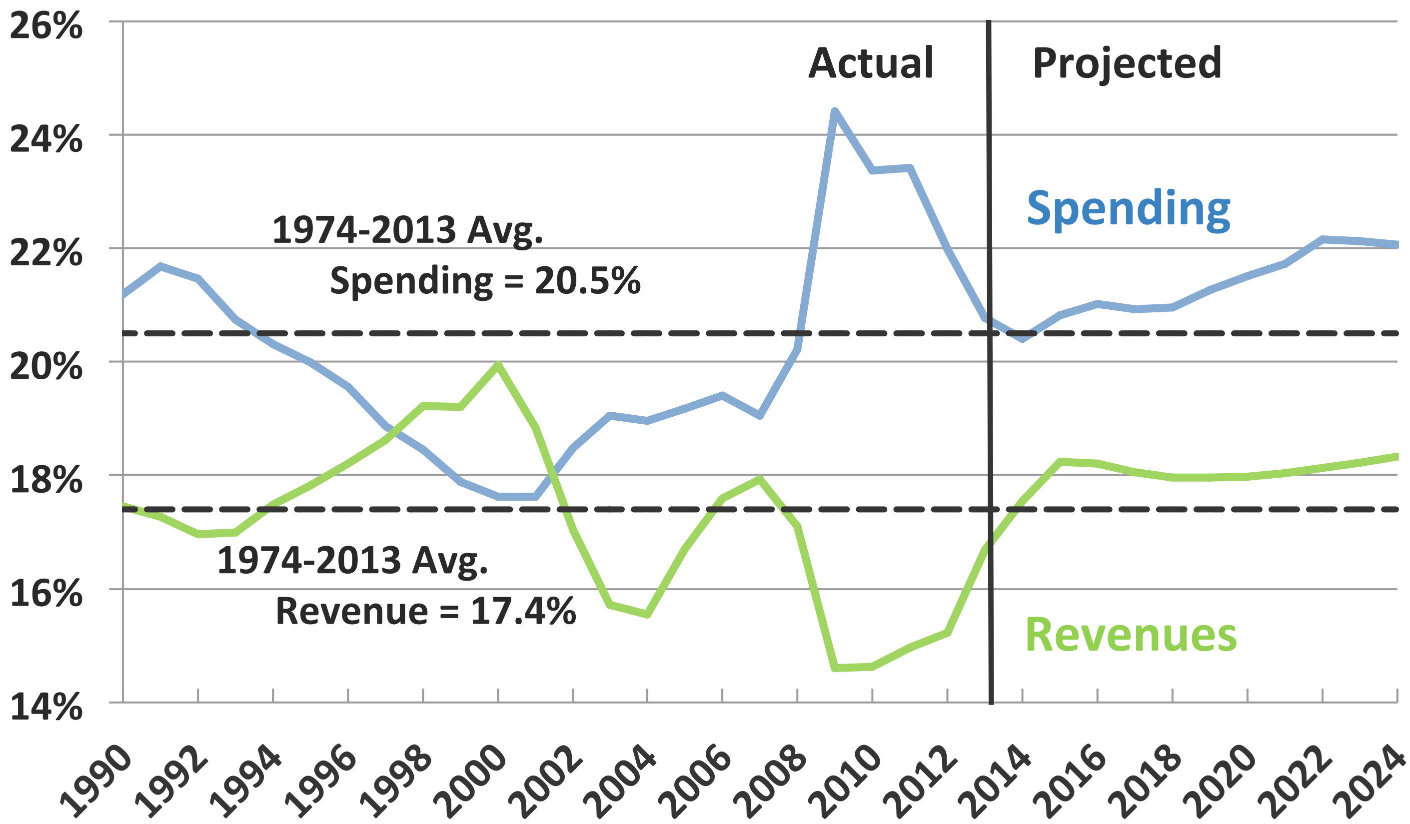
Debt Problems Are Still Far from Solved

- **Part I: The Current Outlook**
- Part II: How We Got Here
- Part III: Effects of Fiscal Imbalance
- Part IV: Federal Spending and Revenues
- Part V: The Current Debate
- Part VI: The Opportunities Ahead

Gap Between Revenue and Spending

(Percent of GDP)



Note: Projections based on CBO current law.

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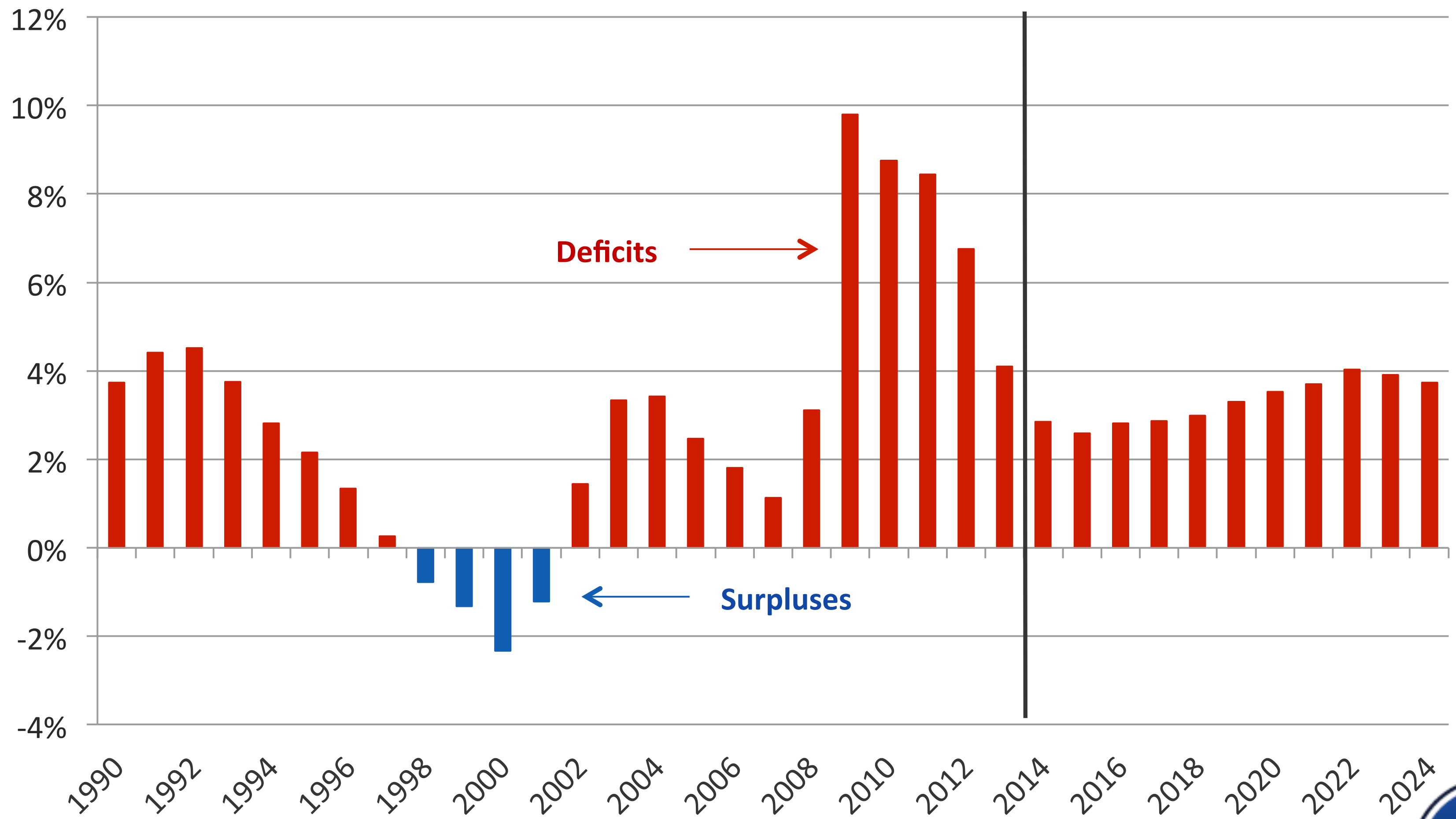
Deficit Projections

(Percent of GDP)



Note: Estimates based on CBO current law.

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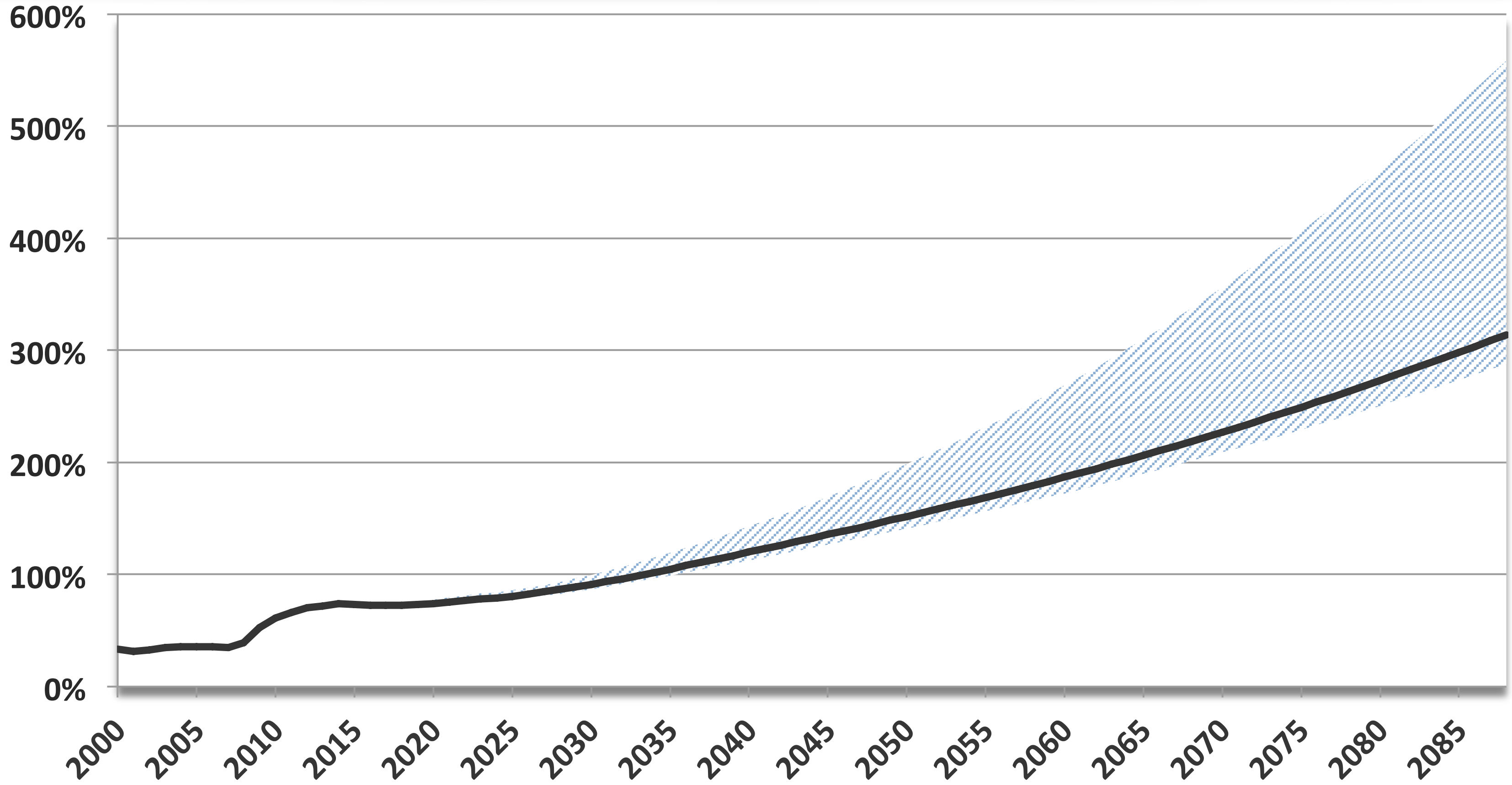
Debt Projected to Rise to Historic Levels

(Percent of GDP)



Source: CRFB calculations based on CBO data.

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Projections Tell Two Stories: Long and Short

- Deficits will decline in the short term, continuing to fall from 8.8 percent in 2010 to 4.1 percent in 2013 to a low of 2.6 percent in 2015.
  - *Due to both a recovering economy and deficit reduction efforts.*
  - *Debt will fall to 72 percent of GDP by 2017, but still nearly twice its historical average.*

- After 2017, debt as a percentage of GDP will start to rise indefinitely.
  - *A combination of population aging, rising health care costs, an ineffective tax code, and rising interest costs will put debt on a clear upward path.*
  - *Debt will rise to the size of the economy by 2034, twice the size of the economy by 2064, and three times the size of the economy by 2086.*

- Without significant changes, debt will remain on this upward path, even with faster economic growth or a moderate improvement in health care cost growth.

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- **Part II: How We Got Here**
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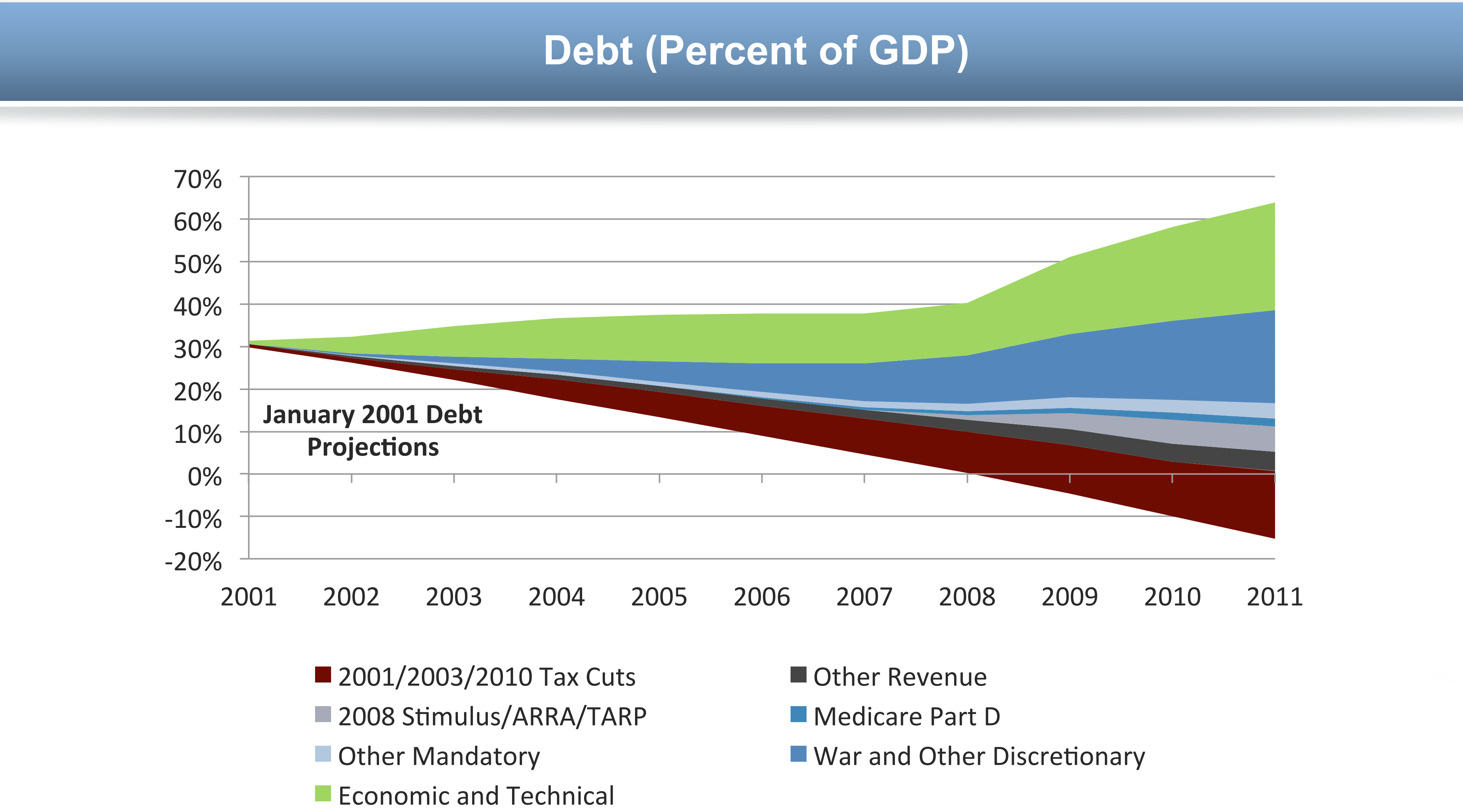
Debt Drivers

Short-Term	Long-Term
Economic Crisis (lost revenue and increased spending on safety net programs like Food Stamps)	**Rapid Health Care Cost Growth** (causing Medicare and Medicaid costs to rise)
Economic Response (stimulus spending/tax breaks and financial sector rescue policies)	**Population Aging** (causing Social Security and Medicare costs to rise, and revenues to fall)
Tax Cuts (in 2001, 2003, 2010, and 2013)	**Growing Interest Costs** (from continued debt accumulation)
War Spending (in Iraq and Afghanistan)	**Insufficient Revenue** (to meet the costs of funding government)

Changes Since 2001



Note: Estimates from CBO.

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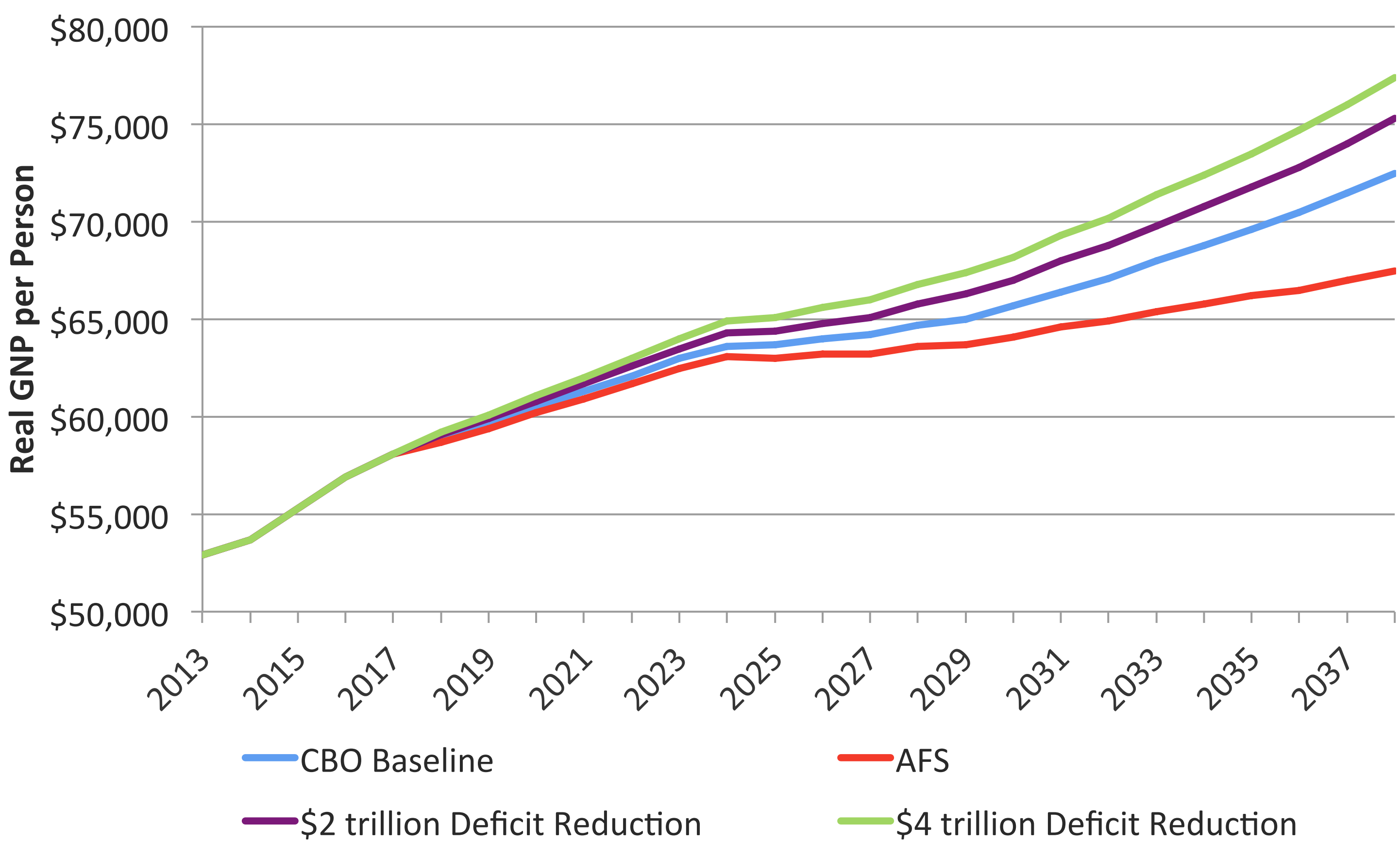
Consequences of Debt

- **Increased Cost of Living.** More debt will mean higher interest rates on everything from credit card debt to car loans to mortgages.
- **Slower Wage Growth.** Government debt will crowd out productive investments, leading to slower economic growth and lower wages.
- **Increased Interest Rate Risk.** Today's historically low interest rates will rise as the economy recovers, increasing interest costs, but high levels of debt may cause interest rates to increase further, worsening the problem.
- **Less Budgetary Flexibility.** Lawmakers have less fiscal space to work with high levels of debt, giving them less flexibility to react to unforeseen crises like national disasters, economic downturns, or national security threats.
- **Generational Injustice.** By not taking responsibility for the debt now, we put a larger burden – be it spending cuts, tax increases, or a combination – on future generations that will threaten their standard of living.
- **Eventual Fiscal Crisis.** If we do not act now on our own terms, we face a higher risk of a financial crisis brought on by our debt down the road.

The Effect of Higher Debt on Wages

Stronger Wage Growth with Lower Debt



Note: Estimates from CBO Long-Term Outlook.

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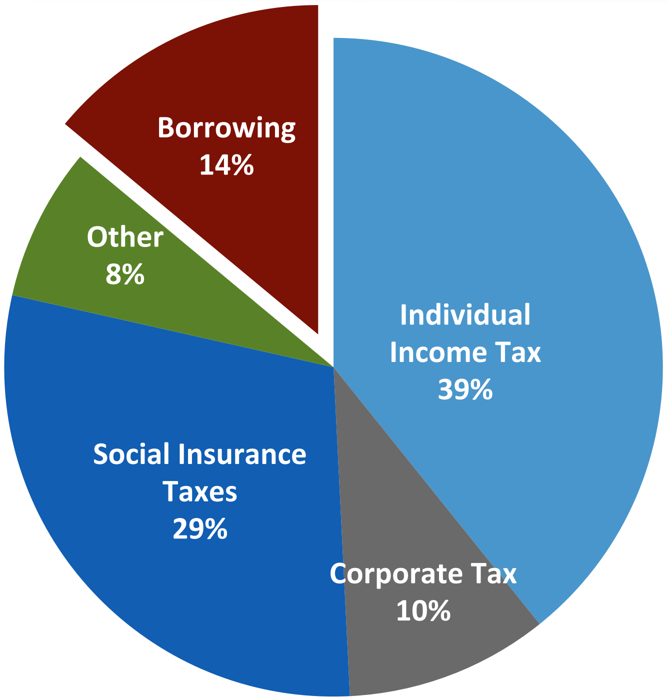
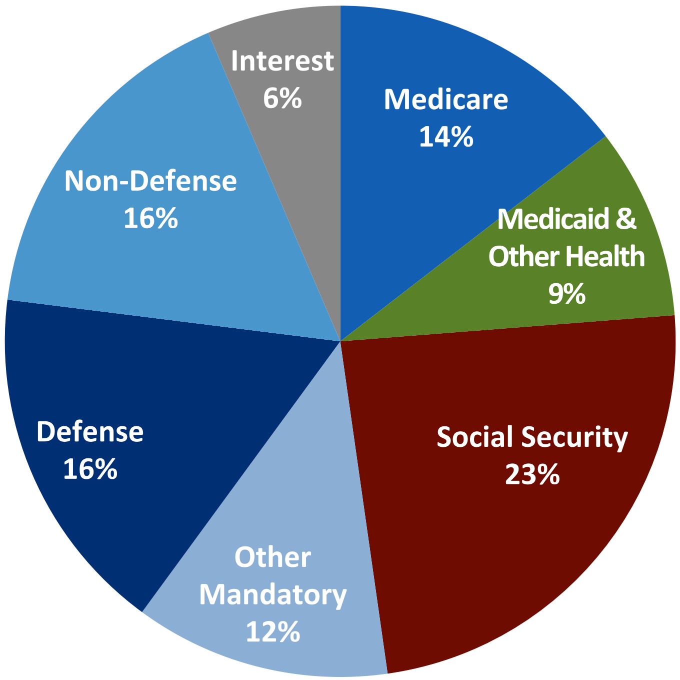
Revenue and Spending in the Federal Budget

Revenues and Financing	Outlays



2014



Total Revenues = $3.0 Trillion
Total Revenues and Borrowing = $3.5 Trillion

Total Outlays = $3.5 Trillion

Source: CBO Budget and Economic Outlook

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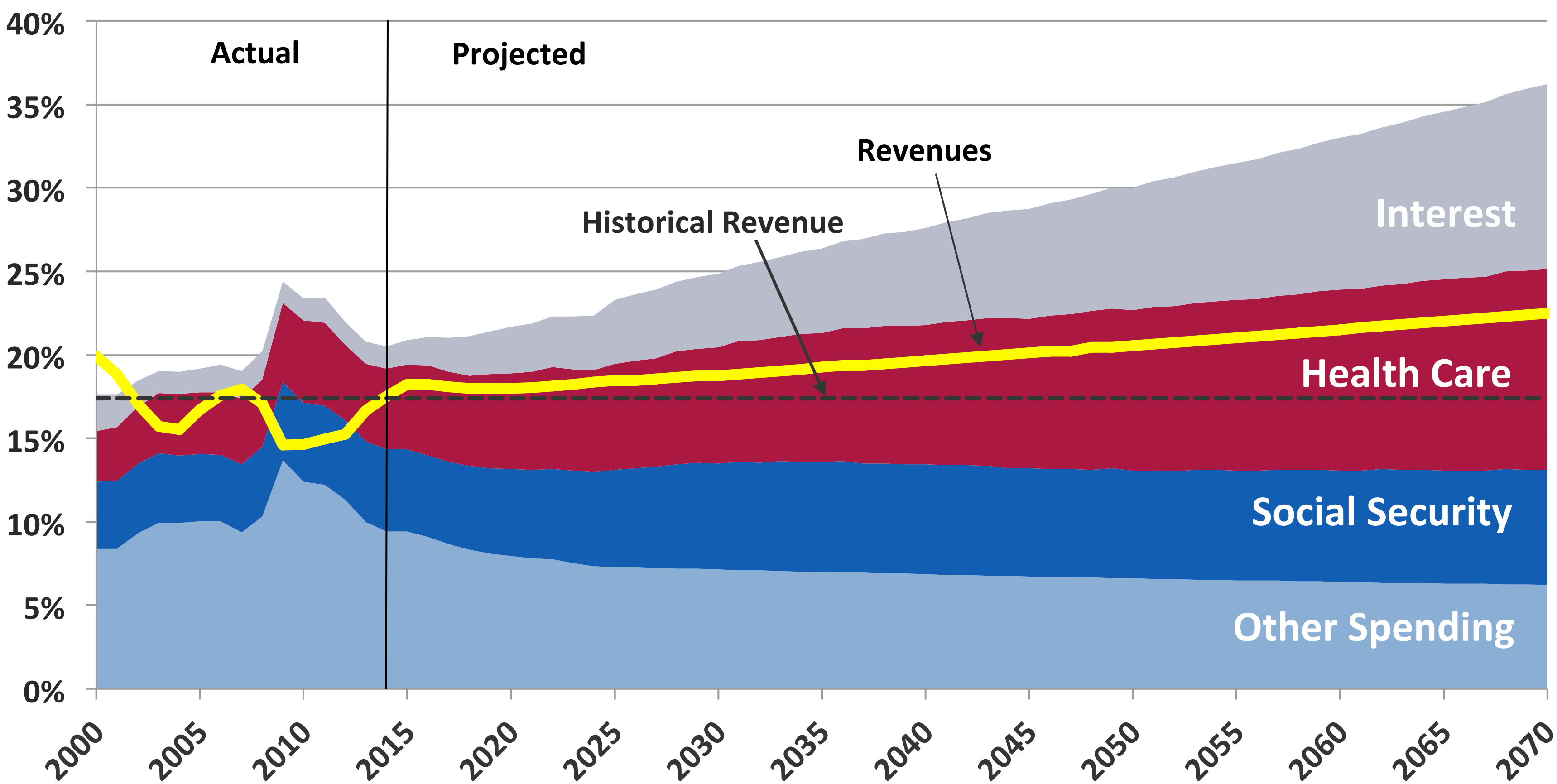
Growth of Spending Will Outpace Revenues

Federal Spending and Revenues (Percent of GDP)



Note: Estimates based on CBO current law baseline.

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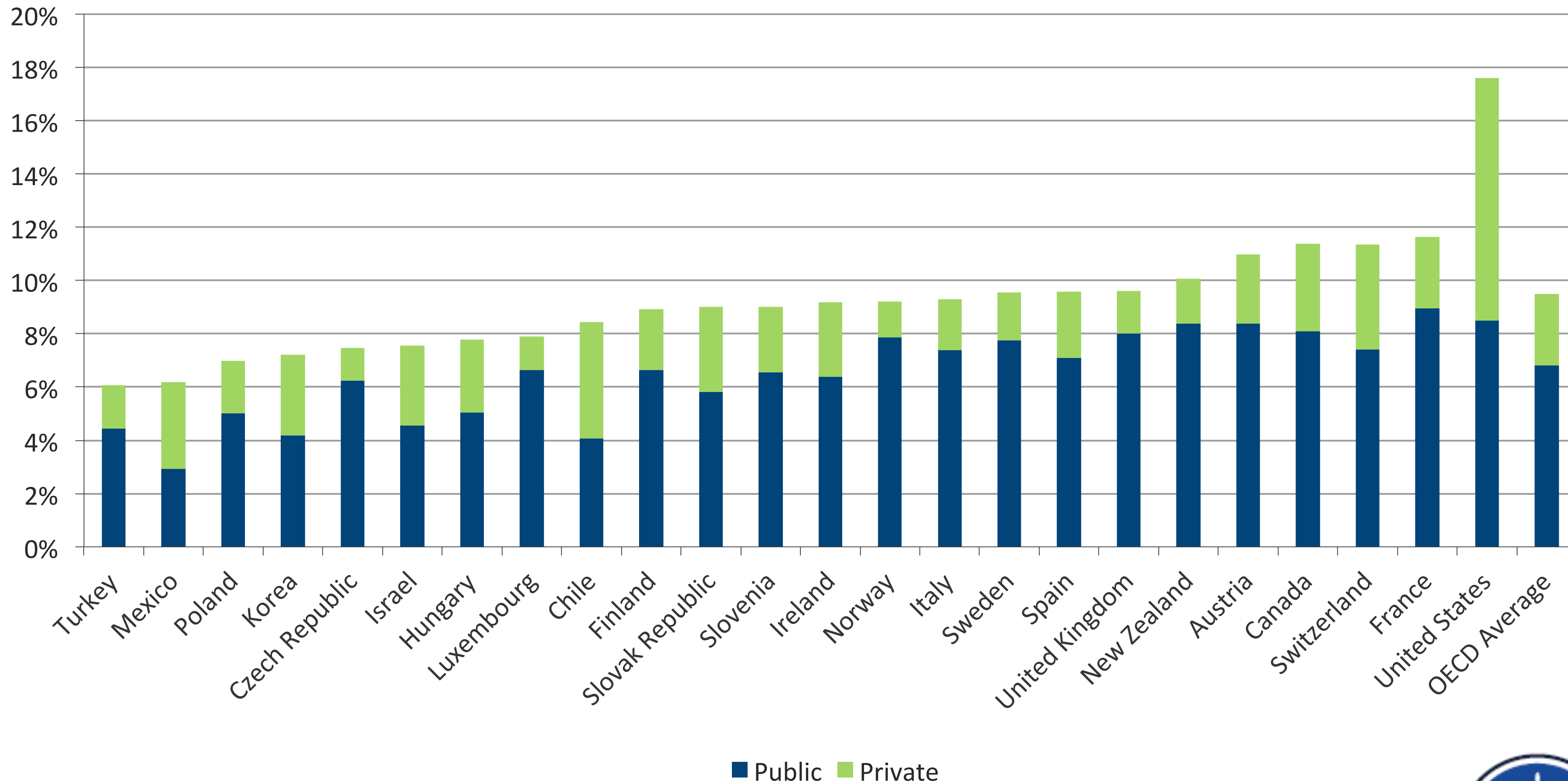
Why is Federal Health Care Spending Increasing?

- **The Population Is Aging** due to increased life expectancy and retirement of the baby boom generation, adding more beneficiaries to Medicare and Medicaid
- **Per Beneficiary Costs Are Growing** faster than the economy in both the public and private sector. Causes of this excess cost growth include:
  - **Americans Are Unhealthy** when compared to populations in similar economies
  - **Americans Are Wealthy and Willing to Pay More**
  - **Fragmentation and Complexity** among insurers, providers, and consumers make normal market competition difficult
  - **Incentives Are Backwards** by hiding true costs of care through insurance and by hiding costs of insurance enrollment through employer sponsorship, incentivizing overspending

Health Care Spending By Country

Percent of GDP (2011)



Source: 2013 Data from the Organization for Economic Cooperation and Development.

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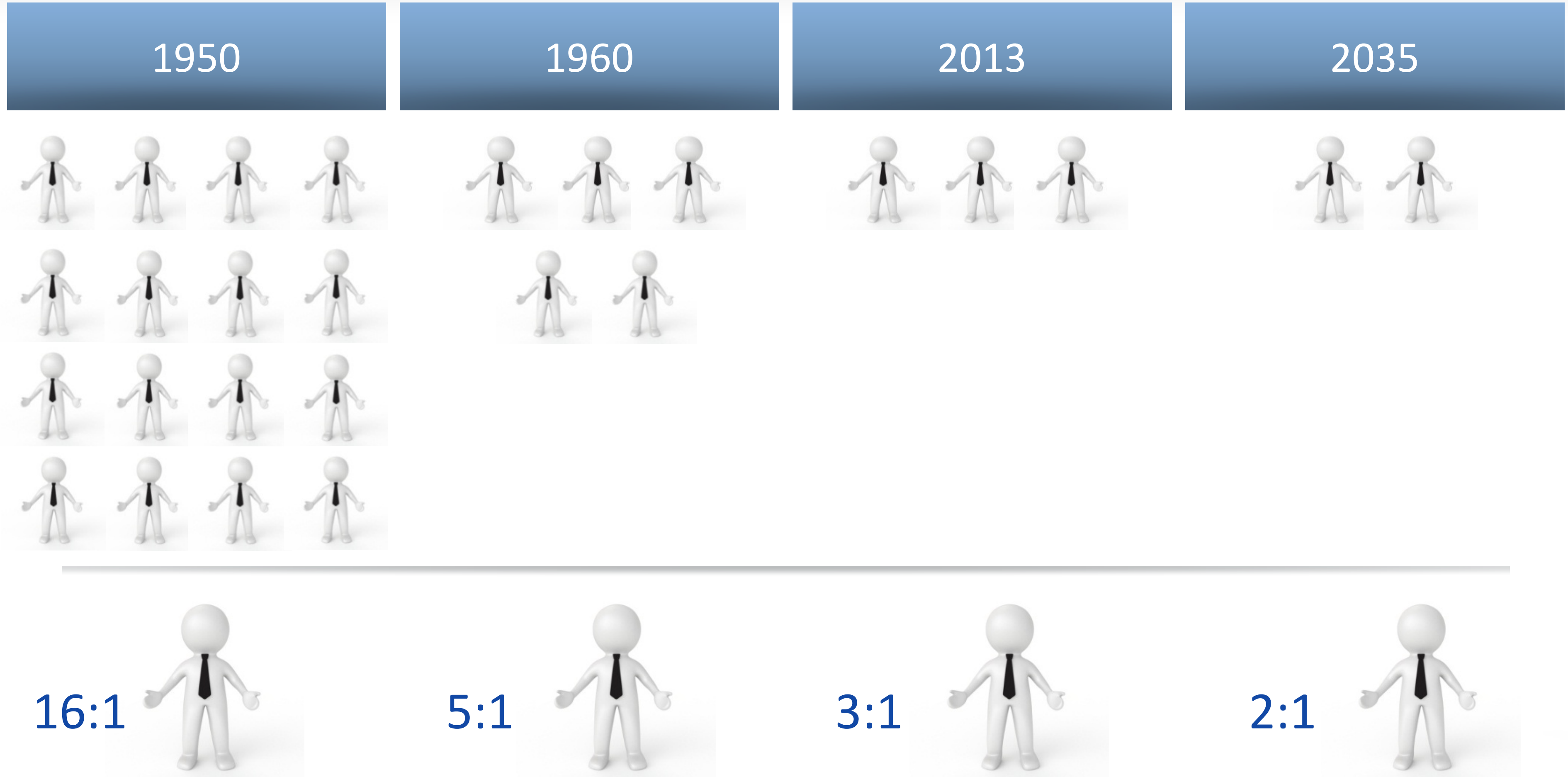
Number of Workers for Every Social Security Retiree is Falling



Source: 2013 Social Security Trustees Report.

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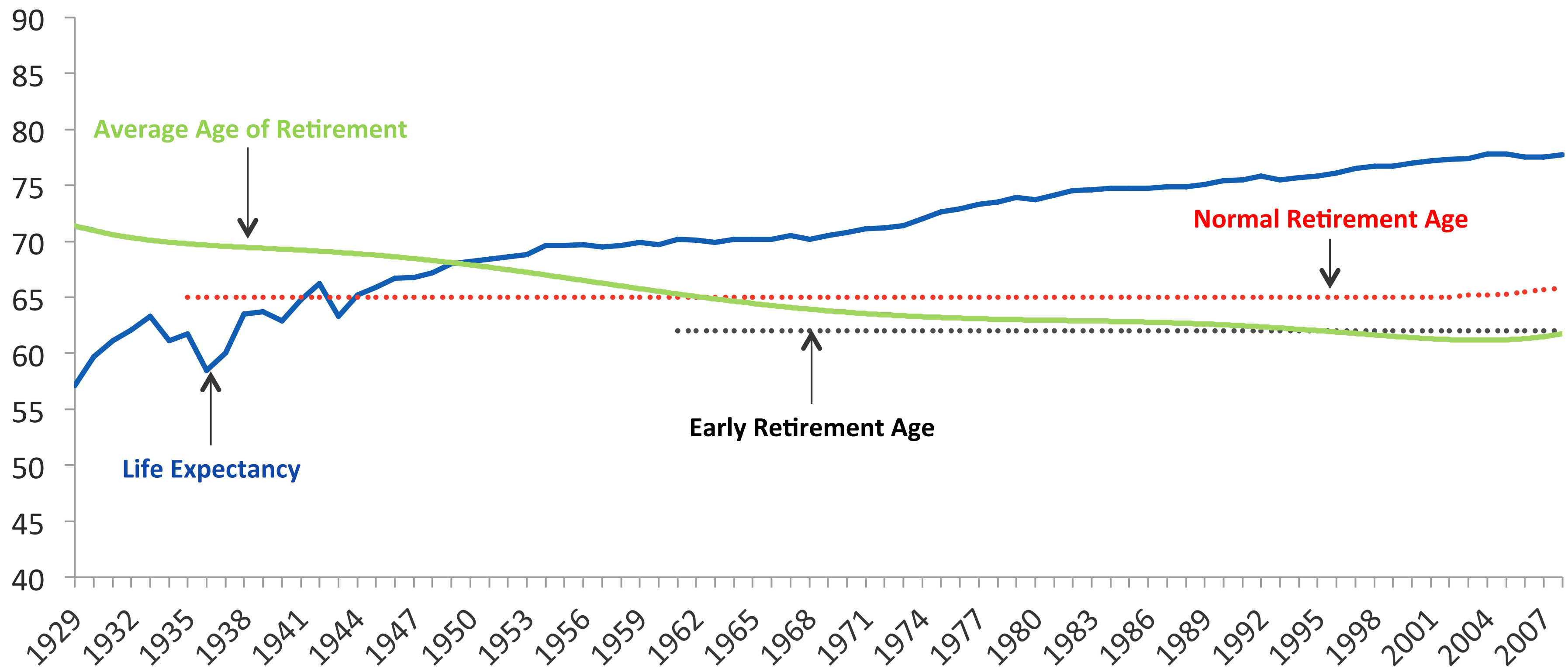
Living Longer, Retiring Earlier



Source: Social Security Administration and U.S. Census Bureau.

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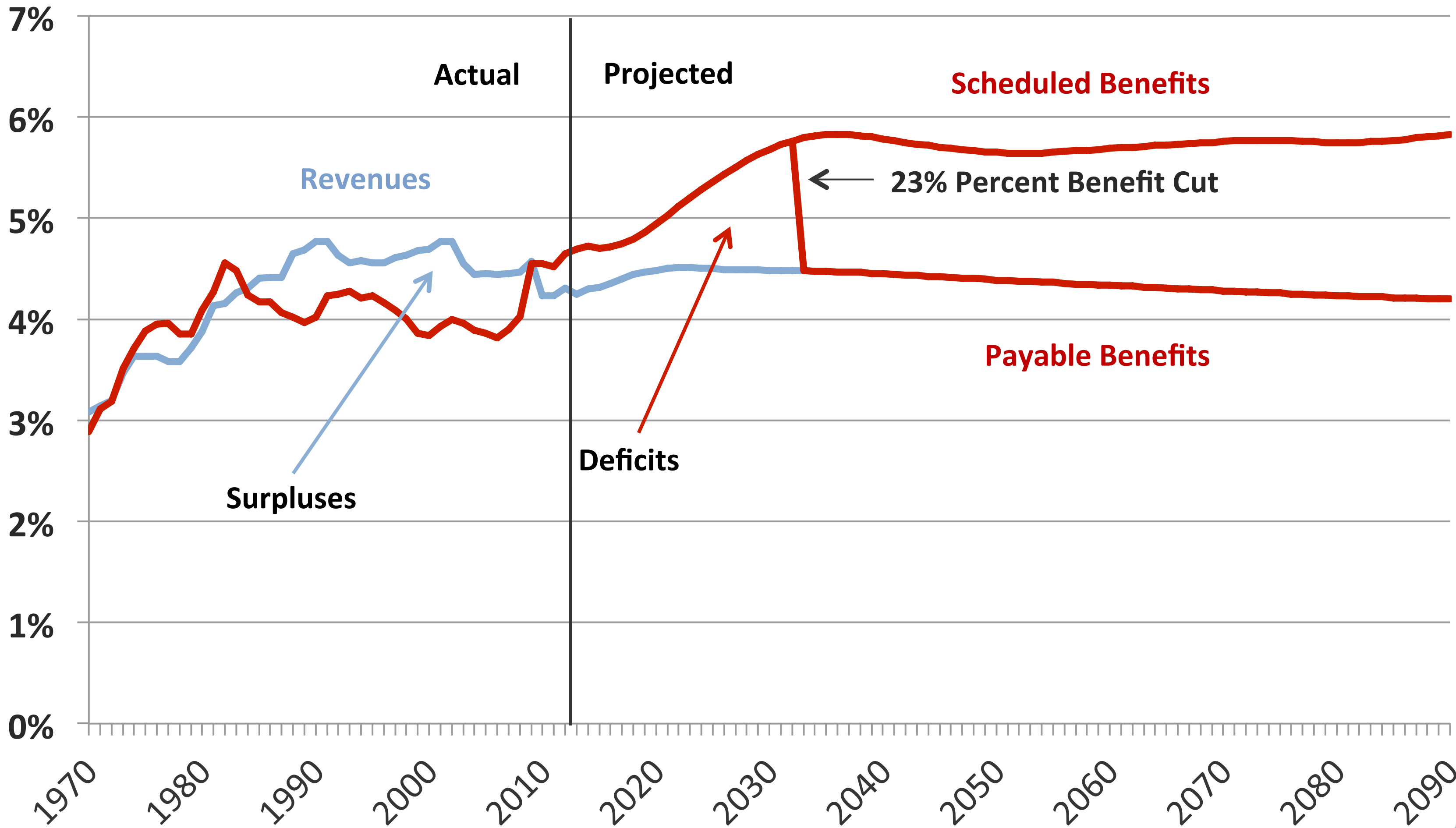
Looming Social Security Insolvency

Social Security Costs and Revenues (Percent of GDP)



Source: 2013 Social Security Trustees Report.

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Insufficient Revenues

- **Unpaid for Tax Cuts** in 2001, 2003, 2010, and 2013 lowered revenue collection without making corresponding spending cuts or tax increases to offset the budgetary effect

- **Spending in the Tax Code Costs $1.2 Trillion** annually in lost revenues through so called "tax expenditures," which make the tax code more complicated, less efficient, and force higher rates

Source: Joint Committee on Taxation (2013).

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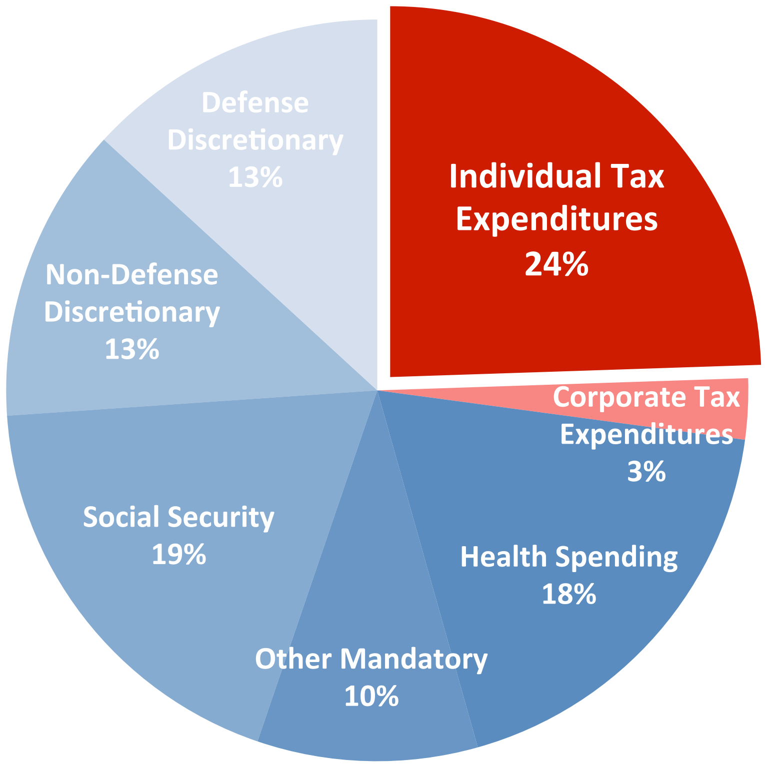
Excessive Spending Through the Tax Code (Tax Expenditures)

Tax Expenditures as a Percent of Primary Spending if Included in the Budget



Large Individual Tax Expenditures and Their 2014 Costs (billions)

Employer Health Insurance Exclusion	**$143**
Special Rates on Dividends and Capital Gains	**$91**
401(k)s and IRAs	**$79**
Mortgage Interest Deduction	**$72**
Earned Income Tax Credit	**$67**
Child Tax Credit	**$58**
State and Local Taxes Deduction	**$52**
Charitable Deduction	**$46**

Source: Joint Committee on Taxation (2013)

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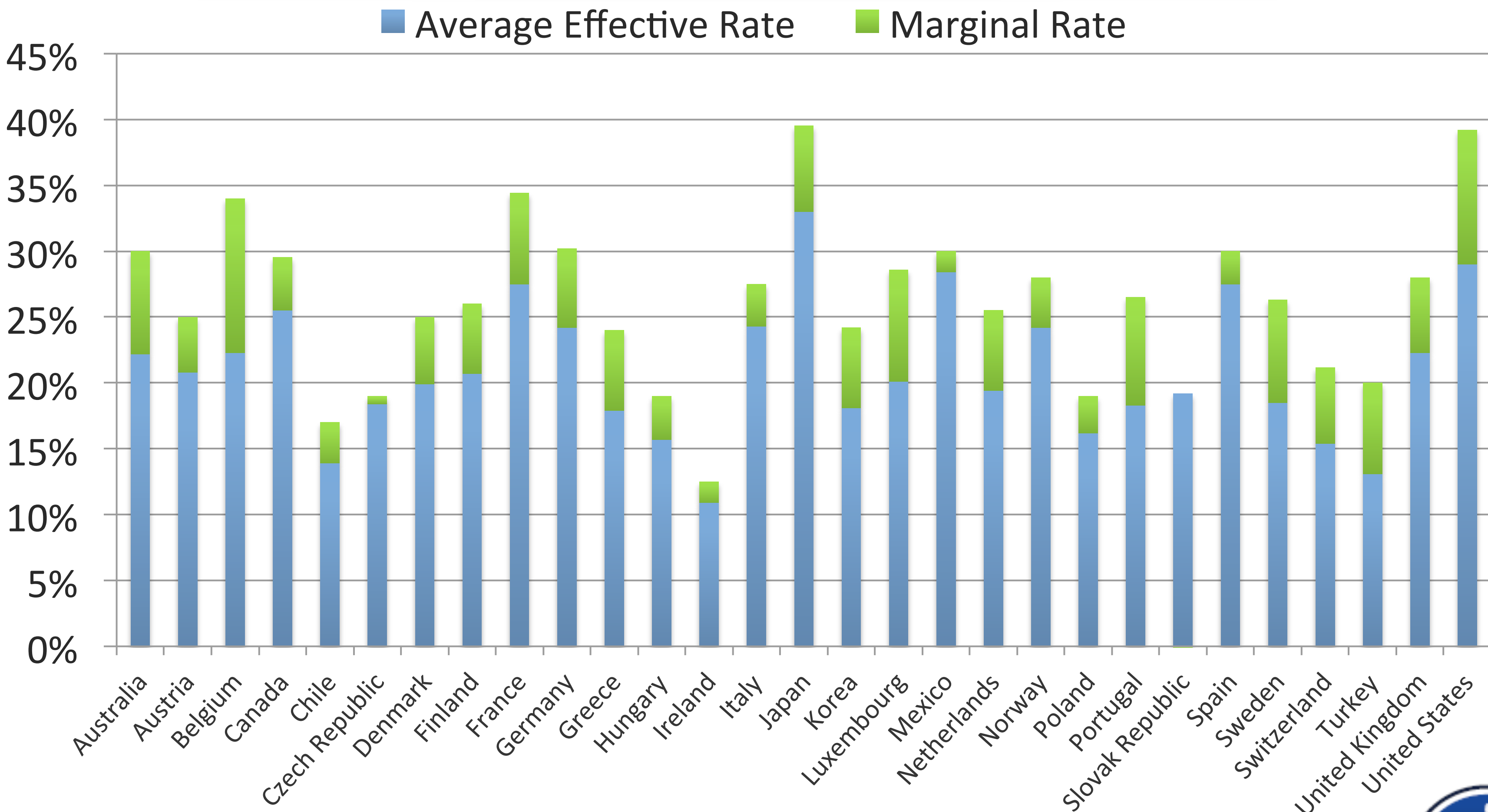
Corporate Tax Rates By Country



Note: Estimates based on 2010 data from the OECD and AEI.

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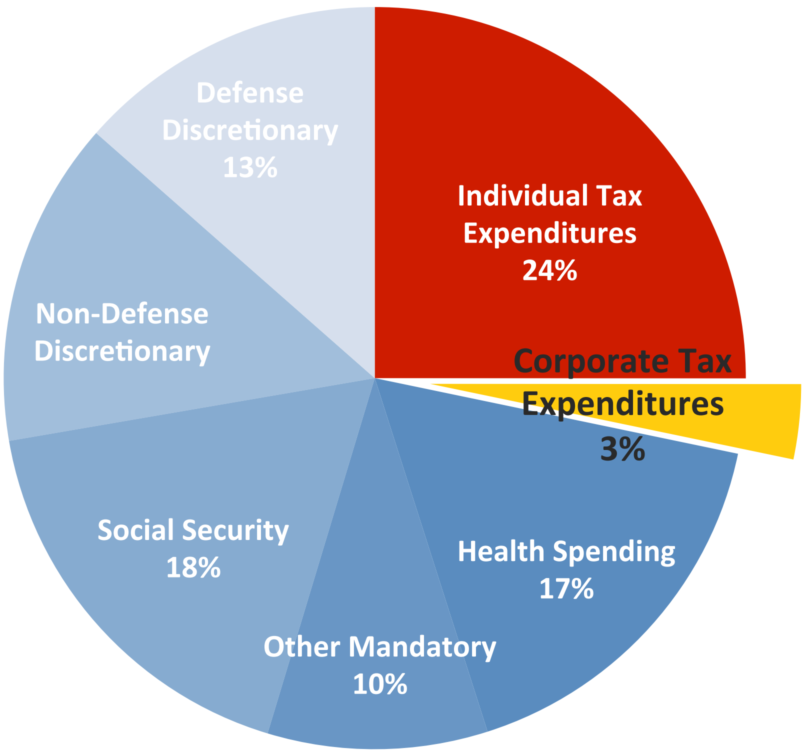
Large Corporate Tax Expenditures

Tax Expenditures as a Percent of Primary Spending if Included in the Budget



Large Corporate Tax Expenditures and Their 2013 Costs (billions)

Deferral of Foreign Income	**$42**
Accelerated Depreciation	**$14**
Domestic Production Activities Deduction	**$10**
Exclusion of Interest on State and Local Bonds	**$9**
Credit for Research Activities	**$7**
Deferral of Active Financing	**$6**

Source: Joint Committee on Taxation, Congressional Budget Office

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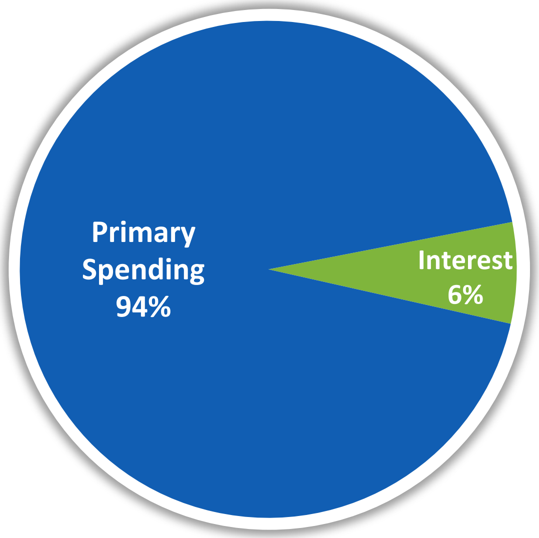
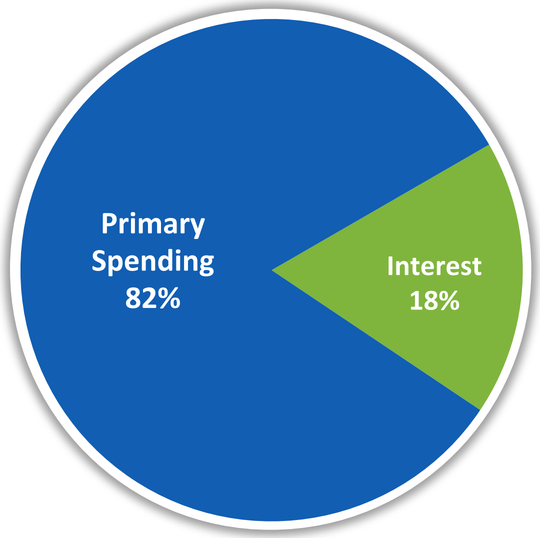
Interest as a Share of the Budget

2013



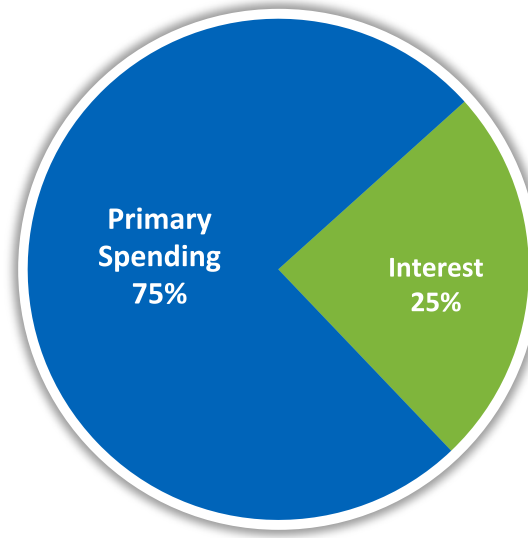
Total Spending = 21% of GDP

2030



Total Spending = 25% of GDP

2050



Total Spending = 30% of GDP

Note: Estimates based on CBO current law Baseline.

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Setting the Record Straight

- **We can't CUT our way out**

  Eliminating Congressional salaries, foreign aid, and earmarks would reduce the deficit by only 4%.

  Balancing the budget through spending cuts alone would require cutting all spending by a third.

- **We can’t TAX our way out**

  To bring the debt down to 60% over the next decade by increasing tax rates on **EVERYONE**, the bottom rate would have to rise from 10% to 16% and the top rate from 39.6% to 55%

  To fix the debt by taxing families making over $250,000, the top rate would have to exceed 100%*

- **We can’t GROW our way out**

  Faster growth means more revenue, but also higher spending on entitlement programs

  Fixing the debt with growth alone would require record-high growth rates every year

*Data from the Tax Policy Center.

We Can't Inflate or Grow Our Way Out

Inflation

- An unexpected increase in inflation could temporarily reduce the real value of debt and federal interest payments to investors
- However, higher inflation would prompt investors to demand higher interest payments, increasing the costs of financing new debt
- Higher inflation would also push up spending for all inflation-indexed programs, including Social Security, food stamps, military pensions, veterans' benefits

Growth

- Strong economic growth is a necessary but not sufficient condition
- Many spending programs grow as the economy does, and would outpace revenue growth
  - Social Security payments would increase as wages and, thus, benefits grew over time
  - Health care spending would grow even faster, given that costs grow faster than the overall economy
- The levels of growth needed to significantly reduce medium-term debts would be way above historical norms

How to Reduce the Deficit

- Domestic Discretionary Cuts
- Defense Spending Cuts
- Health Care Cost Containment
- Social Security Reform
- Other Spending Cuts
- Tax Reform and Tax Expenditure Cuts
- Budget Process Reform

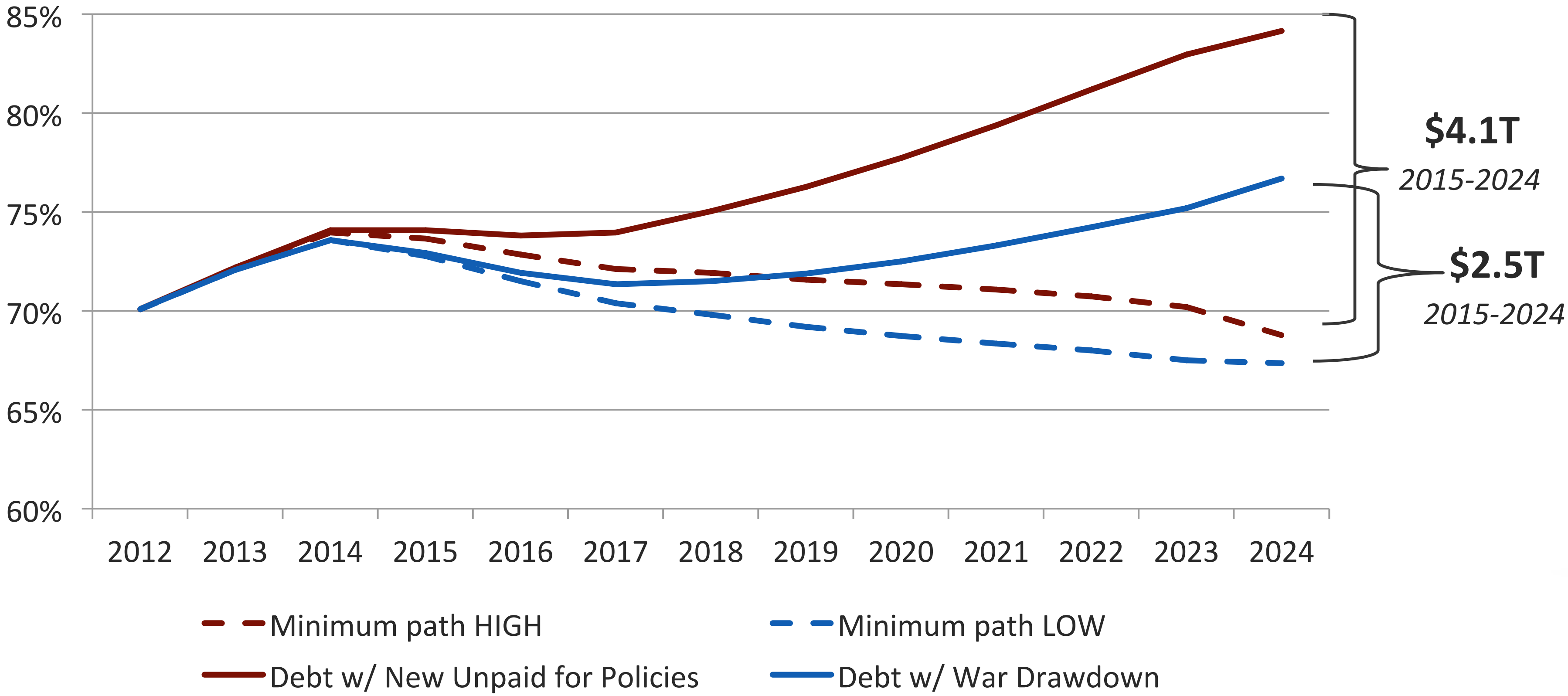
We Have Made Some Progress…

Deficit Reduction Enacted So Far	(2015-2024)
Continuing Resolutions in FY2011	$920 billion
Budget Control Act (2011)	$1,235 billion
American Taxpayer Relief Act (2013)	$970 billion
Sequestration	$1,255 billion
Bipartisan Budget Act (2013)	$40 billion
TOTAL ENACTED SAVINGS	**$4.4 TRILLION**
Total spending cuts	*$2.0 trillion*
Total revenues	*$0.8 trillion*
Total interest	*$1.6 trillion*

Note: CRFB calculations from current policy baseline

Lawmakers Need At Least Another $2.5 Trillion…

Debt to GDP Under Various Scenarios



*Source: CRFB calculations based on CBO data.
Note: Projections for debt with unpaid for policies assumes war drawdown, sequester repealed, doc fixes, refundable tax credits extended, and normal tax extenders.

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Lawmakers Need an Additional $2.5 Trillion in Savings

$2.5 trillion in savings over ten years is the minimum amount of deficit reduction needed to put debt on a clear downward path as a share of the economy.

Falling short of this goal would:

- ***Leave no margin for error***: Should projections prove too optimistic, debt levels could easily be on an upward path.
- ***Would result in slower economic growth***: A larger debt stock will crowd out private investment an slow growth.
- ***Leave little fiscal flexibility***: Lawmakers will find it more difficult to respond to a disaster or financial crisis.
- ***Have little chance of stabilizing the debt beyond the ten-year window***: While less savings may stabilize the debt temporarily, aging and rising health care costs will put debt on a unsustainable path in the long term.

Advantages of a Grand Bargain

- **Debt stabilized and falling** as a share of the economy later in the decade, and all the benefits associated with a declining debt burden:
  - **Less "crowding out"** of private sector investment
  - **Stronger confidence** in businesses and markets
  - **Greater certainty and stability**
  - **Stronger economy** over the long-term
  - **Lower interest payments** and increased fiscal space
  - **Intergenerational equity**
  - **Reduced or eliminated risk of fiscal crisis**

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Advantages of a Grand Bargain

- **Increased chances of enacting a comprehensive debt solution**
  - **Political trade offs** necessary to address entitlement growth and revenues
  - **Shared sacrifice** in a Grand Bargain approach
  - **Realize the gains of debt reduction** by stabilizing and reducing the debt, and not just making difficult decisions that solve only part of the problem

- **Restore America's faith** in the political system

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The Announcement Effect

- **Just announcing the adoption of a debt reduction plan** can provide a boost in confidence, aiding the economic recovery today
- **Businesses and investors frequently cite the uncertainty** over if and how the U.S. might control its debt trajectory when holding back on investment
- **Prominent lawmakers, government officials, economists, and experts across the ideological spectrum** have reiterated the benefits of the announcement effect, including:
  - Ben Bernanke, Fed Chairman
  - The International Monetary Fund
  - Glenn Hubbard, former Chair of the President's CEA
  - Mark Zandi, Chief Economist, Moody's Analytics
  - Michael Bloomberg, Mayor of New York City
  - Alan Blinder, former Fed Vice Chairman
  - Larry Summers, former Director, NEC

Note: For more information on the "announcement effect," see CRFB at http://crfb.org/blogs/announcing-announcement-effect-club

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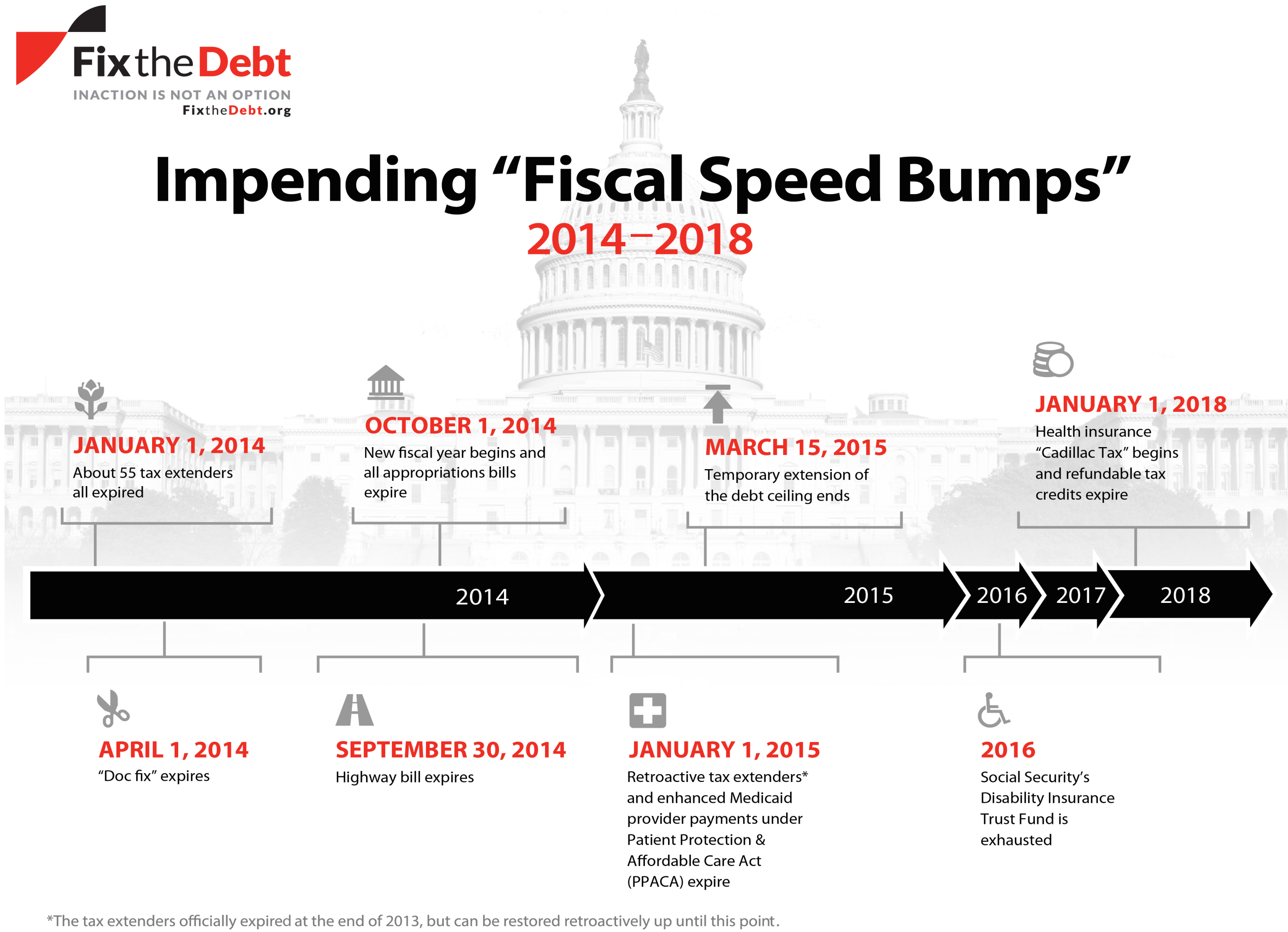
Upcoming Opportunities



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We’ve Gone Small, Stupid, and Short

The Ideal Plan Would Go Big, Go Smart, and Go Long in Deficit Reduction, But Lawmakers Have Come Up Short

They’ve Gone Small

- Lawmakers have enacted more than $4.4 trillion in savings, but $2.5 trillion is still needed to put debt on a downward path as a percent of GDP this decade.

They’ve Gone Short

- Little progress has been made on either reforms to the tax code or entitlement programs, the long-term drivers of the debt.

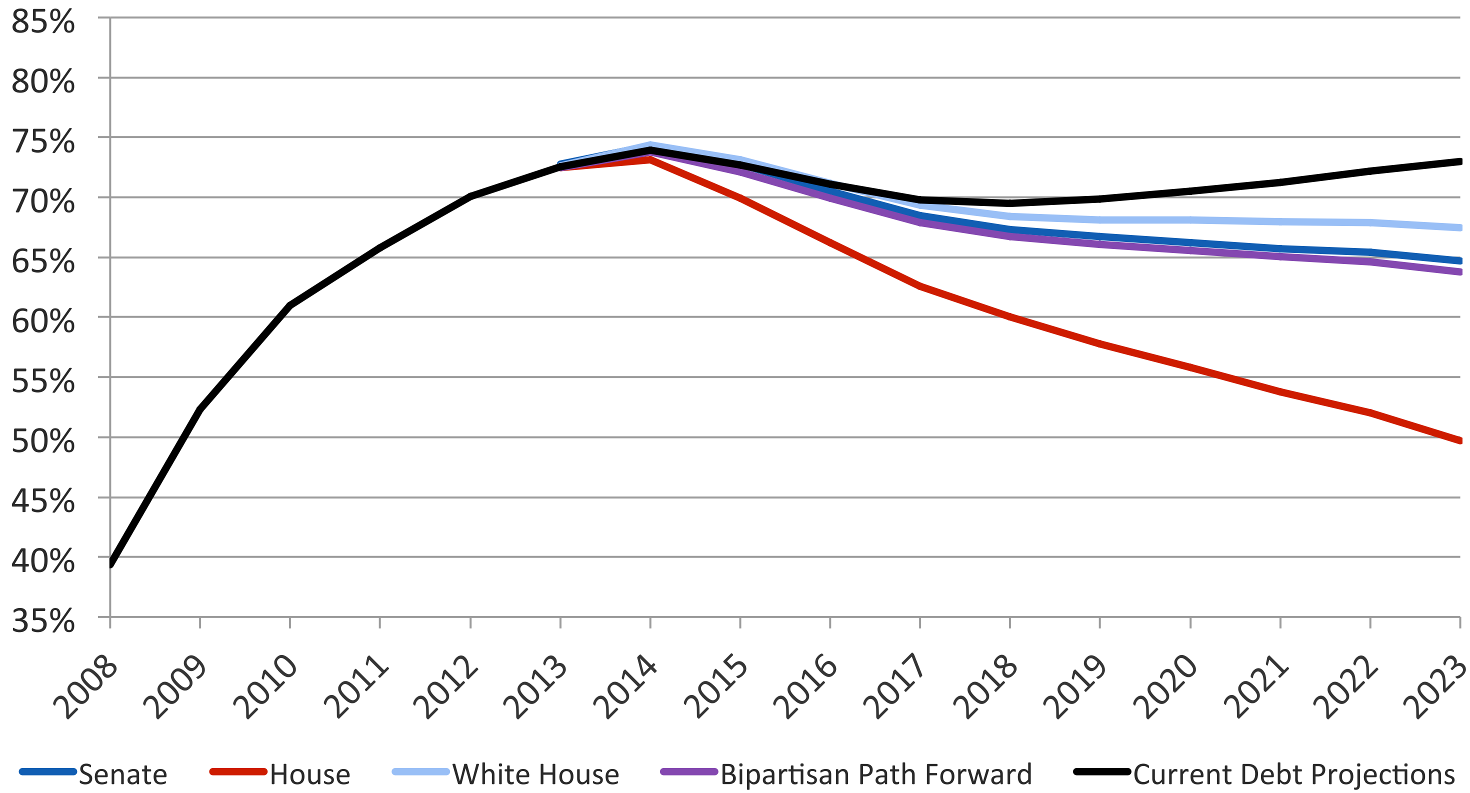
They’ve Gone Stupid

- Sequestration does not identify inefficiencies and achieves much of its savings upfront when the economy is still recovering.

Recent Proposals

Debt Projections (Percent of GDP)

Encouragingly, the House, Senate, and White House budgets would all put the debt on a downward path as a share of the economy this decade (though to different degrees).



Note: "Bipartisan Path" refers to Erskine Bowles and Alan Simpson's new deficit reduction proposal (April 2013)

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Prominent Deficit Reduction Proposals

Savings/Costs in Billions (2014-2023)

	"Step 3" of Bipartisan Path Forward	President's Deficit Reduction Plan	President's Full Budget	Senate Budget	House Budget
Jobs Measures	$0 billion	-$50 billion	-$215 billion	-$100 billion	$0 billion
War and Sandy Drawdowns	$0 billion	N/A	$100 billion	$385 billion	$50 billion
Discretionary	$385 billion	$175 billion	$175 billion	$380 billion	$250 billion
Health Care	$585 billion	$400 billion	$400 billion	$275 billion	$2.72 trillion
Other Mandatory	$285 billion*	$145 billion*	$25 billion	$75 billion	$960 billion
Chained CPI	$280 billion	$230 billion	$230 billion	$0 billion	$0 billion
Sequester	$0 billion**	$0 billion	$0 billion	$0 billion	$995 billion
Revenues	$615 billion*	$630 billion*	$905 billion	$975 billion	$165 billion
Subtotal	**$2.15 trillion**	**$1.53 trillion**	**$1.62 trillion**	**$1.99 trillion**	**$5.14 trillion**
Interest	$350 billion	$200 billion	$160 billion	$310 billion	$1.02 trillion
Total New Savings	**$2.50 trillion**	**$1.73 trillion**	**$1.78 trillion**	**$2.30 trillion**	**$6.16 trillion**
Memo:					
Tax Provisions	$740 billion	$730 billion	$1.01 trillion	$975 billion	$165 billion^
Spending Provisions	$1.76 trillion	$1.0 trillion	$770 billion	$1.33 trillion	$6.00 trillion

Note: Savings are rounded and calculated from a current policy baseline.

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Simpson and Bowles's "Bipartisan Path Forward"

- In April, FTD co-founders Erskine Bowles and Alan Simpson released a new deficit reduction plan – *A Bipartisan Path Forward*
- Calls for $2.5 trillion in new deficit reduction against realistic projections, on top of the $2.7 trillion that lawmakers have already enacted over the 2014-2023 period
- Would reduce the debt from over 73% of GDP at the end of FY2013 to 64% of GDP by FY2023
- The Bipartisan Path Forward calls for:
  - Tax reforms that raise $585 billion in new revenue
  - $585 billion in health care savings
  - $280 billion in savings from switching to the chained CPI
  - $265 billion in other mandatory savings
  - $385 billion of discretionary savings

Source: OMB, CRFB

The House Budget

- Calls for over $6.1 trillion in new deficit reduction against realistic projections, on top of the $2.7 trillion that lawmakers have already enacted over the 2014-2023 period
- Would reduce the debt from over 73% of GDP at the end of FY2013 to below 50% of GDP by FY2023
- The House budget calls for:
  - Revenue-neutral tax reform that reduces tax rates to 10% and 25% and eliminates the AMT
  - Maintains sequester, but shifts defense savings to non-defense discretionary
  - Repeals coverage provisions of health reform act
  - Medicare: competitive bidding system that begins in 2024, further means-testing premiums, malpractice reforms
  - Block grants Medicaid
  - Other mandatory reforms: federal retirement, farm subsidies, food stamps, Fannie/Freddie, energy subsidies, land purchases, and other programs
  - Reduces transportation spending

Source: CBO

The Senate Budget

- Calls for $2.25 trillion in new deficit reduction against realistic projections, on top of the $2.7 trillion that lawmakers have already enacted over the 2014-2023 period

- Would reduce the debt from over 73% of GDP at the end of FY2013 to 65% of GDP by FY2023

- The Senate budget calls for:
  - Tax reforms that raise $975 billion in new revenue
  - $275 billion in Medicare savings
  - $100 billion in new infrastructure spending
  - Further reductions to war spending
  - Other spending cuts

Source: CBO

The President's Budget

- Calls for $1.78 trillion in new deficit reduction against realistic projections, on top of the $2.7 trillion that lawmakers have already enacted over the 2014-2023 period
- Would reduce the debt from over 73% of GDP at the end of FY2013 to 67% of GDP by FY2023
- The President's budget calls for:
  - Tax reforms that raise $580 billion in new revenue
  - $400 billion in health care savings
  - $230 billion in savings from switching to the chained CPI
  - $145 billion in other mandatory savings
  - $200 billion in new jobs measures
  - Further reductions to war spending
  - $175 billion of discretionary savings
  - New spending initiatives paid for by mostly tax increases

Source: OMB, CRFB

A Better Path Forward

Our leaders should come together to enact a comprehensive and thoughtful plan which would be:

Targeted

- Spending cuts should be smart to ensure that they only target wasteful spending, rather than gutting vital government functions

Enacted Now but Implemented Gradually

- A big plan would provide the policy certainty necessary for business planning, and gradual implementation would preserve the momentum of the economic recovery

Addressed to the Drivers of the Debt

- Any deal should focus on reining in the out-of-control growth of healthcare costs and entitlement spending, while preserving programs for those who need them most

Background on the Campaign to Fix the Debt

Fix the Debt

The Campaign to Fix the Debt - Overview

- The Campaign to Fix the Debt is a national bipartisan effort to encourage our elected leaders to enact a comprehensive debt deal within the next year by creating an environment where voting 'yes' reflects both good policy and safe politics.

- The Campaign believes that the national debt is the most serious economic and national security threat facing this country, and we must come together as a nation to fix it.

- To achieve this goal, the Campaign works at the grassroots and grasstops levels through a combination of state and local coalition building, business leader support, social media efforts, Congressional outreach, and both earned and paid media.

The Fix the Debt Campaign by the Numbers

- 364,500 citizen activists
- 23 state chapters with 625+ steering committee members
- 180 CEOs
- 2,500 small business owners
- 136 former members of Congress
- 29 partner organizations
- 43 former Governors
- More than 2,700 small business leaders are members of the Campaign to Fix the Debt.
- There have been over 180,000 letters sent to Congress

Useful Resources

The Committee for a Responsible Federal Budget

http://crfb.org

http://www.fixthedebt.org

Policy Papers:

Our Debt Problems Are Still Far From Solved

Going Big Could Improve the Chances of Success

What We Hope to See from the Budget Conference Committee

Revenue and Health Care Savings Options

Congressional Budget Office

Federal Debt and the Risk of a Fiscal Crisis