Statement of
Sally A. Ferris
Assistant to the Director
Congressional Budget Office

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Mr. Congressman, it is my pleasure to appear here today to discuss the economic and budget outlook. My statement covers several points--the outlook for the economy, the problem of large and growing budget deficits, and the budget proposals put forth by the Administration and by the House of Representatives. This statement will draw upon material presented in the Congressional Budget Office's annual report to the Budget Committees, as well as the CBO analysis of the President's 1984 budget request. 1/

THE CBO ECONOMIC FORECAST AND PROJECTION

During the last several years, the U.S. economy has followed an irregular course, with several periods of decline and recovery. But essentially the economy has not grown since 1979. When the current recession began in the summer of 1981, the economy had not fully recovered from the brief but deep 1980 recession, and by last December, it was operating much further below capacity than at any time since the Depression.

This recession has been the deepest and longest of the post-World War II period. Unemployment was close to 11 percent by the fourth quarter of 1982 and remained over 10 percent during the first quarter of 1983,

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1/ See Congressional Budget Office, Annual Report to the Senate and House Committees on the Budget, The Outlook for Economic Recovery--Part 1, Baseline Budget Projections for Fiscal Years 1984-1988--Part II, and Reducing the Deficit: Spending and Revenue Options--Part III (February 1983), and CBO's Analysis of the President's Budgetary Proposals for Fiscal Year 1984 (February 1983).

with manufacturers using less than 68 percent of capacity. The inflation picture, however, has improved markedly; the combination of record slack in the U.S. economy and a depressed world economy has brought it down to less than 5 percent, well below the double-digit rates seen during the late 1970s and early 1980s.

The economy now seems on the road to recovery. The inventory decline appears to be slowing; auto production is rising; a sharp rise in housing starts portends a pick-up in residential construction; and consumer balance sheets suggest that they are in a position to increase spending. Declining inflation, particularly the fall in petroleum product prices, together with the tax cuts scheduled for next summer will provide a further boost in consumer purchasing power. There are reasons to believe, though, that economic growth will be less vigorous in this recovery than in past recoveries. Interest rates, after adjustment for inflation, still remain at high levels, and business investment is not expected to pick up for some time to come. Exports are also expected to remain weak, largely because of the high value of the dollar.

CBO has made a short-run economic forecast for the next two years. This is summarized in Table 1. Gross national product is seen as rising by 4 percent in real terms between the fourth quarter of 1982 and the fourth quarter of 1983, and by 4.7 percent the next year. Unemployment declines gradually to 9.4 percent by the final quarter of 1984. Inflation is forecast at 4.7 percent (fourth-quarter-to-fourth-quarter) in 1983 and 4.6 percent in 1984 (as measured by the GNP deflator). Short-term interest rates are

TABLE 1. THE CBO SHORT-RUN FORECAST

Economic Variable	1981:4 to 1982:4 Actual	1982:4 to 1983:4 Forecast	1983:4 to 1984:4 Forecast
Nominal GNP (percent change)	3.3	8.9	9.6
Real GNP (percent change)	-1.2	4.0	4.7
GNP Implicit Price Deflator (percent change)	4.6	4.7	4.6
Unemployment Rate a/ (calendar year average)	9.7	10.6	9.8
Three-Month Treasury Bill Rate (calendar year average)	10.6	6.8	7.4

a/ Excludes uniformed military personnel.

projected to average 6.8 percent in 1983, rising slightly as the recovery proceeds. CBO has also made projections for 1985 through 1988 that are summarized in Table 2. CBO economic projections after 1984 are not a forecast but merely assumptions about attainable growth and price behavior.

Because of the uncertainty in the economic outlook, CBO has prepared projections according to two alternative economic paths, both of which can be compared with the base projection (see Table 2). The high-growth path shows a normal cyclical recovery, with more than 5 percent growth during the first three years and 4 percent thereafter. In this scenario, inflation declines more slowly than in the baseline projection, consistent with the lower unemployment path and less slack in the economy generally. The low-growth path, on the other hand, shows a very weak recovery, with

TABLE 2. CBO BASELINE AND ALTERNATIVE ECONOMIC PROJECTIONS (By calendar year)

Economic Variable	1983	1984	1985	1986	1987	1988
			CBO Baseline Projections			
GNP (percent change)	6.8	9.6	9.0	8.1	7.6	7.4
Real GNP (percent change)	2.1	4.7	4.1	3.7	3.5	3.5
GNP Deflator (percent change)	4.6	4.7	4.7	4.3	3.9	3.8
CPI-U (percent change)	4.5	5.0	4.7	4.1	3.9	3.7
Unemployment Rate a/ (percent)	10.6	9.8	9.0	8.4	8.0	7.5
Three-Month Treasury Bill Rate (percent)	6.8	7.4	7.2	6.6	6.1	5.9
			Alternative Projections			
GNP (percent change)						
High-growth path	9.0	11.3	9.5	9.1	8.9	9.1
Low-growth path	5.4	7.9	7.9	7.2	6.6	6.4
Real GNP (percent change)						
High-growth path	4.0	6.0	4.2	4.0	4.0	4.0
Low-growth path	0.8	3.3	3.3	3.2	3.0	3.0
GNP Deflator (percent change)						
High growth path	4.8	4.9	5.1	4.9	4.8	4.9
Low-growth path	4.5	4.4	4.4	3.9	3.5	3.2
CPI-U (percent change)						
High-growth path	4.6	5.3	5.0	4.6	4.6	4.8
Low-growth path	4.5	4.9	4.4	3.8	3.4	3.2
Unemployment Rate a/ (percent)						
High-growth path	9.9	8.5	7.7	7.0	6.4	6.0
Low-growth path	11.2	10.9	10.3	9.8	9.4	9.0
Three-Month Treasury Bill Rate (percent)						
High-growth path	4.4	5.4	5.7	5.0	5.0	4.9
Low-growth path	8.4	9.9	8.9	7.7	7.2	6.3

a/ Excludes uniformed military personnel.

unemployment rates averaging about 10 percent over the 1983-1988 period, but with inflation declining more rapidly than in the baseline projection.

The economic assumptions underlying the Administration's fiscal year 1984 budget request showed the same basic pattern as the CBO projection; the CBO projection being somewhat more optimistic about real growth and inflation during 1983 and 1984, while the Administration assumed slightly higher growth, a faster decline in unemployment, and higher inflation in later years (see Table 3).

THE BUDGET OUTLOOK UNDER CURRENT POLICIES

Although the economy is expected to begin its recovery this year and to move into a period of continued growth, the outlook for the federal budget is not good. Under existing tax laws and spending policies, both CBO and the Administration see large and rising deficits throughout the 1983 to 1988 period. In CBO's baseline projection, deficits climb from $195 billion in 1983 (or almost double the $104 billion target set last year by the Congress in its budget resolution) to $268 billion in 1988. These baseline projections take as their starting point the taxing and spending policies for fiscal year 1983 and show what would happen to the federal budget if those policies were to continue unchanged for the following five fiscal years. The baseline projections assume that the Congress will take action as needed to continue the policies embodied in the current legislation, including the maintenance of real resource levels in the face of inflation.

TABLE 3. COMPARISON OF CBO AND ADMINISTRATION ECONOMIC PROJECTIONS (By calendar year)

	1982	1983	1984	1985	1986	1987	1988	1982:4 to 1983:4 Forecast	1983:4 to 1984:4 Forecast
Real GNP (percent change)									
CBO	-1.8	2.1	4.7	4.1	3.7	3.5	3.5	4.0	4.7
Administration	-1.8	1.4	3.9	4.0	4.0	4.0	4.0	3.1	4.0
GNP Deflator (percent change)									
CBO	6.0	4.6	4.7	4.7	4.3	3.9	3.8	4.7	4.7
Administration	6.0	5.2	5.2	4.9	4.6	4.5	4.4	5.6	5.0
CPI-W (percent change)									
CBO	6.0	3.8	4.6	4.4	4.1	3.9	3.7	3.8	4.5
Administration	6.0	4.9	4.6	4.6	4.6	4.5	4.4	5.0	4.4
Unemployment Rate a/ (percent)									
CBO	9.7	10.6	9.8	9.0	8.4	8.0	7.5	--	--
Administration	9.7	10.9	10.0	9.0	8.2	7.4	6.6	--	--
Three-Month Treasury Bill Rate (percent)									
CBO	10.6	6.8	7.4	7.2	6.6	6.1	5.9	--	--
Administration	10.7	8.0	7.9	7.4	6.8	6.5	6.1	--	--

a/ Excludes uniformed military personnel.

The extremely large deficits projected under CBO's baseline assumptions result primarily from three factors:

- The current slack in the economy, which reduces revenues in fiscal year 1983;
- The large tax cuts enacted in 1981 (under the Economic Recovery Tax Act of 1981--ERTA), which reduce revenue growth over the period; and
- Substantial increases in defense, Social Security, and Medicare and Medicaid spending, and in interest costs.

Federal revenues under current law are projected to be $606 billion in 1983, $12 billion below the amount collected in 1982 and $60 billion below last year's budget resolution target (see Table 4). This decrease lowers the starting point for the 1984-1988 baseline revenue projections.

Revenues are projected in the baseline to resume their growth as the economy recovers, but the projected growth in revenues is slightly lower than the assumed average growth in nominal GNP. The main reason for the decline in revenues relative to GNP over the 1984-1988 projection period is the large tax reductions enacted in 1981 under ERTA, reductions that were only partly offset by the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), as shown in Table 5.

Federal outlays in 1983 are now estimated to total $801 billion, or $31 billion higher than projected by last year's budget resolution. Under CBO's

TABLE 4. CBO BASELINE BUDGET PROJECTIONS
(By fiscal year) a/

	1982 Actual	1983 Base	Projections 1984	1985	1986	1987	1988
			In Billions of Dollars				
Revenues	618	606	654	718	773	827	882
Outlays	728	801	855	928	1,000	1,074	1,150
Deficit	111	195	201	211	227	247	268
			As a Percent of GNP				
Revenues	20.4	19.0	18.7	18.8	18.7	18.5	18.4
Outlays	24.0	25.1	24.4	24.3	24.1	24.1	24.0
Deficit	3.6	6.1	5.7	5.5	5.5	5.5	5.6

a/ Revised to reflect new information provided in the President's 1984 budget.

TABLE 5. REVENUE EFFECTS OF ERTA AND TEFRA
(By fiscal year)

	1983 Base	Projections 1984	1985	1986	1987	1988
		In Billions of Dollars				
Economic Recovery Tax Act of 1981	-88	-135	-167	-205	-236	-267
Tax Equity and Fiscal Responsibility Act of 1982	18	38	42	47	54	56
		As a Percent of GNP				
Economic Recovery Tax Act of 1981	-2.6	-3.9	-4.4	-5.0	-5.3	-5.6
Tax Equity and Fiscal Responsibility Act of 1982	0.6	1.1	1.1	1.1	1.2	1.2

baseline assumptions, unified budget outlays would increase to $855 billion in 1984 and would grow to over $1.1 trillion by 1988. More than 90 percent of this growth is concentrated in just four areas: national defense, Social Security, Medicare and Medicaid, and net interest costs (see Table 6). Relative to GNP, baseline outlays would decline from 25.1 percent in 1983--the highest ratio since World War II--to 24.0 percent in 1988, a ratio still higher than for all postwar years up to 1982.

CBO projections show that, if no changes are made in tax laws and spending policies, the budget deficit would rise to about $200 billion in 1984 and then grow gradually to nearly $270 billion by 1988. These projections of the budget deficit are greatly affected by economic assumptions (as shown in Appendix Table 1 and Figure 1). But even under the "high growth"

Figure 1.
Federal Deficit Under Alternative Economic Assumptions

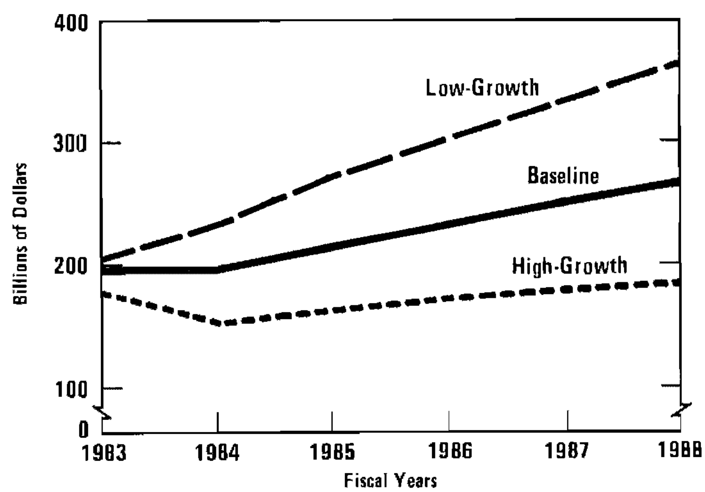


TABLE 6. COMPOSITION AND GROWTH OF FEDERAL OUTLAYS (By fiscal year, in billions of dollars) a/

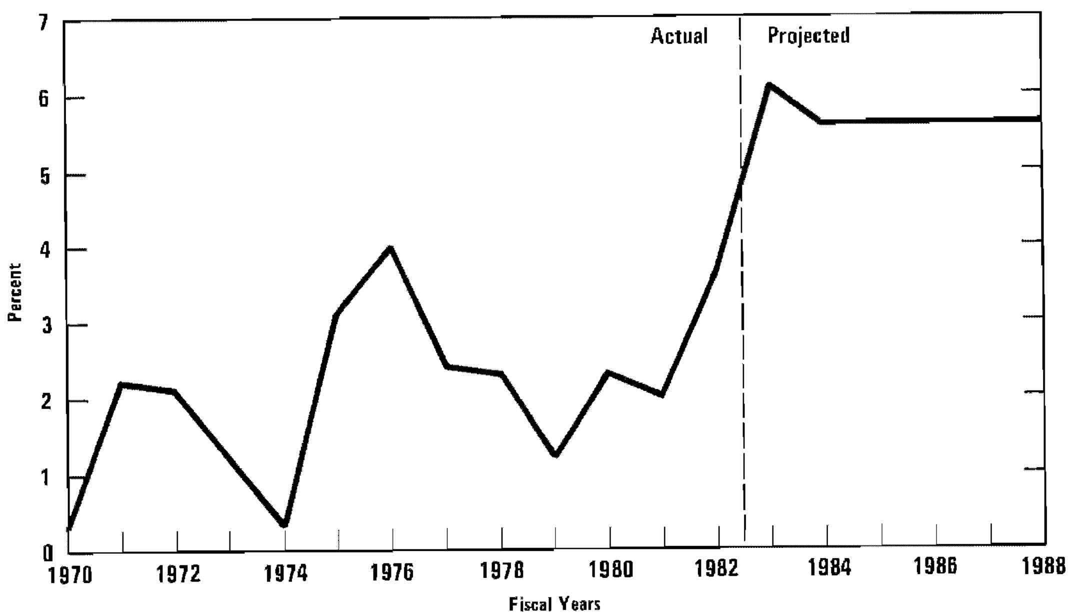
	1983 Base	1988 Projection	Cumulative Five-Year Growth 1984-1988	Distribution of Outlay Growth between 1984-1988 (Percent)
National Defense	214	358	450	45
Entitlements and Other Mandatory Spending				
Social Security Benefits	166	229	182	18
Medicare and Medicaid	76	143	184	18
Other Entitlements	143	145	-34	-3
Subtotal	385	517	333	33
Nondefense Discretionary Spending	145	183	114	11
Net Interest	87	132	136	14
Offsetting Receipts	-31	-40	-30	-3
Total	801	1,150	1,002	100

a/ Revised to reflect new information provided in the President's 1984 budget.

economic path, the budget deficit would remain large throughout the projection period, ranging from $155 billion in 1984 to $183 billion in 1988.

When gauged in relation to a growing gross national product (GNP), the size of these deficits is startling. For 1983 and 1984, CBO projects postwar record deficits amounting to 6.1 and 5.7 percent of GNP respectively (see Figure 2). As noted above, these near-term deficits are, to a great extent, attributable to the economic recession, which has reduced federal revenues and increased federal outlays for unemployment compensation and other income maintenance programs. But even as these cyclical causes wane as economic recovery proceeds, the projected deficits remain at the high level of 5.5 percent of GNP throughout the 1984-1988 period. This indicates a long-term mismatch between federal spending and taxing policies.

Figure 2.
Federal Deficit as a Percentage of GNP



THE CONSEQUENCES OF CURRENT BUDGET POLICY

The prospect of continuing large federal deficits over the longer run poses severe risks to the economy. One possibility is that the Federal Reserve, facing such large deficits, will not be able to maintain an anti-inflationary monetary policy; as a result, inflation may be rekindled. Alternatively, the normal rise in business and consumer demand for credit during the recovery may collide with large federal credit demands to finance the persistent deficits. In a deep recession, the growth of federal debt is usually funded in the capital markets from savings that have no other outlet because business, consumer credit, and mortgage demands are at a low level. But as the economy recovers, private demands for credit will increase, leading to competition for funds between federal and private borrowers. Since total credit in the economy tends to remain at a fairly steady percentage of GNP, any increase in the ratio of federal debt to GNP threatens to "crowd out" other credit claimants. Intense competition for loanable funds might drive up real interest rates and increase the risk of aborting economic recovery. And even if the recovery proceeded, high interest rates would discourage investment. A low-investment economy in turn reduces the chances for productivity growth. Failure to modernize equipment prevents our industries from remaining competitive. In the long run, advances in the nation's standard of living rely on the productivity growth and maintenance of trade that deficits jeopardize.

NARROWING BUDGET DEFICITS

It is now generally agreed that a balanced federal budget is not an attainable goal in the near term. Much federal expenditure for the near term is fixed either by contract or by tacit commitment. Changing those expenditures would not only be disruptive; in many instances, it would raise, rather than lower federal costs. Moreover, substantial cutbacks in spending or increases in taxes undertaken to reduce near term deficits (that is, during fiscal years 1983 or 1984) might delay or weaken the economic recovery. Substantial reductions in the deficit over the entire projection period 1984-1988 are needed, however, if a balanced recovery is to be sustained and the low-investment scenario avoided. This points to the need for a multiyear plan that would ensure an orderly reduction in outyear deficits and less uncertainty about future fiscal policy. Before such a plan is embarked on, however, two broad policy choices have to be resolved.

The first choice is to settle on a budget deficit target for, say, 1988. Most of the responsible debate has centered on a range of target deficits by 1988 of between 1 percent and 3 percent of GNP. The Administration is calling for a deficit target of 2.6 percent of GNP by 1988 (under its economic assumptions).

The second choice is whether the emphasis should be on spending cuts or tax increases. Obviously, neither of these routes will be easy.

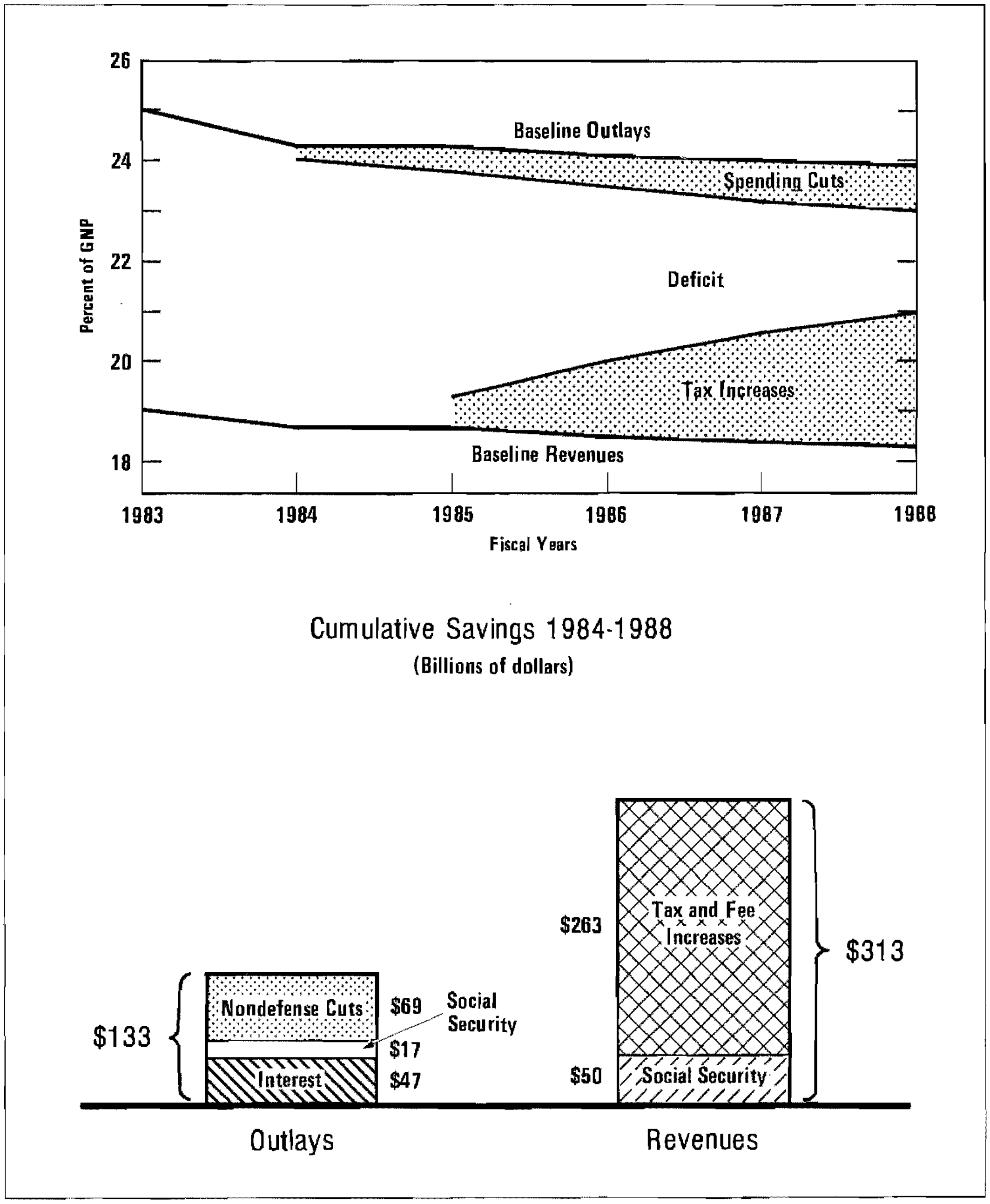
ILLUSTRATIVE MULTIYEAR DEFICIT REDUCTION PLANS

A simple way to grasp the dimensions of the budget problem is as follows: Suppose the budget deficit target for 1988 were set at 2 percent of GNP. This would require that the 1988 deficit be held at $100 billion, about $170 billion below currently projected levels. Finding $170 billion in deficit-reducing measures by 1988 would not be easy, however. The annual rate of the domestic budget cuts in the first year of the Reagan Administration was about $40 billion, and the hard-fought tax increases of the second year realized an average annual gain of about $33 billion. Achieving an even more ambitious deficit reduction goal would require consideration of all parts of the budget and tax base.

To indicate the magnitudes involved in the choices that currently face the Congress, the CBO has developed three illustrative budgetary plans designed to reduce the deficit gradually to 2 percent of GNP, or approximately $100 billion, by 1988. The first plan (included here as Figure 3) emphasizes tax increases (raising the tax burden to 21 percent of GNP by 1988) and holding national defense spending to levels consistent with last year's budget resolution. Such an approach would imply a cumulative five-year increase of more than $300 billion from new tax initiatives. About $50 billion of this would be furnished by enactment of the proposals

Figure 3.

Strategy Example 1—Restore Tax Share to 1981 Level, Maintain Baseline Projection for Defense



advanced by the National Commission on Social Security Reform. 2/Raising the additional revenues would require repeal of major provisions of ERTA, adoption of significant new tax sources, or a truly comprehensive broadening of the income tax base (see Appendix Table 2). On the other hand, this illustration would only require about $70 billion in nondefense spending cuts (over and above the Social Security commission's proposals and the debt service savings made possible from lower deficits) over five years, which is well within the bounds of recent experience. (Appendix Table 3 lists some options.)

Alternatively, if revenues were allowed only to creep back to the current level of 19 percent of GNP, the need for spending reductions would be extreme (see Figure 4). More than $300 billion in program cuts would be needed over the 1984-1988 period (beyond Social Security reform and interest savings). Curbing defense growth sharply--by holding budget authority for national defense to zero real growth--could furnish almost half of the needed deficit reduction; but that would still leave $150 billion to be recovered in nondefense cuts. Even if all cost-of-living adjustments in Social Security benefits were held to 2 percentage points below inflation, and if all nondefense discretionary programs were frozen at current levels

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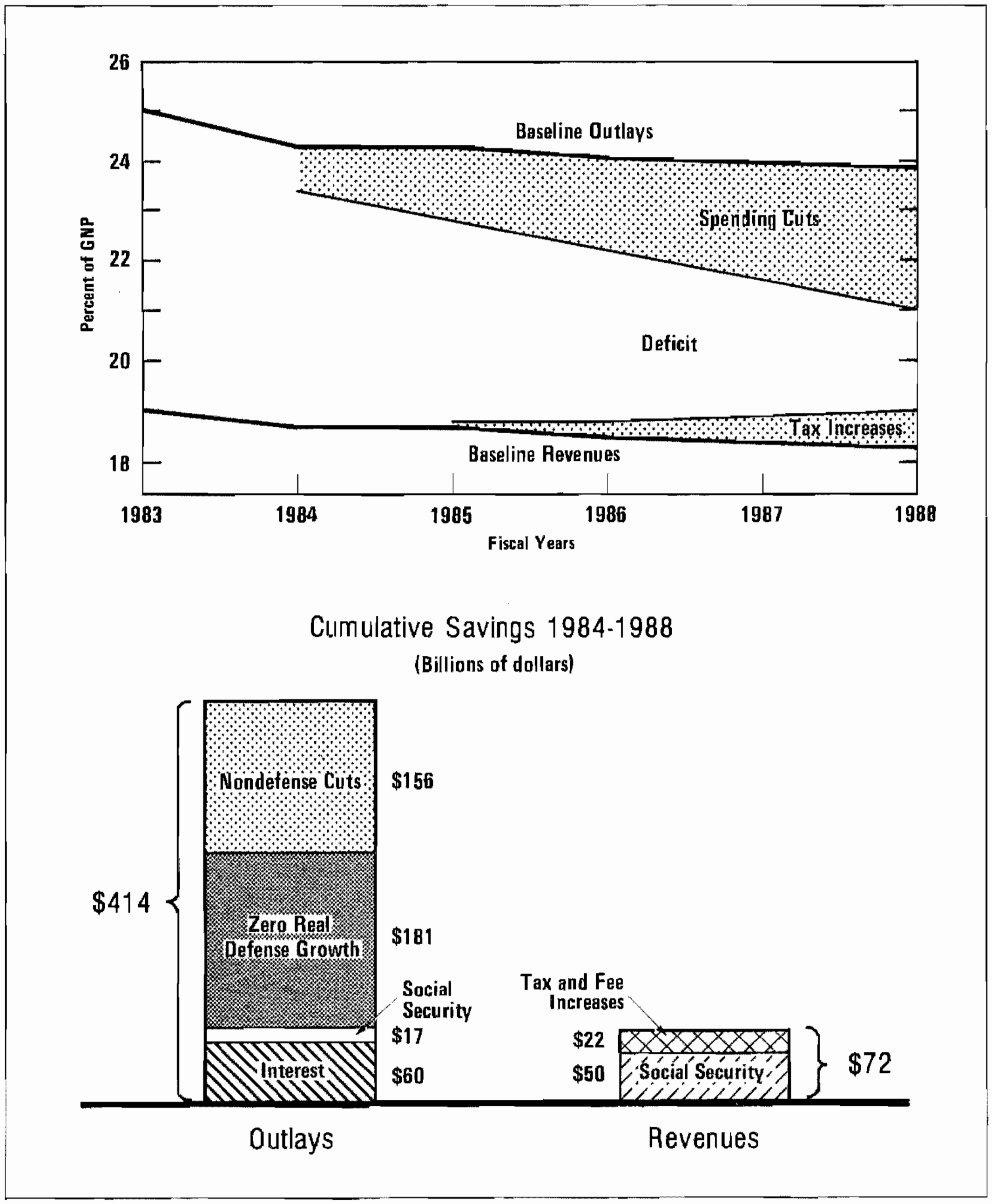
2/ CBO's estimate of the revenue increases from enactment of the Social Security commission's proposals has been revised downward since the publication of Part III of the annual report--from an increase of $57 billion to an increase of $50 billion. This adjustment has been made in the figures depicting the three illustrative budgetary plans. However, other revised CBO estimates--for example, for the baseline outlays and revenues--are not reflected in the figures.

Figure 4.

Strategy Example 2—Freeze Tax Share at 1983 Level, Cut Government Spending



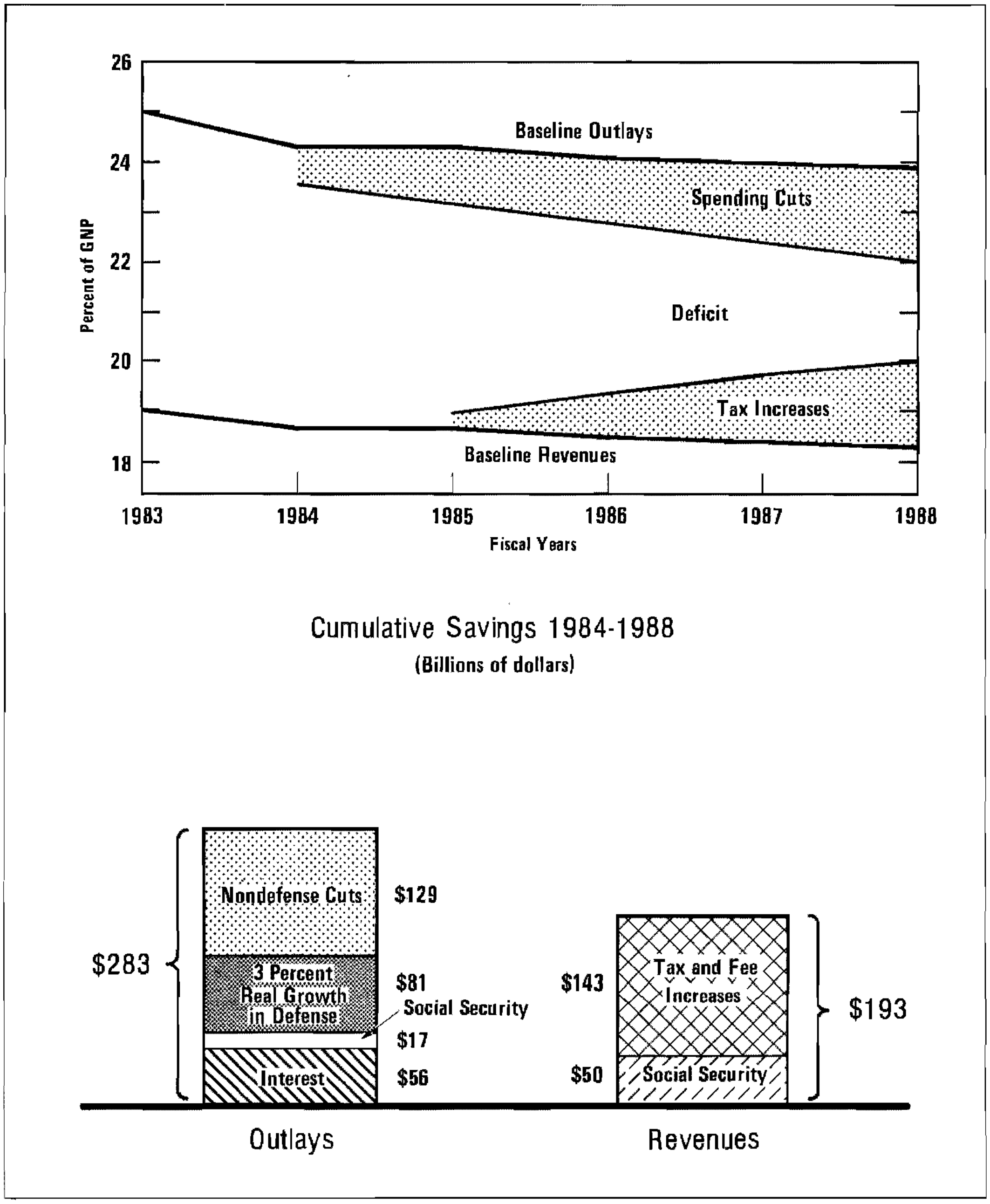
(both measures assumed effective for five years), the cumulative savings would fall far short of the mark (see Appendix Table 3). Such draconian cuts in domestic programs and reversals of defense growth are unlikely to gain broad support.

A reasonable conclusion to draw from these illustrations is that a deficit reduction plan will have to take both roads: it will have to raise taxes significantly and it will have to make major spending cuts. In one such plan (illustrated in Figure 5) taxes are gradually raised to the intermediate level of 20 percent of GNP, and spending is brought down to 22 percent of GNP in 1988. In this alternative, significant tax and spending legislation would be needed, but some flexibility of choice would be preserved. For example, on the revenue side, repeal of indexing of the individual income tax and a small assortment of base-broadening options could bring taxes up to the required level (see Appendix Table 2). Several alternative outlay packages that accumulate to about $200 billion in savings (after Social Security and interest savings) could be devised. For example, the figure shows that limiting national defense budget authority growth to 3 percent after inflation would contribute about $80 billion in savings from the 1984-1988 baseline, and several less extreme reductions (in Medicare and other entitlement programs, for example) could supply the rest.

Perhaps the main lesson in these illustrations is that, without a substantial contribution from increased taxes and reduced spending for all major programs, it is very hard to devise a deficit reduction package that is realistic or sensible. These examples represent three quite different

Figure 5.

Strategy Example 3—Raise Tax Share to Intermediate Level, Limit Defense to 3 Percent Real Growth



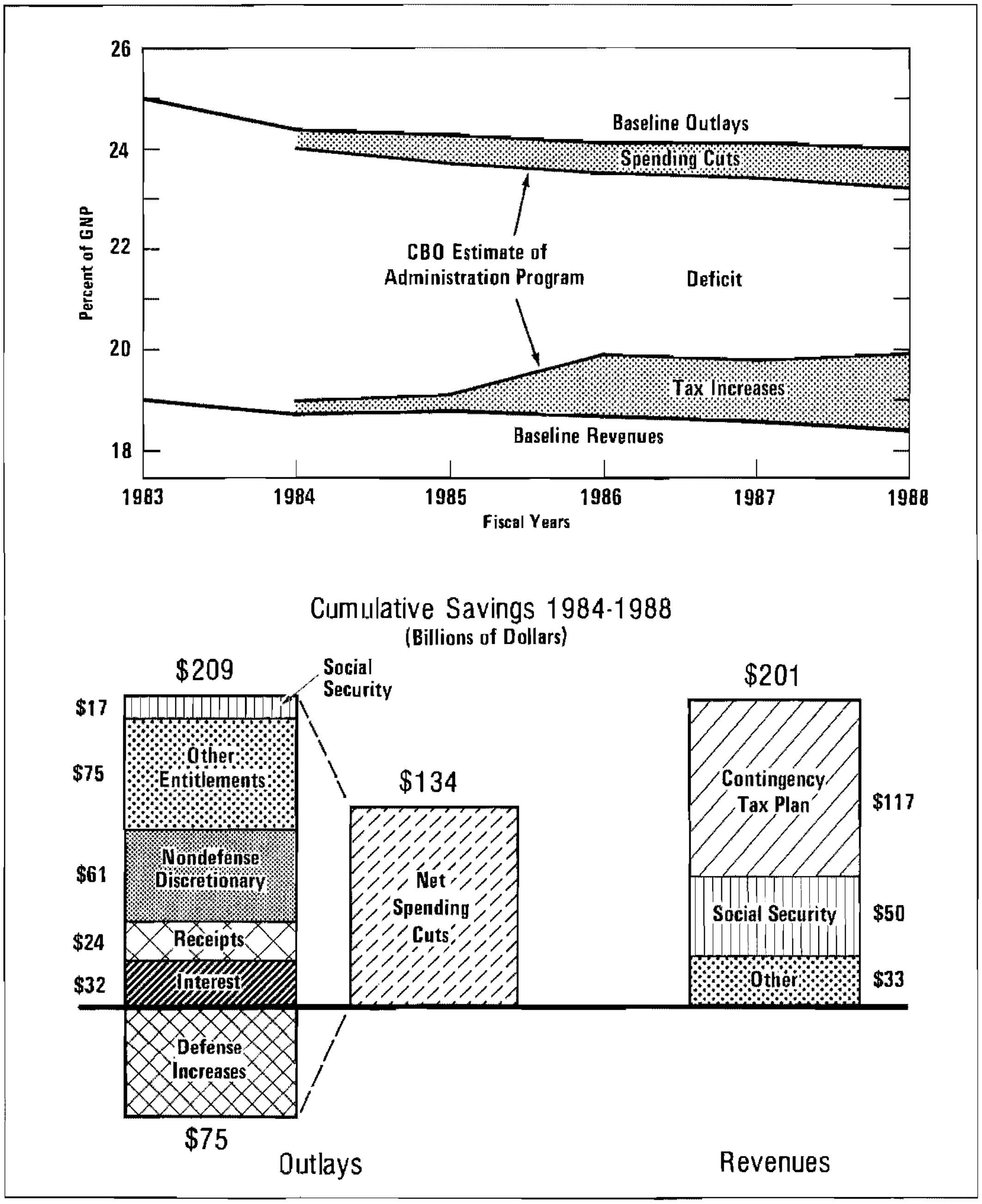
approaches to narrowing the budget deficit under a common deficit goal. Now, let's turn to the deficit reduction proposals advanced by the Administration and by the House of Representatives.

THE ADMINISTRATION'S BUDGET PLAN

The Administration's budget proposal for fiscal year 1984 would narrow the deficit by a somewhat smaller amount than that assumed in the foregoing examples. CBO estimates that the Administration's proposals would reduce the deficit to 3.3 percent of GNP or $158 billion by 1988. The proposal (depicted in Figure 6) includes substantial tax increases, totaling $201 billion over the 1984 to 1988 period (see Table 7), with the tax share estimated by CBO (under our baseline economic assumptions) to rise to 20 percent of GNP in 1988. Most of the new revenue is derived from the contingency tax plan of an income tax surcharge and a petroleum tax.

The net outlay reduction in the Administration's program is at the lower end of the range of alternatives that I have illustrated--about $134 billion over the five year period--but the composition of the proposed spending cuts is quite different. Relative to the CBO baseline projections, the Administration is requesting a substantial increase in defense spending--some $75 billion over the 1984-1988 period. The defense increase simultaneously raises the gross spending reductions needed and restricts such

Figure 6.
Administration's Budget Program



SOURCE: Congressional Budget Office.

TABLE 7. COMPARISON OF DEFICIT REDUCTIONS PROPOSALS ADVANCED BY THE ADMINISTRATION AND THE HOUSE OF REPRESENTATIVES
(In billions of dollars)

	Estimated 1983	Projected 1984	1985	1986	1987	1988	Cumulative 1984 through 1988
CBO Baseline Projections							
Outlays							
Defense	214.2	242.1	277.7	310.0	333.0	358.0	1,520.8
Nondef. Disc.	145.2	154.1	159.9	166.9	175.7	183.3	839.9
Entitlements	385.1	394.4	418.1	448.2	480.5	517.0	2,258.3
Net Interest	87.4	96.0	106.9	114.7	123.6	131.7	572.9
Offs. Receipts	-30.9	-31.7	-34.2	-39.7	-39.1	-40.0	-184.8
Total	801.0	854.8	928.1	1,000.2	1,073.8	1,149.9	5,007.0
Revenues	606.3	653.9	717.8	773.5	827.1	882.4	3,854.7
Deficit	194.6	200.9	210.5	226.7	246.7	267.5	1,152.3
Changes from CBO Baseline Projections							
President's Budget Request Reestimated							
Outlays							
Defense	0	2.6	4.6	11.6	24.6	31.8	75.2
Nondef. Disc.	.3	-6.5	-7.7	-11.0	-16.5	-20.9	-62.6
Entitlements	-.1	-8.7	-14.6	-19.2	-22.7	-25.5	-90.7
Net Interest	0	0	-1.9	-4.9	-9.5	-15.3	-31.6
Offs. Receipts	.1	-1.5	-3.4	-4.7	-6.3	-8.2	-24.1
Total	.3	-14.0	-23.2	-28.1	-30.5	-38.2	-134.0
Revenues	0	10.9	10.6	51.7	56.7	71.2	201.1
Deficit	.4	-24.9	-33.8	-80.0	-87.1	-109.4	-335.2
House Budget Resolution Extrapolated to 1987 and 1988							
Outlays							
Defense	.1	-6.7	-21.4	-25.7	-19.1	-14.7	-87.6
Nondef. Disc.	9.3	11.2	8.2	6.7	3.7	.7	30.5
Entitlements	4.0	4.0	.9	-4.7	-6.8	-8.6	-15.2
Net Interest	.5	.1	-3.5	-9.1	-15.6	-22.9	-51.0
Offs. Receipts	0	.1	.1	.1	.2	.2	.7
Total	13.8	8.8	-15.8	-32.6	-37.6	-46.6	-123.8
Revenues	-.1	35.2	48.1	58.0	74.2	100.0	315.5
Deficit	13.9	-26.4	-63.9	-90.6	-111.8	-146.6	-439.3

reductions to the nondefense portion of the budget. CBO's estimates indicate that, under the Administration's proposal, the cumulative reductions in entitlement programs other than Social Security would come to about $75 billion, and in nondefense discretionary spending to about $61 billion. These cuts represent more than half of all projected spending growth after 1983 in the CBO baseline for these categories.

These estimates are based on CBO's reestimate of the Administration's revenue and spending projections using our own economic assumptions and technical estimating methods. Last year, this process produced a dramatic difference with the Administration's estimates, showing rising instead of declining deficits. This year, we do not have major estimating differences with the Administration (see Table 8). The estimating differences are slight and remain well within the range of estimating error--particularly if the experience of the last several years is any guide.

THE HOUSE BUDGET RESOLUTION

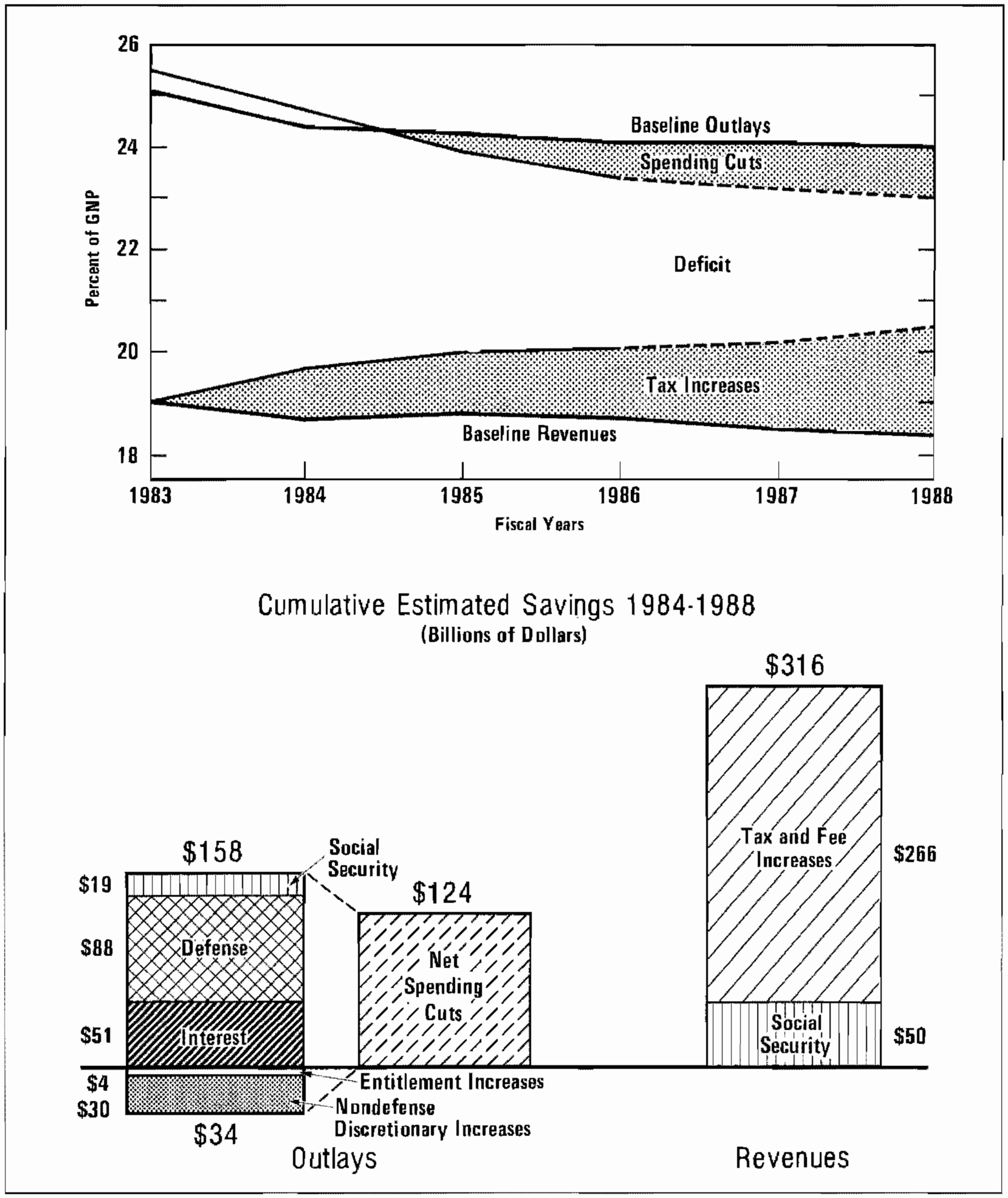
The concurrent budget resolution for fiscal year 1984 passed by the House of Representatives last month sets spending and revenue targets for fiscal years 1984 through 1986. The Congressional Budget Office has extrapolated these targets to fiscal year 1988 in order to facilitate comparison with other budget plans. The resulting spending and revenue path (depicted in Figure 7) would achieve about $104 billion more in deficit

TABLE 8. THE BUDGET OUTLOOK UNDER ADMINISTRATION POLICIES (By fiscal year, in billions of dollars)

	1983	1984	1985	1986	1987	1988
Revenues						
Administration estimate	598	660	724	842	916	1,010
CBO estimate	606	665	728	825	884	954
Outlays						
Administration estimate	805	848	918	990	1,058	1,127
CBO estimate	801	841	905	972	1,043	1,112
Deficit						
Administration estimate	208	189	194	148	142	117
CBO estimate	195	176	177	147	160	158
Differences in Projections						
Revenues						
Economic	*	2	3	-7	-21	-40
Technical	9	3	1	-10	-12	-17
Total	9	5	4	-17	-33	-57
Outlays						
Economic	-2	-9	-9	-11	-12	-14
Technical	-2	1	-4	-6	-3	-1
Total	-4	-8	-13	-18	-15	-15
Deficit						
Economic	-2	-11	-13	-5	9	26
Technical	-11	-2	-5	4	8	16
Total	-13	-13	-17	-1	17	41

* Less than $500 million.

Figure 7.
House Budget Resolution with CBO Extrapolation for 1987 and 1988



SOURCE: Congressional Budget Office.

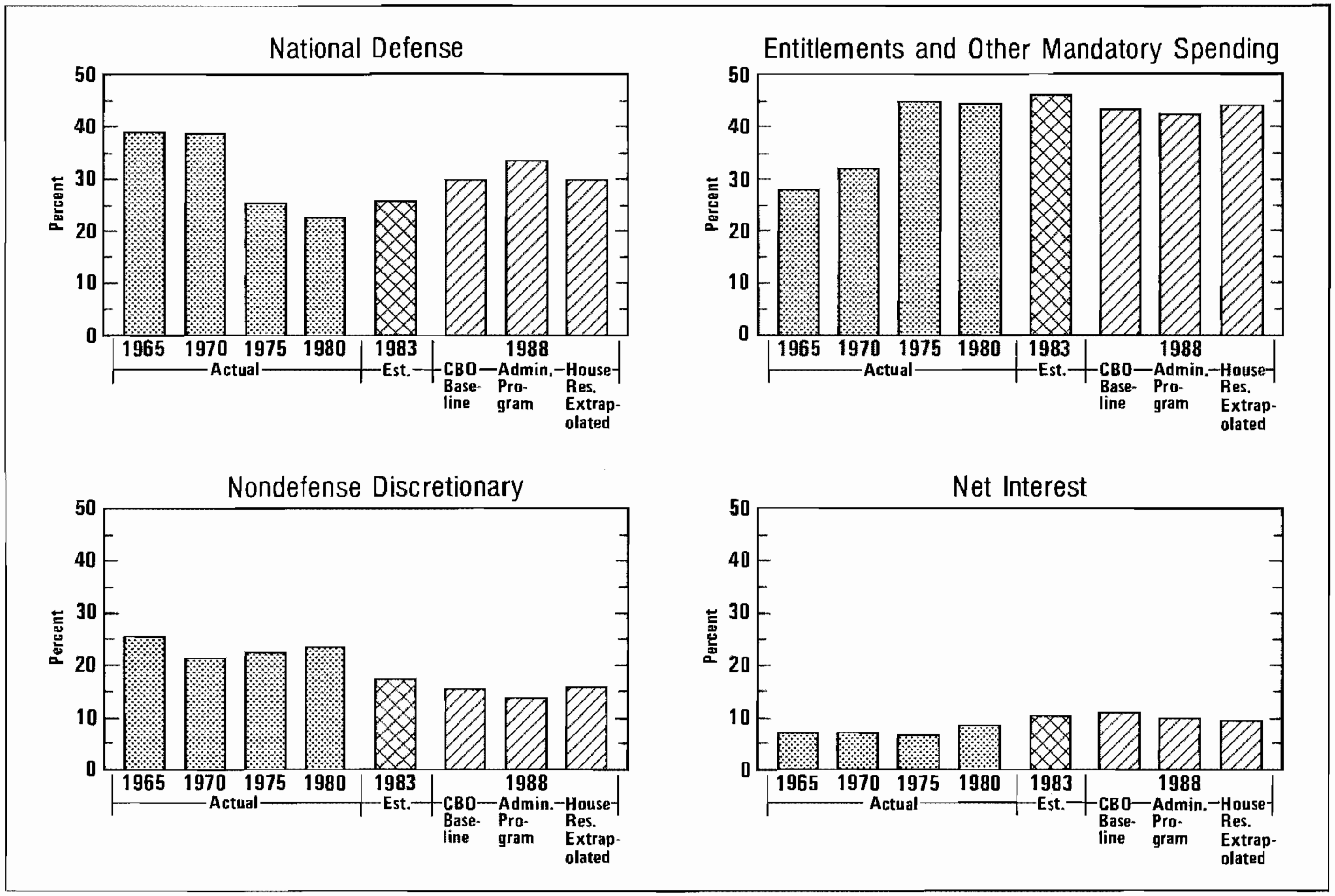
reductions than proposed by the President for the 1984-1988 time period, reducing the deficit to 2.5 percent of GNP or $121 billion by 1988.

The tax increases implicit in the House budget resolution total $316 billion over the 1984-1988 period, bringing revenues to 20.5 percent of GNP by 1988, up from the 1983 level of 19 percent. By comparison, the Administration's plan calls for $201 billion in additional revenues over that period, bringing the tax share to 20 percent of GNP by 1988.

The net outlay reduction implicit in the House Budget Resolution is slightly less than that proposed by the President--about $124 billion over the five-year period compared to the $134 billion level proposed by the President. The composition of the proposed spending in the House Budget Resolution differs substantially from that proposed by the Administration, however. Relative to the CBO baseline projection, the House Budget Resolution extrapolated would increase spending for various programs by $34 billion over the 1984-1988 period--$30 billion for nondefense discretionary programs and $4 billion for entitlement programs (other than Social Security). This increase is counterbalanced by a reduction in defense spending, totaling some $54 billion over the 1984-1986 period, and an estimated $34 billion in 1987 and 1988. Additional spending cuts of about $19 billion are obtained through revisions to the Social Security System. Interest savings resulting from reductions in the deficit total an estimated $50 billion over the 1984-1988 period. Figure 8 illustrates the distribution of spending contained in the House Budget Resolution and the President's proposed budget relative to historical levels.

Figure 8.

Outlay Categories as Percentages of Gross Federal Spending



SOURCE: Congressional Budget Office.

CONCLUSION

In summary, Mr. Congressman, it is now widely agreed that spending cuts and tax increases will be needed to reduce projected budget deficits to acceptable levels as the economy recovers. While prompt action will be needed to achieve desired deficit reductions in the outyears, balancing this consideration against the need to allow sustained recovery will be difficult; some spending cuts and tax increases may have to be put off to permit recovery to regain momentum. An appropriate deficit reduction program thereby requires a multiyear plan--legislated this year--with a balanced mix of tax increases and spending reductions. Many difficult choices confront the Congress, and the country, in devising and implementing such a program.

APPENDIX TABLE 1. BASELINE BUDGET PROJECTIONS UNDER ALTERNATIVE ECONOMIC ASSUMPTIONS, FISCAL YEARS 1983-1988
(In billions of dollars)

	1983 Base	Projections 1984	1985	1986	1987	1988
			In Billions of Dollars			
High-Growth Path						
Revenues	615	676	742	798	862	933
Outlays	793	830	904	971	1,041	1,116
Deficits	178	155	162	172	179	183
Low-Growth Path						
Revenues	599	636	686	730	777	825
Outlays	804	868	958	1,032	1,110	1,187
Deficits	205	232	272	302	333	363
			As a Percent of GNP			
High-Growth Path						
Revenues	19.0	18.7	18.7	18.4	18.3	18.1
Outlays	24.4	23.0	22.8	22.4	22.1	21.7
Deficits	5.5	4.3	4.1	4.0	3.8	3.6
Low-Growth Path						
Revenues	18.9	18.7	18.6	18.5	18.4	18.4
Outlays	25.3	25.5	26.0	26.1	26.3	26.5
Deficits	6.5	6.8	7.4	7.6	7.9	8.1

APPENDIX TABLE 2. MAJOR TAX INCREASE OPTIONS
(By fiscal year, in billions of dollars)

Option	1984	1985	1986	1987	1988	Cumulative Five-Year Increase
Repeal Parts of ERTA						
Repeal July 1, 1983 Rate Reduction	30	33	35	38	40	177
Cap Third-Year Tax Rate Cut at $700	6	7	7	8	9	37
Repeal Indexing	--	6	17	28	40	90
Initiate New Tax Sources						
10 Percent Value-Added Tax			150 - 200 per year			
Energy Tax			10 - 20 per year			
Possible Base-Broadening Options a/						
Tax Some Employer-Paid Health Insurance	3	5	6	7	9	30
Eliminate Deductibility of State and Local Sales Taxes	1	6	6	7	8	28
Limit Nonbusiness, Non-Investment Interest Deductions to $10,000	1	2	2	2	2	9
Lengthen Building Depreciation Period to 20 Years	b/	2	4	6	8	19
Require Full Basis Adjustment for the Investment Tax Credit	b/	1	2	4	5	12
Tax Nonstatutory Fringe Benefits	1	1	1	2	2	6
Freeze Estate and Gift Tax Credit at Exemption Equivalent of $275,000	--	1	1	2	3	6
Social Security Commission Proposal	8	5	8	9	20	50

SOURCE: Congressional Budget Office, Reducing the Federal Deficit: Spending and Revenue Options (February 1983).

a/ Assumes January 1, 1984, effective dates.

b/ Less than $0.5 billion.

APPENDIX TABLE 3. MAJOR OUTLAY REDUCTION OPTIONS
(By fiscal year, in billions of dollars)

Option	1984	1985	1986	1987	1988	Cumulative Five-Year Savings
National Defense						
3 percent real growth	4	16	23	19	19	81
5 percent real growth	2	10	12	2	-6	20
Social Security						
Reform commission	2.9	3.1	3.5	3.7	4.0	18.6
Cap COLA at CPI growth less 2 percentage points	4.2	7.8	11.5	15.3	19.1	57.9
Medicare						
Expand hospital coinsurance days 2-30	2.0	3.0	3.4	3.8	4.3	16.5
Move to prospective hospital reimbursement	--	--	2.1	4.1	4.6	10.9
Increase SMI premiums	0.9	1.1	1.7	2.5	3.4	9.6
Entitlements						
Eliminate all COLAs (including Social Security)	11	23	34	46	58	172
Nondefense Discretionary						
Limit increase to 2 percent nominal per year	0.8	2.4	4.2	6.2	8.3	21.9
Freeze program funding at 1983 levels	2.1	6.0	10.6	15.6	20.7	55.0

SOURCE: Congressional Budget Office, Reducing the Federal Deficit: Spending and Revenue Options (February 1983).