In Our Estimation: Episode 2 – Budget 101
TRANSCRIPT

Adam Russell: Hello and welcome to *In Our Estimation*, a podcast from the Congressional Budget Office that looks at the inner workings of CBO and its role in the legislative budget process. I'm your host, Adam Russell, and in this episode we'll introduce you to the federal budget.

We're going to break down the budget process, the stages where CBO gets involved, and talk a little bit about the current budget scenario. Joining me today are three of my colleagues in CBO's Budget Analysis Division.

Adam Wilson works in the scorekeeping unit, Avi Lerner is in the projections unit, and Sunita D'Monte is in the cost estimates unit that covers Defense, International Affairs, & Veterans' Affairs.

Welcome to the podcast!

Adam Wilson: Thanks!
Avi Lerner: Sure!
Sunita D'Monte: Glad to be here!

AR: Most people understand what a budget is, whether they have a budget for themselves or their families. Many folks out there use apps that let them keep track of what they owe and how much income they have each month so they can manage their finances and savings, avoid overspending, and going into debt. Now, Avi, can you explain those two terms—deficit and debt—when we talk about the federal budget?

AL: Sure. When you hear about the federal government running a deficit in a given year, it just means the government spent more than what it collected in revenue. And the debt is, generally speaking, the cumulative deficits that build up over time.

AR: And by revenue, you just mean all the taxes the government collects?

AL: Right, exactly.

AR: OK. We'll talk more about the debt later on. Right now, let's breakdown the two main components of any budget: income and expenditures. Or, when you're talking about the federal budget, revenues and outlays. What are the federal government's primary sources of revenue?

AL: Specifically, the taxes it collects are income taxes from people in the workforce, payroll taxes like for Social Security and Medicare from workers and companies, and corporate income taxes. There are other, smaller revenues like excise taxes, the estate tax, and so on. But those first three are the big ones.

AR: And when you add up all of that revenue, how much does the federal government take in?

AL: It's been $3.3 trillion over the last few years, about half of which comes from individual income taxes.

AR: And the other component of federal budgeting is expenses, or outlays. How much does CBO estimate that the government is going to spend in 2018?

AL: About $4.1 trillion overall.

AR: Wow! $4.1 trillion is a lot of money. Sunita, how does the government spend all of that?

SD: Well, there are three types of federal spending: discretionary spending, mandatory spending, and net interest paid on the debt. And those categories cover everything from funding for Medicare, to spending on education, the military, transportation, to name just a few.

AR: And what share of the federal budget is spent on each of those types of spending?

SD: In 2017, the government spent roughly $4 trillion. And about $2.5 trillion—a little over 60 percent—was mandatory spending and roughly $1.2 trillion—or 30 percent—was discretionary spending. The remaining $300 billion was for interest payments on the debt. CBO has infographics on its website that show federal spending and the budget in a little more detail.

AR: OK. So just by those names alone, I'm guessing that discretionary refers to spending that the Congress decides to allocate, mandatory spending is for things the government is required to fund, and net interest is money paid for previously borrowed funds?

SD: That's more or less true. Mandatory spending, which is also known as direct spending, refers to the budget authority provided by laws other than appropriation acts and the outlays from that budget authority.

Most of that direct—or mandatory—spending is for programs such as Social Security, Medicare, and Medicaid.

AR: So that's why the Congress doesn't have to pass a bill every year to fund something like Social Security?

SD: That's right. But there are a lot of things that Congress does have to fund every year in appropriation bills.

AR: And that's the spending known as discretionary spending?

SD: Right again. Discretionary spending is set at the *discretion* of the Congress and it can be separated into two, broad categories: defense spending and non-defense spending.

AR: OK. So, Avi, I want to go back to you real quick. When CBO talks about "net interest" in terms of the debt, what does that mean?

AL: Well, as we said earlier, the deficit is, roughly speaking, a measure of how much the government needs to borrow in a given year. Whereas the debt—which stands at 15 and-a-half trillion dollars—is the cumulative total of that yearly borrowing. When we mention interest, we mean the amount that the government has to pay on that debt. Now, the government also loans money to people. For example, students or small businesses. And it gets interest back from those loans, so we typically talk about "net" interest to include the amount of interest we pay minus what we receive.

AR: So based on the numbers you and Sunita mentioned, the government spent, I guess, roughly about $4 trillion but collected only $3.3 trillion in revenue. Which means a deficit of about $700 billion?

AL: Right. And when the government needs to borrow money to finance a budget deficit, it doesn't go to a bank and apply for a loan like you or I do.

AR: So what does it do?

AL: It borrows from the public; Treasury issues debt by selling government securities such as Treasury bills, notes, bonds, and other inflation-protected securities.

AR: OK – but who buys these securities?

AL: The Treasury sells them to individuals, corporations, pension funds, and foreign governments to name a few.

AR: And like a savings bond, the money lent to the government from these securities is paid back with interest?

AL: Right. Those interest payments on publicly-held debt are part of the spending in the federal budget.

AR: OK. So that's a very high-level overview of the federal budget. I want to change gears here and talk about the timeline for the budget process and how CBO supports the Congress during the legislative budget process. Adam, can you tell us a little more about that?

AW: Sure. The Congressional budget process begins when the President submits his annual budget proposal. That's required by law to be submitted no later than the first Monday in February. Next comes CBO's report on the Budget and Economic Outlook. That's supposed to be published by February 15, though it often comes out earlier than that. And the budget committees are supposed to use that report then to work in both the House and the Senate to come up with a concurrent resolution on the budget by April 15. They're supposed to come up with that, so that they can then move on to considering annual appropriation bills with the idea that those will all be enacted and in place before the next fiscal year begins on October 1.

AR: Now, in that response that you just gave me, you had a term that was "concurrent budget resolution." Can you just briefly explain what that is?

AW: Yeah! "Concurrent" just means that both chambers agree, but it's a measure that both the House and the Senate agree to that doesn't have to be sent to the President and it's not enacted into law. It serves as a budgetary framework for considering legislation—a "baseline", if you will. It's simply an agreed-upon set of terms by both chambers of Congress can use to consider budgetary legislation lays out the next – or upcoming – fiscal years.

AR: So this budget resolution is a framework or blueprint that outlines how the Congress will implement that spending through appropriations?

AW: Right, but not just appropriation legislation, all budgetary legislation. As I mentioned, CBO has to submit its report on the budget and economic outlook by February 15. That report includes our baseline budget projections, though CBO typically updates those a couple more times throughout the year.

AR: This baseline that we're talking about, that's the one that helps the Congress with the budget?

AW: Right. The baseline projections give the, particularly the budget committees, a sense for what the current law state of the budget is. So assuming no other legislation is enacted, it's a projection of the budget over the next ten years. It typically forms the basis for the concurrent budget resolution and it provides the Congress with a guidepost to measure the budgetary effects of proposed legislation against.

AR: And this is the same baseline that CBO uses to produce its cost estimates?

AW: Yes. CBO uses that baseline to produce cost estimates for proposed legislation. Listeners may already know that CBO is required to provide formal cost estimates for virtually every bill reported by committees, but we also prepare many more cost estimates that are preliminary or informal throughout the legislative process, including draft legislation; amendments in committee and when a bill is on the floor; and during the final stages of legislation in conference committees after it has been passed by both the House and Senate.

AR: Just a shameless plug: if folks are interested in learning more about cost estimates, they can head over to www.cbo.gov/podcasts and look for that podcast episode that we did specifically on cost estimates.

AR: OK. So the budget baseline is a critical tool that helps the Congress and it's used in CBO's cost estimates. But since the federal budget is running a deficit right now, what else does CBO do, Sunita, to keep Members and Committees more informed about the budgetary implications of altering current law?

SD: Well, CBO also releases a volume of options for reducing the deficit—it's something we call "budget options" and you can find it on our website. CBO produces these volumes every other year—near the start of a new Congress. They include a wide range of options from many sources for reducing federal spending and increasing revenues.

The options are posted on our website at cbo.gov/budgetoptions and they have options from other CBO reports that offer approaches to changing spending and federal tax policy.

AR: OK, so if I went to CBO's website, what kind of information would I see included in these budget options?

SD: Well, for each option, CBO presents an estimate of the effects on the budget and a discussion of the relative pros and cons of those changes. But we make no recommendations as to whether that particular option should be enacted. All we do is present the information and potential outcomes.

AR: So in addition to producing cost estimates, CBO also provides the Congress with baseline budget projections as well as options for reducing the deficit. Now that's all helpful for future budget scenarios, but what does CBO do for any short-term analyses on budget trends?

SD: Well, we have something we call the Monthly Budget Review and we publish that on our website on the fifth business day of every month. It covers federal spending and revenues for the previous month and the fiscal year to date. Monthly Budget Reviews are based on information from the Treasury, and they provide details on the monthly status of outlays, receipts, and the deficit.

AR: Now, Adam, you're the chief of CBO's scorekeeping unit. I've heard often that CBO is referred to as a scorekeeper. Can you explain just what that means?

AW: Scorekeeping refers to CBO's role in tracking the budgetary effects of legislation as it's considered or adopted by the Congress. We keep a tabulation of the budgetary effects of all enacted legislation and we use that information to help the Budget Committees gauge compliance with the budget resolution. We also use those estimates to inform subsequent baseline projections.

We also track the budgetary effects of appropriation legislation specifically as it moves through Congressional consideration. That way the Congress knows whether it's acting within the limits set by the budget resolution or existing statutory limits. We call this the "Current Status of Discretionary Appropriations."

AR: And all this information – the status of appropriations – that's available for everyone and not just Members?

AW: That's correct. CBO posts that information to its website. Essentially, this information provides the House and Senate with information of the most recent tabulations of Congressional action on appropriation bills from the time they are reported out of committee to the time they are enacted into law.

It's important to note though that our role as a scorekeeper is purely advisory—CBO applies the scorekeeping rules, or guidelines as they're sometimes referred to, in developing its estimates, but it has no role in enforcing them as they relate to points of order in either chamber—that's reserved for the Budget Committees.

AR: So we've taken a look at the budget process and a few ways CBO supports the Congress with that process. Avi, let's talk now about the fiscal outlook. What do CBO's projections tell us about the nation's budget challenges?

AL: Well as Adam [Wilson] said earlier, two or three times a year CBO publishes a baseline or 10-year forecast. The most recent one came out in April, and there we show that we expect the deficit to grow quickly over the first half of that 10-year window. Over the second half, so between 2023 and 2028, we think the deficit will stabilize relative to the size of the economy, but at a very high level by historical standards.

AR: What are the drivers behind that estimation?

AL: The growth over the first few years stems from new legislation: the recent tax reform law, the Bipartisan Budget Act, and the Consolidated Appropriations Act. Those laws significantly reduced revenues and increased outlays.

AR: By about how much?

AL: Collectively, we estimate that they'll make deficits over the next 10 years $2.7 trillion larger than they otherwise would have been. And about 2/3 of that is from lower revenues and the other third from higher spending.

And this did nothing to help the larger issue at hand: the long-term, unsustainable fiscal path which we've been on for quite some time. Even without the recent legislation, 10-year deficits were projected to exceed $9 trillion and growing over time.

AR: So what would the outcome of these accumulating deficits be?

AL: Well, as deficits accumulate, debt held by the public rises. It'll approach $16 trillion by the end of this year, which is 78 percent of GDP. But, we think it will rise to $29 trillion – or 96 percent of GDP – by 2028. That percentage would be the largest since 1946—the end of World War II—and well more than twice the average over the past fifty years.

AR: Now, you mentioned the growing debt burden as being unsustainable. Can you clarify a little bit more what that means?

AL: Sure. Unfortunately, no one knows how much debt is too much debt. It's important to keep debt levels in check because as the debt grows in relation to the size of the economy, it becomes a bigger burden on current and future generations.

AR: Then what would the economic consequences be, I guess, of waiting to tackle the debt problem?

AL: Well, not to be a downer, but large, continuously growing debt would increase the chance of a fiscal crisis.

AR: Oh, how so?

AL: For starters, investors might become less willing to buy treasuries unless they're compensated with higher returns. Interest rates on federal debt could potentially rise abruptly, and quickly increase the cost for the government to borrow. There's no identifiable tipping point in debt-to-GDP – or any other measure – to indicate a crisis is likely or imminent. But all else being equal, the larger a government's debt and the steeper its rise, the greater the risk of a crisis.

AR: So you're saying the longer we wait to address the debt problem, the more severe or drastic the policies will need to be in order to correct course?

AL: Yeah, that's right.

SD: If there is a silver lining to all of this, it's that lawmakers still have some flexibility in the policies they could enact to correct that course. That may not always be the case down the road, but today it seems to be.

AR: I think that's an interesting point to make, Sunita, and it's a good place to wrap up our conversation. So I just want to thank you, Adam, and Avi for taking the time to be here today.

SD: Sure!
AL: You’re welcome!
AW: Thank you!

AR: For more information about the CBO’s outlook on the federal budget, head over to our website, cbo.gov.

If you would like to leave us feedback about this podcast or have suggestions for future podcast topics, send an email to communications@cbo.gov.

This has been another installment of *In Our Estimation*, a podcast from the Congressional Budget Office. Thanks for listening. We’ll see you next time.

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