tax Cuts and Jobs Act of 2017 (TCJA, P.L. 115-97) as well as the TCJA's passthrough deduction under section 199A, which are scheduled to lapse after 2025—will not be renewed, and revenues will be higher as a result. That assumption similarly applies to current and pending changes affecting bonus depreciation, the interest deduction limitation under section 163(j), the timing of research expenditure deductions, and the minimum tax affecting US multinationals known as the Global Intangible Low-Taxed Income (GILTI) regime that, if left untouched by lawmakers, will have the effect of raising revenue under current law later in the budget window.

Thus, if additional tax cuts or spending increases are 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.

— Alex Brosseau
Tax Policy Group
Deloitte Tax LLP

Copyright © 2022 Deloitte Development LLC
All rights reserved.

This document contains general information only and Deloitte is not, by means of this document, rendering accounting, business, financial, investment, legal, tax, or other professional advice or services. This document is not a substitute for such professional advice or services, nor should it be used as a basis for any decision or action that may affect your business. Before making any decision or taking any action that may affect your business, you should consult a qualified professional advisor. Deloitte shall not be responsible for any loss sustained by any person who relies on this document.

About Deloitte
Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited ("DTTL"), its global network of member firms, and their related entities (collectively, the "Deloitte organization"). DTTL (also referred to as "Deloitte Global") and each of its member firms and related entities are legally separate and independent entities, which cannot obligate or bind each other in respect of third parties. DTTL and each DTTL member firm and related entity is liable only for its own acts and omissions, and not those of each other. DTTL does not provide services to clients. Please see www.deloitte.com/about to learn more.

Copyright © 2022 Deloitte Development LLC
All rights reserved.