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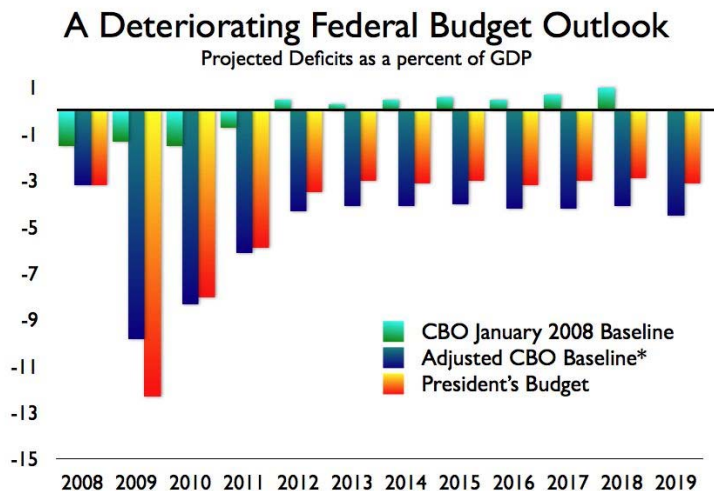
The President's FY 2010 Budget

President Obama's first budget contains many encouraging signs, along with some items of concern. He is to be commended for providing a 10-year budget projection and a specific deficit-reduction goal; for including a number of items in the baseline budget that previously were not included (e.g., war costs, AMT fix); and for supporting a PAYGO concept in connection with mandatory spending increases and tax cuts.

At the same time, the President is not proposing to adopt discretionary spending caps or automatic reconsideration triggers for mandatory spending items and tax preferences. In addition, he is proposing to move some items from the discretionary to the mandatory spending category. He is also advocating expanding health care coverage before we have demonstrated our ability to control health care costs, and before we make a significant down-payment on the federal government's tens of trillions of dollars in current unfunded health care promises.

The President's budget results in total debt-to-GDP of 96 percent and rising by 2010. This serves to demonstrate the need for the creation of a Fiscal Future Commission to help us get our federal finances in order before we lose the confidence of our foreign lenders.

**-- David M. Walker, President & CEO, PGPF
February 26, 2009**



SOURCE: PGPF based upon Congressional Budget Office January 2008 and February 2009 data. *We have adjusted CBO's January 2009 baseline to reflect the impact of recently-enacted American Recovery and Reinvestment Act (stimulus legislation).

President's Budget for Fiscal Year 2010

	2008 Actual	2009	2010	5-Year Total: 2010-2014	10-Year Total: 2010-2019
<u>In billions of dollars</u>					
Revenues	2,524	2,186	2,381	14,997	35,250
Outlays	<u>2,983</u>	<u>3,938</u>	<u>3,552</u>	<u>18,764</u>	<u>42,219</u>
Deficits	459	1,752	1,171	3,767	6,969
Debt Held by the Public	5,803	8,364	9,509	---	---
 Total (Gross) Public Debt	 9,986	 12,704	 14,078		
<u>As Percent of GDP</u>					
Revenues	17.7%	15.4%	16.2%	---	---
Outlays	<u>21.0%</u>	<u>27.7%</u>	<u>24.1%</u>	---	---
Deficits	3.2%	12.3%	8.0%	---	---
Debt Held by the Public	40.8%	58.7%	64.6%	---	---
Total (Gross) Public Debt	70.2%	89.2%	95.6%		

Highlights:

- The Administration's economic assumptions assume rapid economic recovery, with real GDP growth of 3.2 percent in 2010 and 4.0 percent in 2011. CBO's pre-stimulus baseline assumes real GDP growth of 1.5 percent in 2010 and 4.2 percent in 2011. The Blue Chip Consensus forecast is 2.1 percent and 2.9 percent for 2010 and 2011 respectively. By 2019, the Administration's estimate of GDP is \$608 billion higher than CBO's pre-stimulus GDP estimate.
- Should the economy not recover as quickly as the Administration projects, deficits and debt will be higher than projected in the budget.
- Over the 2010-2019 period, revenues average 18.7 percent of GDP, while outlays (spending) average 22.6 percent. As a result, deficits average 3.9 percent for the 10-year period.
- Discretionary spending would increase by 14 percent from 2008 to 2009 and 7 percent between 2009 and 2010. Once the stimulus is mostly spent out, the budget projects discretionary spending growth of about 2 percent a year beginning in 2015. (Discretionary spending declines between 2010 and 2011, then bumps around as the impact of the budget proposals collide with and the stimulus winding down.)

- Debt held by the public goes from \$5.8 trillion in 2008 to \$15.4 trillion in 2019 (41% of GDP to 67% of GDP). The total public debt rises from 70.2 percent in 2008 to over 100 percent (101.2) of GDP in 2019.
- **Composition of Spending:** The budget would continue the trend towards larger and larger shares of total spending for the major entitlement programs: Social Security, Medicare and Medicaid. As those programs grow (along with net interest costs), there is less available for everything else.

Composition of the President's FY 2010 Budget
(Percent of GDP)

	Actual		
	2008	2013	2019
Social Security	4.3	4.4	4.9
Medicare	2.7	3.1	3.8
Medicaid	1.4	1.7	2.0
Medicare and Medicaid	4.1	4.8	5.8
Net Interest	1.8	2.4	2.7
Defense	4.2	3.4	3.0
Other mandatory	2.9	2.8	2.6
Other Discretionary	3.7	3.7	3.2
Disaster	<u>0.0</u>	<u>0.1</u>	<u>0.1</u>
Total Outlays	20.9	21.7	22.3
Debt held by the public	40.8	65.8	67.2

- **Reserve Funds:** The budget includes “reserve funds” for health care and climate change proposals and a contingent reserve fund for financial stabilization efforts. The purpose of the funds is to set aside financing for those proposals.
 - The *health care reserve fund* earmarks \$318 billion in new revenues from reducing itemized deductions and increasing Medicare Part D drug benefit premiums for high-income taxpayers and \$316 billion in proposed Medicare and Medicaid savings for comprehensive health care reform. The amounts are placeholders. The assumed savings amounts appear to be generally consistent with CBO estimates of similar provisions. The Administration does not put forward a specific health care reform proposal. Nor does it specify any mechanism to assure that the cost of reform would be deficit neutral as the Administration’s budget assumes.
 - The Administration proposes a cap and trade system to reduce greenhouse gases, which would raise about \$80 billion per year beginning in 2012. Those revenues would be set aside in a *climate revenue reserve fund* that the Administration would use to pay for

clean energy initiatives (20 percent of auction proceeds) and to offset the cost of the “Making Work Pay” tax credit (80 percent of receipts).

- The budget includes a placeholder of \$250 billion in a *contingent reserve fund* to pay for additional financial stabilization activities. At an estimated net cost to the government of 33 cents on the dollar, the funds would support \$750 billion in asset purchases.
- **Tax Changes:** The Administration proposes significant tax changes. It would extend the 2001 and 2003 tax cuts for taxpayers earning less than \$200,000 (individuals) and \$250,000 (married). In addition, the Administration would extend its Make Work Pay tax credit, expand the earned income tax credit, create a saver’s credit together with a provision to automatically enroll employees in IRAs and 401(k)s, and provide an “American Opportunity Tax Credit.”

Upper income taxpayers (those earning above the \$200,000 and \$250,000 thresholds) would see a 20 percent rate on capital gains and dividends (currently 15 percent) and a phase-out of the personal exemption and limitation on itemized deductions (in addition to the limitations imposed to help finance health care reform).

Significant changes include:

(Deficit increases (+) or decreases (-) in 2013)

- Limit on itemized deductions: -\$34 billion
- Climate revenues: -\$79 billion
- Other revenue changes: - \$37 billion
 - Placeholder for unspecified reforms: -\$20 billion
- Other upper income tax changes: -\$58 billion
 - Includes higher rates, capital gains, phase-outs
- EITC, child credit, American Opportunity credit, etc.: \$30 billion
- **Iraq and Afghanistan:** As placeholders, the budget includes an additional \$75.5 billion in 2009 and \$130 billion in 2010 for Iraq and Afghanistan. The Administration will provide details in its 2009 supplemental appropriations request and in its full 2010 budget.
- **Budget Enforcement:** The Administration supports a return to pay-as-you go budgeting for mandatory programs and tax proposals. The budget does propose to reimpose caps on discretionary spending. Nor would it require policymakers to reconsider adopted programs or tax cuts if deficits balloon out of control.
- **Budget Baseline:** The Administration’s adjusted baseline deviates significantly from the approaches used by CBO in its baseline projections. CBO’s baseline reflects statutory requirements enacted in the 1990 Budget

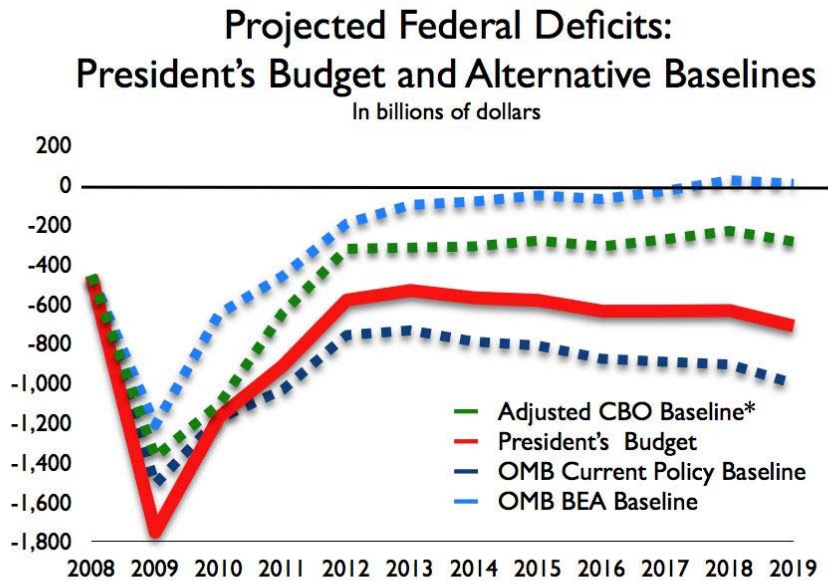
Enforcement Act (BEA). OMB’s “current policy” baseline inserts certain assumptions into future projections, including:

- A continuation of the 2001 and 2003 Bush tax cuts;
- Higher Medicare physician payments than projected under current law requirements;
- Adding funding for overseas military operations and international emergency programs;
- Adding funding for anticipated future disasters; and
- Changing Pell grants into an indexed, mandatory program.

As the result of above and other changes, the OMB preferred “current policy” baseline is \$300 billion higher in 2009 and \$527 billion higher in 2010 than its BEA baseline (which is most comparable to the one calculated by CBO).

The impact of the adjusted, higher OMB current policy baseline is that the Administration (and the Congress, if it follows the Administration’s lead) can increase the budget and the deficit without being charged with doing so.

For example, the 2013 deficit under the President’s proposed budget is \$532 billion. That compares favorably to the \$734 billion deficit contained in its “current policy” baseline, but less favorably to the \$194 billion deficit in its BEA baseline projection.



Source: PGPF based on CBO (January 2009) and OMB (February 2009). *We have adjusted the CBO January 2009 baseline to reflect the American Reinvestment and Recovery Act of 2009. The OMB BEA baseline is most comparable to the adjusted CBO baseline.