THE CONGRESSIONAL BUDGET OFFICE'S BUDGET AND ECONOMIC OUTLOOK

HEARING

BEFORE THE

COMMITTEE ON THE BUDGET HOUSE OF REPRESENTATIVES

ONE HUNDRED TENTH CONGRESS

SECOND SESSION

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THE CONGRESSIONAL BUDGET OFFICE'S BUDGET AND ECONOMIC OUTLOOK

WEDNESDAY, JANUARY 23, 2008

HOUSE OF REPRESENTATIVES,
COMMITTEE ON THE BUDGET,
Washington, DC.

The committee met, pursuant to call, at 10:04 a.m., in room 210, Cannon House Office Building, Hon. John M. Spratt Jr. [chairman of the committee] presiding.

Present: Representatives Spratt, Edwards, Cooper, Schwartz, Becerra, Doggett, Blumenauer, Berry, Boyd, McGovern, Scott, Etheridge, Moore of Kansas, Bishop, Moore of Wisconsin, Ryan, Barrett, Hensarling, Lungren, Conaway, Campbell, Tiberi, Alexander and Smith.

Chairman SPRATT. Let me call the hearing to order and welcome our witness this morning.

Dr. Orszag, as always, we are glad to have you and thank you for coming. Today you are here to lay out your latest forecast or outlook on the budget and economy released just this morning. We are pleased to have your perspective on recent developments in the economy and how these changes have affected the Federal budget and are likely to affect it further.

Given current discussions about economic stimulus proposals in your release on that subject last week, I expect that our members will have questions about the various roles that fiscal policy can play in firing up our faltering economy. Your budget and economic outlook offered some sobering projections on the short-term and long-term fronts. For the short-term, CBO's economic forecast has grown noticeably more pessimistic since last August, and a number of ominous economic signs have emerged since CBO finalized last month the forecast underlying today's report. Unemployment has spiked in 1 month from 4.7 to 5 percent. December retail sales, all important, actually fell by four-tenths of a percentage point from the prior month. And yesterday the Fed felt compelled to make an uncommon if not unprecedented cut of 75 basis points in the Fed funds rate.

Today's new economic forecast adds to the growing evidence that the country and that the economy has weakened and that we as policymakers must and should take action. Meanwhile, CBO shows the deficit for fiscal 2008 is larger than the deficit for fiscal 2007, and the '08 deficit is actually $64 billion worse in this projection than in the projection you made last August. Over the long term, CBO's 10-year forecast is worse and relative to August by $850 billion on an apples-to-apples basis.

Because yours is a baseline forecast, it does not include the full deficit impact of all of the administration's policies and the budget that they will send us in a few weeks. For example, your forecast does not include the roughly $4 trillion impact on revenues which will be occasioned by the President's tax cut agenda or the full cost of ongoing operations in Afghanistan and Iraq.

Under administration policies, the $5.6 trillion surplus projected in 2001 has collapsed, vanished, been replaced by deficits which are nearly equal in amount and which have complicated our efforts, a response to the current slow down in the economy. Today's report provides the latest evidence that we should act and act now to strengthen the economy and that we should do so in a way that is mindful however of the long-term budget challenges, the structural deficits that we face unless we act and act seriously.

This report reminds us also that the President's budget policies, particularly his deficit financed tax cuts, have significantly increased the national debt and make it harder to address our long-term challenges.

So, Dr. Orszag, we have a lot on our plate this morning, a lot to discuss with you, a lot of questions to ask. We look forward to your testimony, your answers to the questions that we will ask and follow. And before turning to you for your testimony, however, I want to recognize Mr. Ryan for any opening statement that he may wish to make.

Mr. Ryan.

Mr. RYAN. Thank you, Chairman Spratt.

And welcome back, Director Orszag.

Over the past few years, I think it is—we have almost come to expect good news when it comes to our near-term deficit projections at every one of these hearings we have had. We have seen dramatic declines in the deficit well below projections for each of the last 3 years. In fact, last year at this time we found ourselves on what many describe as a glide path to near-term balance as a result of our economy's performance. So it is no surprise that we began taking this trend for granted. We simply expected that our economy would keep cranking along, creating jobs, boosting revenues and driving down deficits.

But today I understand that Director Orszag is here to tell us otherwise. CBO is projecting the Federal deficit will increase this year largely as a result of the economic slow down and the drag it is going to place on revenue growth. For the past few weeks there have been broad discussions on how best to address the economic downturn. And there is bipartisan consensus that the Federal Government can and should respond.

But even while the President announced that we should act quickly to move an economic growth package, the exact contents of that package is obviously not yet resolved. As I noted last week, I believe there are several key principles we need to keep in mind. First, do no harm. I am concerned that in our rush to help we will talk ourselves into a quick feel-good hit today that will leave us with a bigger budgetary hangover tomorrow. Second, we need to get the fundamentals right. That means keeping tax rates low and spending under control both in the short and longer term. That is the best prudent recipe for real long-term economic growth. Third, we need to understand that we simply cannot spend our way to prosperity. I am particularly concerned that Congress will be tempted to use the excuse of fiscal stimulus to push through a wish list of new spending, further worsening our budget outlook and our nation's economic future. In short, I believe that in addressing the current economic concerns, we have got to keep our focus on good economic policy that lasts beyond the next few quarters.

On a final note and to be clear, this is in no way a criticism of the CBO. While the information we receive today is critical for drafting our budgets, we have got to recognize the limitations of something we call the baseline. The baseline concept, under which CBO formulates its projections, includes a built-in double standard favoring higher spending and higher taxes. In general, the baseline assumes that spending, even if scheduled to expire, goes on forever while tax relief is always temporary. As a result, extending the spending programs has no impact on baseline deficit while extending tax relief is shown as causing an increase in the deficit. Assuming revenues from the AMT or the expiration of the current tax relief in 2010 simply because they are baked into something called the baseline should not serve as an excuse to impose job-killing tax increases on our nation's economy.

To conclude, as we look at the current economic conditions as well as CBO's longer term forecast, we should pursue policy that maintain low tax rates; keeps spending under control; and works to address the long-term unsustainable growth in our major entitlement programs. Those are the things we should keep our eye on. And I appreciate the Chairman for his indulgence.

Chairman SPRATT. Thank you, Mr. Ryan.

Dr. Orszag, the floor is yours. Before you begin, however, let me attend to a couple of housekeeping details. First let me say that your statement will be made in full part of the record so you can summarize it as you see fit. But I would encourage you, as I did earlier, to take your time and to walk us through this as carefully and deliberately as you see fit.

Secondly, I would ask unanimous consent that all members be allowed to submit an opening statement for the record at this point. There is no objection; so ordered.

[A letter submitted by Mr. McGovern follows:]

The Honorable Jim McGovern
United States House of Representatives
Washington, DC 20515

January 22, 2008

Dear Representative McGovern:

Rising unemployment, declining consumer spending, and contraction in housing values has caused many economists to conclude that federal economic stimulus is needed to reduce the severity of an economic downturn. The warning signs are sobering; if the federal government fails to respond, millions of Americans may pay with lost jobs or serious financial hardship. We urge Congress to act swiftly to enact a stimulus package that ***will work*** to increase consumer spending and employment. Evidence is strong from the most recent recession that the most effective federal policies provide quick infusions of funds to low- and moderate-income households and to state and local governments.

Federal Reserve Chair Ben Bernanke told the House Budget Committee that increased food stamp benefits and tax rebates reaching low-income people are effective ways to spur the economy. "There is good evidence that cash that goes to low and moderate income people is more likely to be spent in the near term." Those with higher incomes are far more likely to save funds they receive, which will not benefit the economy. Increased government spending on unemployment insurance and food stamps will quickly result in more consumer spending, fueling business income and employment. Targeting assistance to state and local governments is also effective stimulus. In the last recession, 37 states reduced their spending by $13 billion, according to the Congressional Budget Office. Federal aid can allow states to spend on vital services such as Medicaid, child support enforcement, job training and employment services, school maintenance and repair, or home energy aid, all of which will lead to job growth and/or increased consumer spending.

A package built from the most effective forms of stimuli would provide the following:

Extend and Improve Unemployment Insurance: Unemployment Insurance has been ranked as the single most effective stimulus measure, with studies showing each dollar of UI spending generating from $1.73 (Zandi, Economy.com, 2004) to $2.15 (Chimerine et al., U.S. Department of Labor, 1999). Because long-term unemployment is rising and more and more of the unemployed will exhaust the basic 26 weeks of benefits, Congress should enact a 20-week supplemental unemployment compensation program for those who have exhausted their basic benefits, with an additional 13 weeks in states with high unemployment, providing adequate funding to states to administer the program. Because UI benefits now average only $285 a week, Congress should also increase weekly benefits by $50. But extensions and increases will only help the minority of unemployed workers who qualify for UI. Only 38 percent of the unemployed now receive any unemployment compensation; the lowest-income workers are disproportionately excluded. To reach more of the unemployed, Congress should provide funding to states to improve their systems by counting more recent earnings, and by extending eligibility to workers only available for part-time work and who leave jobs for compelling family reasons, as provided in the Unemployment Insurance Modernization Act (H.R. 2233; S. 1871).

Increase Food Stamp benefits: Food Stamp benefits average $1 per meal for the 27 million current recipients, 87 percent of whom are living in households below the poverty line. An increase in benefits could be added to Food Stamp electronic debit cards rapidly. Like the current benefits, the temporary raises would be quickly spent and would at the same time prevent childhood ill health and developmental delays associated with inadequate nutrition. The Congressional Budget Office has rated a temporary increase in food stamp benefits highly for cost-effectiveness, short lag time, and relative certainty about the policy impact. Former Treasury Secretary Dr. Lawrence Summers reported to the Joint Economic Committee, "On the spending side the measures most likely to be effective are temporary increases in benefits perhaps for the long term unemployed and food stamp recipients."

Provide a temporary, refundable tax rebate to people who paid payroll or income taxes in 2007: Studies of the impact of the 2001 tax rebates confirmed that low-income, young, credit-constrained households spent more of their rebate checks. The Congressional Budget Office draws this conclusion: "Therefore, policies aimed at lower-income households tend to have greater stimulative effects." If the tax rebate does not broadly reach households that have paid payroll taxes but do not owe income tax, they will miss the households who need the income the most and whose spending will provide the most stimulus. The Economic Policy Institute has estimated that $65 billion would fund rebates of at least $350 per individuals or $700 per married couples who paid payroll or income taxes in 2007. There are good arguments for phasing out the rebate at the upper ends of the income scale, and targeting as much as possible to the lowest-income people, including families with children, whose situation is most precarious.

Increase aid to state and local governments: According to the National Conference of State Legislatures, in mid-December 19 states were already projecting budget shortfalls for the coming FY 2009; 13 of these states estimated budget gaps totaling $23 billion. The number of states in trouble is bound to grow as sales and property tax revenues shrink. If states are forced to cut services, benefits, or personnel, lay-offs and reduced expenditures will make the recession worse. Aid to state and local governments will prevent such ill effects. Helping states and counties to cover Medicaid costs will protect low-income families from loss of medical care at a time when rising joblessness and higher costs make them particularly vulnerable. Reversing child support enforcement cuts now starting to take effect will not only forestall lay-offs but will prevent the loss of billions of dollars in child support collections needed to help low-income families with children make ends meet. In addition, general flexible fiscal relief, similar to the package Congress enacted in 2003 would enable states and localities to quickly address their local varied circumstances.

Fund infrastructure repair or maintenance: The Economic Policy Institute has pointed to more than $100 billion in needed repairs to U.S. public schools – well-defined projects that can be quickly implemented. EPI estimates that $20 billion in such infrastructure repairs would create 280,000 jobs, and would of course be an investment in improving education. We believe that infrastructure investments in a stimulus package should be limited to projects that can be up and running within a year.

Increase home energy assistance: The Low Income Home Energy Assistance Program (LIHEAP) served only 15.6 percent of eligible households in FY 2007, providing assistance averaging $305 per household for home heating or cooling. Between FY 2003 and FY 2007, LIHEAP funding increased by 10 percent, but heating costs rose 47 percent, with costs accelerating this year. We appreciate that Congress increased LIHEAP to nearly $2.6 billion for FY 2008, but unmet need is still very great. Increased LIHEAP funding could be distributed quickly and would help families cope with huge increases in home energy costs.

Congressional leadership to craft an effective stimulus plan is urgently needed. Fortunately, the elements that provide the most economic gain will also serve to reduce hardship and to invest in education, health and job creation – all outcomes that will help in the short and long terms. We strongly urge Congress to enact a package with the elements outlined above, and to reject proposals for permanent tax breaks that provide little or no stimulus at great cost.

Sincerely,

ACORN
AFL-CIO
AFSCME
American Federation of Government Employees, AFL-CIO
American Friends Service Committee
American Network of Community Options and Resources
Americans for Democratic Action, Inc.
Association of Farmworker Opportunity Programs
Bread for the World
Campaign for America's Future
Center for Community Change
Child Welfare League of America
Coalition on Human Needs
Common Cause
Community Action Partnership
Easter Seals
Evangelical Lutheran Church in America
Families USA
Food Research & Action Center (FRAC)
Lutheran Services in America
National AIDS Housing Coalition
National Association for State Community Services Programs
National Association of County Behavioral Health and Development
National Association of Social Workers
National Benedictines For Peace
National Center for Law and Economic Justice
National Coalition for Asian Pacific American Community Development
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National Education Association
National Head Start Association
National Health Care for the Homeless Council
National Immigrant Solidarity Network
National Low Income Housing Coalition
National Network of Abortion Funds
National Poverty Engine
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National Rehabilitation Association
National Research Center for Women & Families
National WIC Association
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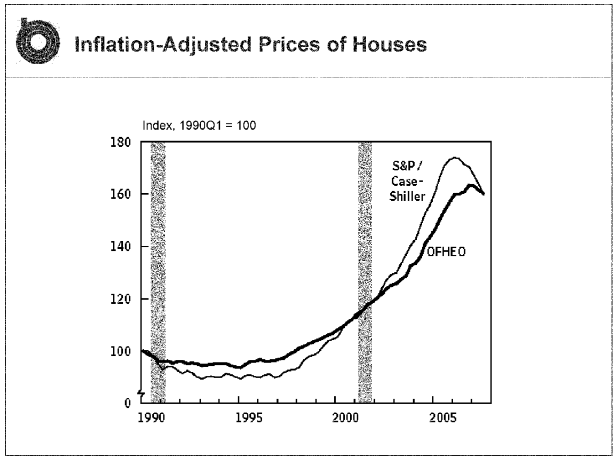
Dr. Orszag, thank you again for coming. We look forward to your testimony.

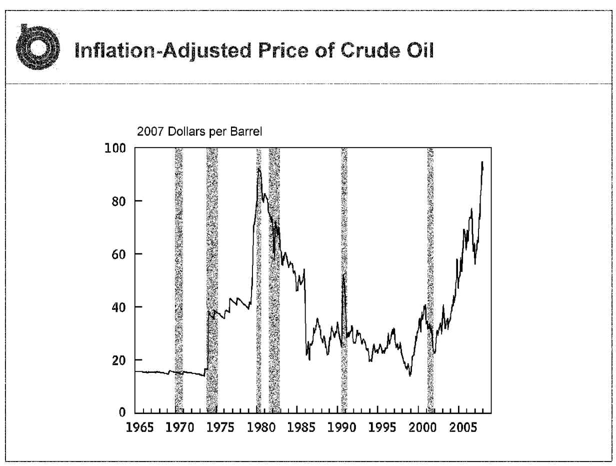
STATEMENT OF PETER P. ORSZAG, DIRECTOR, CONGRESSIONAL BUDGET OFFICE

Mr. ORSZAG. Mr. Spratt, Mr. Ryan, members of the committee, my testimony this morning will focus on the economic and budget outlook. First, the economy has been buffeted by several interlinked shocks, and the risk of recession is significantly elevated relative to normal economic conditions.

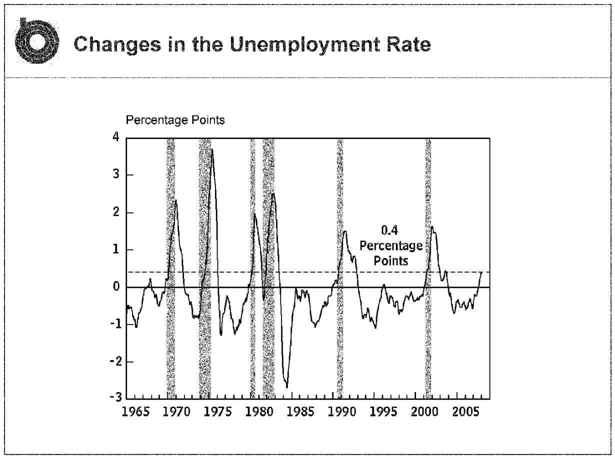


As my first chart shows, there was a dramatic run-up in housing prices during the first half of this decade, but housing prices have started to decline, and most forecasters expect further drops this year. The weakening of the housing sector directly affects the economy by reducing residential investment and indirectly affects the economy through reduced consumer spending as a result of lower housing wealth.

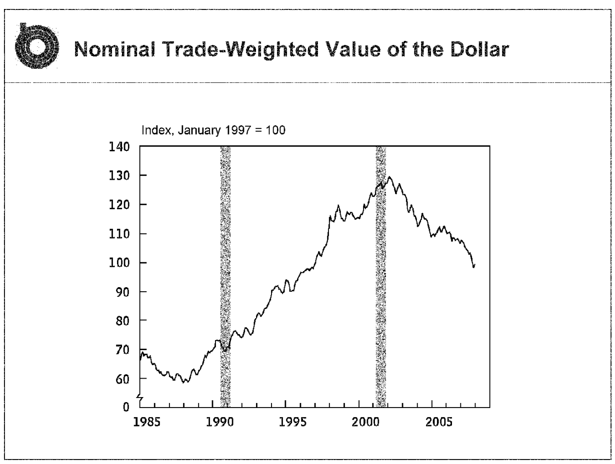
Moreover, problems in the housing markets and mortgage markets have spilled over into broader turmoil in financial markets which poses the risk of impeding the flow of credit essential to a modern economy.



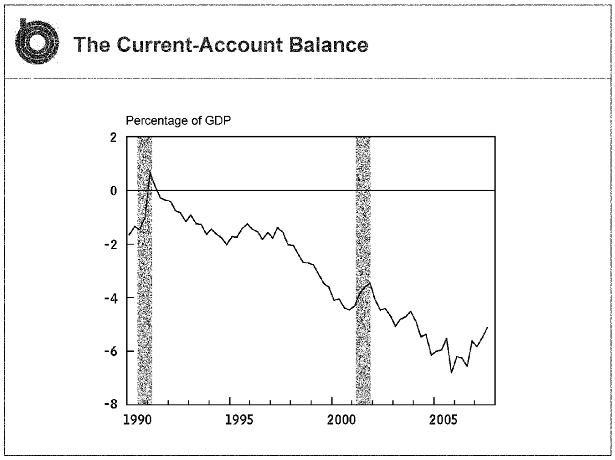
Energy prices have also risen substantially as the next chart shows. Although the effect of an increase in the price of oil on the macroeconomy today is smaller than it was in the 1970s and 1980s, the rise in oil prices is still an economic drag. The combination of these forces has not yet fully manifested, themselves; although the unemployment rate has ticked up. Indeed, as the next chart shows, the 3-month moving average unemployment rate has now risen 0.4 percentage points, almost a half a percentage point, above its level relative to the same period last year, which as you can see from the graph has only and always occurred in periods associated with a recession, which are those dark bars in the graph. You can see that the only times that we have crossed that 0.4 percentage point horizontal line is during those dark bars, which are recessions.



On the other hand, other measures of the labor market that have typically accompanied such a large increase in the unemployment rate at the onset of a recession have not behaved as they have in the past. For example, unemployment insurance claims typically spike up at the beginning of a recession, and they have not done so thus far in recent experience.



Especially with the most recent and notable action by the Federal Reserve yesterday, many professional forecasters are projecting continued, albeit sluggish, economic growth in 2008 rather than an outright recession. And one force leading to that conclusion has been net exports. Thus far, as the next chart shows, the depreciation of the dollar, which is a necessary part of the gradual adjustment of our current account deficit, has itself been gradual, and that has helped to stabilize and, along with growth abroad, even slightly improve the current account deficit, which is shown in the next chart. That force has—and rapid growth in real exports is helping to provide a cushion or a boost to the economy.



The bottom-line is that the risk of recession is substantially elevated, but CBO expects, along with most professional forecasters, a period of unusually weak growth rather than outright recession. In particular, CBO expects growth for the year as a whole of under 2 percent, as the next chart shows, and a rise in the unemployment rate to an average of 5.1 percent during 2008.

CBO's Economic Projections for Calendar Years 2008 to 2018

Percentage Change

	Estimated	Forecast		Projected Annual Average	
	2007	2008	2009	2010–2013	2014–2018
Nominal GDP					
Billions of dollars	13,828	14,330	14,997	18,243	22,593
Percentage change	4.8	3.6	4.7	5.0	4.4
Real GDP	2.2	1.7	2.8	3.1	2.5
PCE Price Index	2.5	2.6	1.8	1.9	1.9
Unemployment Rate (Percent)	4.6	5.1	5.4	4.9	4.8

A reflection of this general slowing in economic activity can be seen in job growth. In 2005, job growth averaged 220,000 per month. It fell in half last year to an average of 110,000 per month. CBO projects that during the first half of 2008, it will fall in half yet again to an average of 55,000 per month during the first half of this year.

Average Annual Growth Rates of Revenues Since 1997 and in 2008 in CBO's Baseline

Percent

	Actual		Estimated
	1997–2006	2007	2008
Individual Income Taxes	4.7	11.5	4.1
Corporate Income Taxes	7.5	4.6	-1.7
Social Insurance Taxes	5.1	3.8	4.6
Other	4.0	-4.2	3.1
Total Revenues	5.2	6.7	3.4
Memorandum:			
Consumer Price Index	2.6	2.3	3.2
Nominal GDP	5.4	4.6	3.9

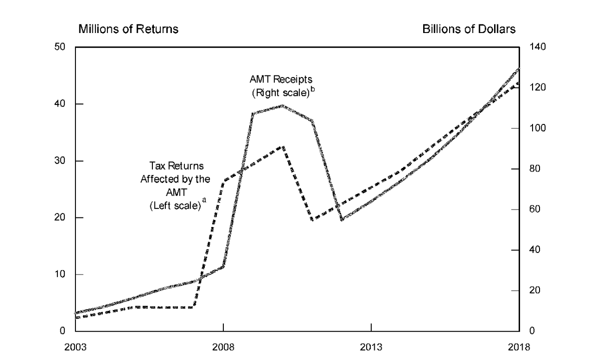
Let me now turn to the budget outlook. As a result of the slowing economy, we have already seen some slowing of revenue growth, as the next chart shows, especially in corporate income taxes. And CBO expects some further slowing this year. Indeed we expect corporate income taxes to decline in nominal terms this fiscal year relative to last year. We now have information for corporate tax receipts during January and project that again in January we will have a year-over-year decline in corporate tax receipts—the seventh month in a row in which that occurred. This is particularly notable because a lot of the fiscal improvement between 2003 and 2006/7 occurred because of a very sharp rise in corporate income tax revenue.

Total Deficit or Surplus Under CBO's Baseline

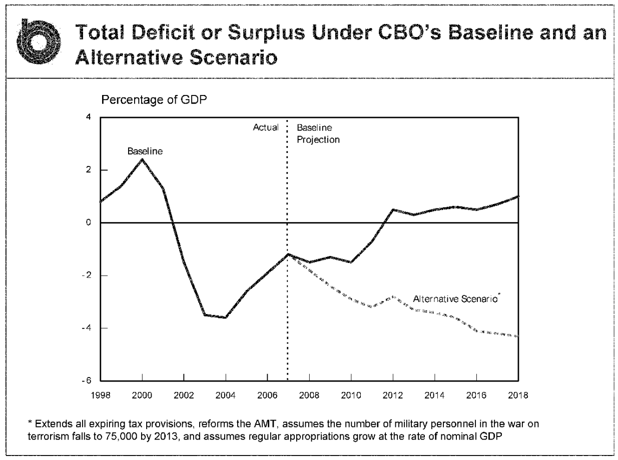
	Actual 2007	2008	2009	2010	2011	2012	2013	Total, 2009–2018
Percentage of GDP	-1.2	-1.5	-1.3	-1.5	-0.7	0.5	0.3	0.1
Billions of Dollars	-163	-219	-198	-241	-117	87	61	274

Our baseline suggests that after 3 years of declining deficits, a slowing economy will boost the deficit to $219 billion this year, as the next chart shows, which amounts to 1.5 percent of GDP or 1.5 percent of the economy, which is up from 1.2 percent last year. If policymakers fund the additional appropriations for Iraq and Afghanistan that the administration has requested, that deficit would rise to—this year to about $250 billion. And if policymakers adopted some fiscal stimulus measures, the deficit this year could rise significantly above that. And indeed, at least from the perspective of short-term stimulus, that would be one of the objectives of providing such stimulus. Thereafter, under our baseline, which assumes a growing impact of the alternative minimum tax and the expiration of the 2001 and 2003 tax legislation, the budget moves towards balance in 2012.

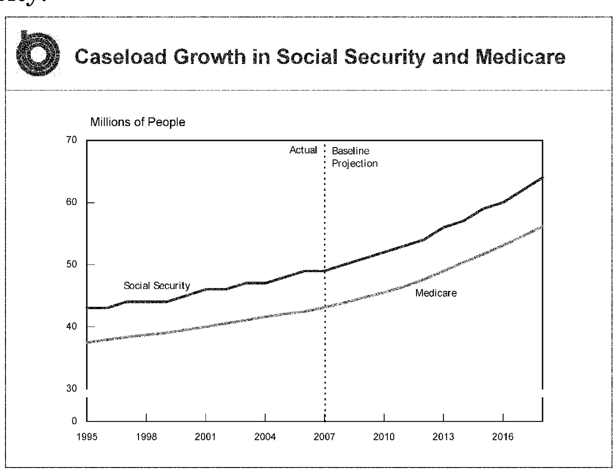
Effects of the Individual Alternative Minimum Tax in CBO's Baseline



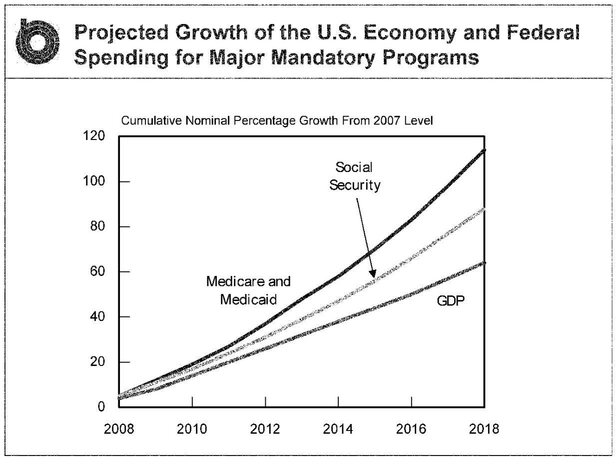
However, as both Mr. Spratt and Mr. Ryan have already noted, that baseline is often viewed as being unrealistic because policy changes that are widely viewed as likely to occur are not incorporated into it. In particular, for example, the baseline assumes no further relief from the alternative minimum tax and, therefore, that the number of taxpayers on the alternative minimum tax will rise from 4 million last year to 26 million this year and continue rising thereafter as you can see on the chart. If, instead of making that assumption, you assumed relief from the AMT was continued, you assume that the 2001 and 2003 tax legislation is continued past its official expiration in 2010, that you adopt one of the scenarios we have put together for the future war—global war on terrorism and you assume that discretionary spending keeps pace with economic growth and not just inflation, the next chart shows you that you get a much different path for the projected deficit than what the baseline shows. And indeed, under that scenario, the cumulative deficit, instead of being a surplus of $274 billion between 2009 and 2018 under our baseline, would show a deficit of $6.3 trillion or about 3.5 percent of GDP.



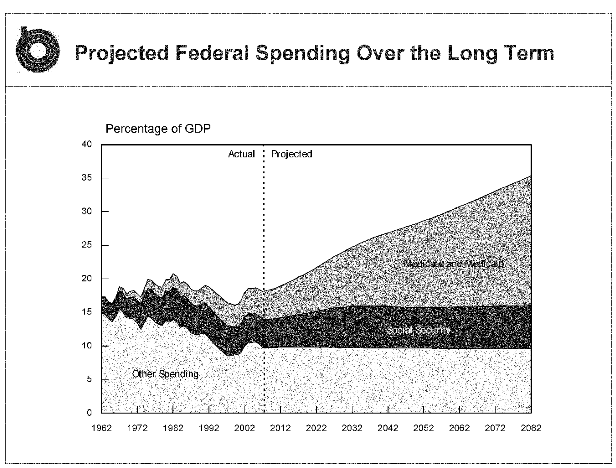
So many of the policy changes that are under discussion clearly have a fairly significant effect on budget projections over the next 10 years. Even over the next 10 years, furthermore, the nation's longer-term budget pressures begin to manifest themselves. Caseloads on both Medicare and Social Security are projected to rise, as the next chart shows. Social Security beneficiaries, for example, rise from 50 million in 2008 to 64 million in 2018 as the first wave of the baby boomer generation becomes eligible for Social Security retirement benefits. Projected increases in caseloads, however, only account for about 30 percent of the growth in mandatory spending over the next decade. More fundamentally, the cost per beneficiary in Medicare is projected to continue rising rapidly, more rapidly than income. And you can see a significant difference even over the next decade, as the next chart shows, in the growth of Medicare and Medicaid spending, which is being driven by those rising health care costs, and the growth in Social Security, even though the increase in beneficiary roles is similar under Medicare and Social Security.



Those projections continue, as the next chart shows, under our long-term budget projections that we released in December. And the conclusion is reinforced even more dramatically that that light blue area, Medicare and Medicaid spending in particular, is the key to our fiscal future. And we project, under our long-term budget projections, that Medicare and Medicaid spending under current law would rise from about 4.5 percent of the economy today to almost 20 percent of the economy by 2082 without a change in policy.



If you combine those spending projections with a revenue path that takes the 2007 tax parameters and projects that forward, you can combine them into what is called the fiscal gap, which is the— basically the summarized difference between projected spending and projected revenue. And as the next chart shows you, over the next 75 years, that gap amounts to 7 percent of the economy, which is a very large number. What that tells you is that you would need to raise taxes or cut spending by 7 percent of GDP—and remember that both of those are about 20 percent now—in order to avoid a significant and unsustainable increase in government debt over the next 75 years.



Most of that increase is not due to demographics, as the next figure shows. The bottom blue bars there are the pure effects of an aging population. And while that is important, by far a more important factor is the rate as which health care costs are growing. That is the single most important variable affecting our long-term fiscal future.

Finally, given the short-term economic difficulties that we face and the very serious long-term fiscal imbalances that I have just highlighted, let me end briefly by discussing the report that CBO wrote for this committee and the Senate Budget Committee on fiscal stimulus options. In particular, when the economy is experiencing unusual weakness, as it appears to be today, the key constraint on economic growth is demand for the goods and services that firms could produce with existing resources. In most circumstances, by contrast, and certainly over the long term, the key constraint on economic growth is the rate at which those resources are expanded through forces like increases in capital and workforce, labor and improvements in productivity. When the constraint on short-term economic growth—on growth is aggregate demand—and again, those kinds of periods are unusual—both monetary and fiscal policy can help by boosting spending.

On the fiscal policy side, the automatic stabilizers built into the budget will help to attenuate any economic downturn by providing a cushion to after-tax income. The question is whether additional fiscal action is necessary. One way to think about it is that fiscal stimulus can help provide insurance against the risk and severity of a possible recession. Our estimates suggest that stimulus of between a half and 1 percent of GDP or so—that is roughly $75 to $150 billion or so—would reduce the elevated risk of recession to more normal levels as long as the stimulus is well designed.

And that brings me to design questions. The stimulus need not be targeted at what caused the economic weakness in the first place. Instead, the key is that it bolsters aggregate demand and thereby helps to jump start a positive cycle of increased demand leading to increased production until the constraint once again becomes how much we are willing to produce or how much we can produce rather than how much we are willing to spend. We laid out some principles that can help guide policymakers interested in designing a package in as cost effective manner as possible, and it would have at least three central principles. First, it would be delivered rapidly. You do not want to be delivering additional stimulus to aggregate demand after the economy is already growing rapidly because all you would succeed in doing is stoking inflationary pressures and you would miss the period in which economic weakness was the key constraint on growth. Second, it would be temporary. As I just mentioned, we face a very serious long-term fiscal imbalance, and one would want to avoid exacerbating that long-term fiscal gap. And finally, it would be cost effective in the sense of boosting aggregate demand as much as possible at a given budgetary cost. And our report to this committee and the Senate Budget Committee evaluated various options according to that criterion also.

Thank you very much, Mr. Chairman.

[The prepared statement of Peter R. Orszag follows:]

The Budget and Economic Outlook: Fiscal Years 2008 to 2018

Chairman Spratt, Ranking Member Ryan, and Members of the Committee, thank you for giving me the opportunity to present the Congressional Budget Office's (CBO's) outlook for the budget and the economy in fiscal years 2008 to 2018.[1]

CBO projects that after three years of declining budget deficits, a slowing economy this year will contribute to an increase in the deficit. Under an assumption that current laws and policies do not change, CBO projects that the budget deficit will rise to 1.5 percent of gross domestic product (GDP) in 2008 from 1.2 percent in 2007 (see Table 1). Enactment of legislation to provide economic stimulus or additional funding for military operations in Iraq and Afghanistan could further increase the deficit for this year.

The state of the economy is particularly uncertain at the moment. The pace of economic growth slowed in 2007, and there are strong indications that it will slacken further in 2008. In CBO's view, the ongoing problems in the housing and financial markets and the high price of oil will curb spending by households and businesses this year and trim the growth of GDP. Although recent data suggest that the probability of a recession in 2008 has increased, CBO does not expect the slowdown in economic growth to be large enough to register as a recession.[2] Economic performance worse than that suggested in CBO's forecast could significantly decrease projected revenues and increase projected spending. Furthermore, policy changes intended to mitigate the economic slowdown would, by design, tend to increase the budget deficit in the short term.[3]

CBO expects the economy to rebound after 2008, as the negative effects of the turmoil in the housing and financial markets fade. Under the assumptions that govern CBO's baseline, the budget deficit will amount to 1.5 percent of GDP or less each year from 2009 to 2011. Subsequently, the budget will show a small surplus of 0.5 percent of GDP in 2012 and remain near that level each year through 2018 (the end of the current 10-year projection period).

The relatively sanguine outlook suggested by the 10-year baseline projections should not be interpreted as implying that the nation's underlying fiscal condition is sound, both because the United States continues to face severe long-term budgetary challenges and because many observers expect policy changes that would deviate from the current-law baseline over the next decade. Ongoing increases in health care costs, along with the aging of the population, are expected to put substantial pressure on the budget in coming decades; those trends are already evident in the current projection period. Economic growth alone will be insufficient to alleviate that pressure, as Medicare and Medicaid and, to a lesser extent, Social Security require ever greater resources under current law. A substantial reduction in the growth of spending, a significant increase in tax revenues relative to the size of the economy, or some combination of the two will be necessary to maintain the nation's long-term fiscal stability.[4]

1. For further details, see Congressional Budget Office, *The Budget and Economic Outlook: Fiscal Years 2008 to 2018* (January 2008).
2. The National Bureau of Economic Research, which by convention is responsible for dating the peaks and troughs of the business cycle, defines a recession as "a significant decline in economic activity spread across the economy, lasting more than a few months, normally visible in real [inflation-adjusted] GDP, real income, employment, industrial production, and wholesale-retail sales."
3. See Congressional Budget Office, *Options for Responding to Short-Term Economic Weakness* (January 2008).
4. For a detailed discussion of the long-term pressures facing the federal budget, see Congressional Budget Office, *The Long-Term Budget Outlook* (December 2007).

Table 1.

CBO's Baseline Budget Outlook

	Actual 2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Total, 2009-2013	Total, 2009-2018
						In Billions of Dollars								
Total Revenues	2,568	2,654	2,817	2,907	3,182	3,442	3,585	3,763	3,941	4,131	4,334	4,548	15,933	36,649
Total Outlays	2,731	2,873	3,015	3,148	3,299	3,355	3,524	3,666	3,824	4,037	4,183	4,325	16,341	36,376
Total Deficit (-) or Surplus	**-163**	**-219**	**-198**	**-241**	**-117**	**87**	**61**	**96**	**117**	**95**	**151**	**223**	**-408**	**274**
On-budget	-344	-414	-396	-450	-343	-151	-184	-154	-136	-160	-102	-27	-1,525	-2,104
Off-budget[a]	181	195	198	210	226	238	244	251	254	254	253	249	1,117	2,378
Debt Held by the Public at the End of the Year	5,035	5,232	5,443	5,698	5,827	5,751	5,701	5,613	5,503	5,414	5,269	5,050	n.a.	n.a.
						As a Percentage of Gross Domestic Product								
Total Revenues	18.8	18.7	19.0	18.6	19.3	19.9	19.9	20.0	20.0	20.1	20.2	20.3	19.4	19.8
Total Outlays	20.0	20.2	20.4	20.2	20.1	19.4	19.5	19.4	19.4	19.7	19.5	19.3	19.9	19.7
Total Deficit (-) or Surplus	**-1.2**	**-1.5**	**-1.3**	**-1.5**	**-0.7**	**0.5**	**0.3**	**0.5**	**0.6**	**0.5**	**0.7**	**1.0**	**-0.5**	**0.1**
Debt Held by the Public at the End of the Year	36.8	36.8	36.7	36.5	35.4	33.3	31.6	29.8	28.0	26.4	24.6	22.6	n.a.	n.a.
Memorandum:														
Gross Domestic Product (Billions of dollars)	13,670	14,201	14,812	15,600	16,445	17,256	18,043	18,856	19,685	20,540	21,426	22,355	82,156	185,018

Source: Congressional Budget Office.

Note: n.a. = not applicable.

a. Off-budget surpluses comprise surpluses in the Social Security trust funds as well as the net cash flow of the Postal Service.

CBO's baseline budget projections for the next 10 years are not a forecast of future outcomes; rather, they are based on the assumption that current laws and policies remain the same. The projections stem from long-standing procedures that were, until recently, specified in law, and they serve as a benchmark that lawmakers and others can use to assess the potential impact of future policy decisions.[5] Following those procedures generates deficits and surpluses in the baseline that are predicated on two key projections:

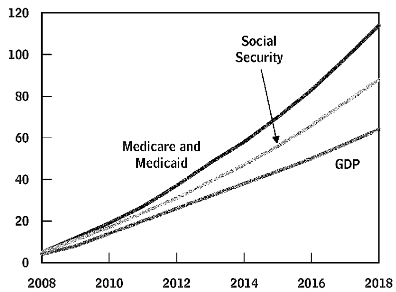
- That revenues will rise from 18.7 percent of GDP this year to almost 20 percent of GDP in 2012 and then remain near that historically high level through 2018. Much of the projected increase in revenues results from the growing impact of the alternative minimum tax (AMT) and, even more significantly, the expiration at the end of 2010 of various provisions originally enacted in the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) and the Jobs and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA).
- That outlays for discretionary programs (those whose spending levels are set anew each year through appropriation acts) will decline from 7.6 percent of GDP last year to 6.1 percent by 2018—a lower percentage than any recorded in the past 40 years. Such a projection derives mainly from the assumption in the baseline that discretionary funding will grow at the rate of inflation, which is lower than the growth rate that CBO projects for nominal GDP. Implicit in the projection for discretionary spending is an assumption that no additional funding is provided for military

5. The Balanced Budget and Emergency Deficit Control Act of 1985, which established rules that have governed the calculation of CBO's baseline, expired on September 30, 2006. Nevertheless, CBO continues to prepare baselines according to the methodology prescribed in that law.

Figure 1.

Projected Growth of the U.S. Economy and Federal Spending for Major Mandatory Programs

(Cumulative nominal percentage growth from 2007 level)



Source: Congressional Budget Office.

operations in Iraq and Afghanistan in 2008 and that future appropriations for activities related to the war on terrorism remain equivalent, in real (inflation-adjusted) terms, to the $88 billion appropriated so far this year.

Policy choices that differ from the assumptions in the baseline would produce different budgetary outcomes. For example, if lawmakers continued to provide relief from the AMT (as they have done on a short-term basis for the past several years) and if the provisions of EGTRRA and JGTRRA that are scheduled to expire were instead extended, total revenues would be $3.6 trillion lower over the next 10 years than CBO now projects. Similarly, if discretionary spending (other than that for military operations in Iraq and Afghanistan and other spending labeled as emergency) grew at the rate of nominal GDP over the next 10 years, total discretionary outlays during that period would be about $1.4 trillion higher than in the baseline. Combined, those policy changes—and associated debt-service costs—would produce a deficit of $402 billion (2.3 percent of GDP) in 2012 and a cumulative deficit of $5.7 trillion (3.1 percent of GDP) over the 2009–2018 period.

The Budget Outlook

CBO estimates that if today's laws and policies did not change, federal spending would total $2.9 trillion in 2008 and revenues would total $2.7 trillion, resulting in a budget deficit of $219 billion. That deficit could increase significantly if legislation is enacted to provide economic stimulus—as is currently under consideration. Furthermore, additional funding that is likely to be needed to finance military operations in Iraq and Afghanistan could add $30 billion to outlays this year.

Baseline Projections for the 2009–2018 Period

According to CBO's projections, under current laws and policies the deficit will drop slightly in 2009, to $198 billion. That decrease results primarily from two factors. On the revenue side of the budget, receipts from the AMT are estimated to increase by about $75 billion next year, largely because of the scheduled expiration of the relief provided through tax year 2007. On the spending side of the budget, outlays for military operations in Iraq and Afghanistan are about $10 billion lower in 2009 than in 2008 under the assumptions of the baseline.

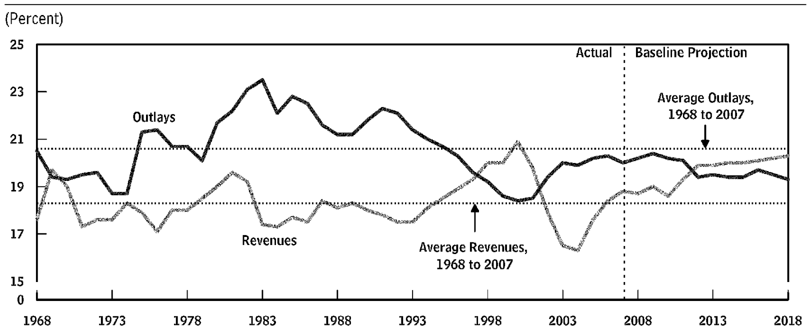
The deficit is projected to rise modestly in 2010, as outlays grow by about 4.4 percent and revenues increase by about 3.2 percent. That projected growth rate for revenues is lower than in recent years, mainly because of a projected slowdown in corporate tax receipts (to a level that is more consistent with their historical relationship to GDP).

After 2010, spending related to the aging of the baby-boom generation will begin to raise the growth rate of total outlays. The baby boomers will start becoming eligible for Social Security retirement benefits in 2008, when the first members of that generation turn 62. As a result, the annual growth of Social Security spending is expected to accelerate from about 5.1 percent in 2008 to 6.4 percent by 2018.

More important, because the cost of health care is likely to continue rising rapidly, spending for Medicare and Medicaid is anticipated to grow even faster—generally in the range of 7 percent to 8 percent annually. Total outlays for those two health care programs are projected to more than double during the baseline period, increasing by 114 percent, while GDP is projected to grow somewhat more than half as fast, by 64 percent (see Figure 1). Under the assumptions underlying CBO's baseline, spending for Medicare and Medicaid will rise to

Figure 2.

Total Revenues and Outlays as a Percentage of Gross Domestic Product



Source: Congressional Budget Office.

5.9 percent of GDP in 2018, compared with about 4.6 percent this year, and spending for Social Security will rise to 4.9 percent of GDP from 4.3 percent this year.

Revenues are projected to increase sharply after 2010 under the assumption that various tax provisions expire as scheduled. In the baseline, total revenues grow by 9.4 percent in 2011 and by 8.2 percent in 2012, thereby bringing the budget into surplus. Beyond 2012, revenues are projected to grow at roughly the same pace as outlays (between 4 percent and 5 percent a year), keeping the budget in the black through 2018.

Outlays over the 2009–2018 period are projected to range between 19.3 percent and 20.4 percent of GDP under the assumptions of the baseline—somewhat lower than the 20.6 percent average of the past 40 years (see Figure 2). Mandatory spending (funding determined by laws other than annual appropriation acts) is projected to grow by nearly 6 percent a year over that period, which is faster than the economy as a whole. By contrast, discretionary appropriations are assumed simply to keep pace with inflation and, to a lesser extent, with the growth of wages. Thus, discretionary outlays are projected to increase by about 2.2 percent a year, on average, or less than half as fast as nominal GDP.

In CBO's projections, revenues average 18.8 percent of GDP in 2009 and 2010 (close to the 18.7 percent level expected for this year) before the sharp jump in 2011 and 2012 with the expiration of tax provisions originally enacted in EGTRRA and JGTRRA. After that, revenues continue growing faster than the overall economy for three reasons: increases in total real income combined with the progressive structure of the tax code, the increasing reach of the AMT, and taxable withdrawals of retirement savings as the population ages. Under the assumptions used for the baseline, CBO projects that revenues will equal 20.3 percent of GDP by 2018—a level reached only once since World War II.

Federal government debt that is held by the public (mainly in the form of Treasury securities sold directly in the capital markets) is expected to equal about 37 percent of GDP at the end of this year. Thereafter, the baseline's projections of short-term deficits followed by emerging surpluses diminish the government's need for additional borrowing, causing debt held by the public to shrink to 22.6 percent of GDP by 2018.

Changes in the Baseline Budget Outlook Since August

The budget outlook for 2008 has deteriorated somewhat since CBO issued its previous projections in August, but the pattern of deficits and surpluses in the outlook for the

Table 2.

CBO's Economic Projections for Calendar Years 2008 to 2018

(Percentage change)

	Estimated	Forecast		Projected Annual Average	
	2007	2008	2009	2010-2013	2014-2018
Nominal GDP					
Billions of dollars	13,828	14,330	14,997	18,243 [a]	22,593 [b]
Percentage change	4.8	3.6	4.7	5.0	4.4
Real GDP	2.2	1.7	2.8	3.1	2.5
GDP Price Index	2.5	1.9	1.8	1.9	1.9
PCE Price Index[c]	2.5	2.6	1.8	1.9	1.9
Core PCE Price Index[d]	2.1	1.9	1.9	1.9	1.9
Consumer Price Index[e]	2.8	2.9	2.3	2.2	2.2
Core Consumer Price Index[f]	2.3	2.2	2.2	2.2	2.2
Unemployment Rate (Percent)	4.6	5.1	5.4	4.9	4.8
Interest Rates (Percent)					
Three-month Treasury bills	4.4	3.2	4.2	4.6	4.7
Ten-year Treasury notes	4.6	4.2	4.9	5.2	5.2

Sources: Congressional Budget Office; Department of Commerce, Bureau of Economic Analysis; Department of Labor, Bureau of Labor Statistics; Federal Reserve Board.

Notes: GDP = gross domestic product; PCE = personal consumption expenditure.

Percentage changes are measured from one year to the next.

Year-by-year economic projections for 2008 to 2018 appear in Appendix E.

a. Level in 2013.

b. Level in 2018.

c. The personal consumption expenditure chained price index.

d. The personal consumption expenditure chained price index excluding prices for food and energy.

e. The consumer price index for all urban consumers.

f. The consumer price index for all urban consumers excluding prices for food and energy.

following 10 years is about the same.[6] At $219 billion, the deficit projected for 2008 is $64 billion higher than what CBO estimated in August. Because the August projections already reflected some expected slowing of the economy in 2008, most of that difference stems from legislation that extended relief to individuals from the AMT for one year.

For the 2009–2017 period, the baseline's bottom line has improved slightly, compared with CBO's projections in August. In the current baseline, projected revenues are lower, mostly as a result of lower estimates of corporate profits. Projected outlays are also lower, primarily because of the use of partial-year funding for military operations in Iraq and Afghanistan; this baseline extrapolates the $88 billion appropriated thus far for 2008, whereas the August baseline extended the entire funding provided for 2007 (about $170 billion). With the effect of partial-year funding excluded, the current baseline would show an increase in the cumulative deficit for 2008 through 2017 of more than $850 billion (0.5 percent of GDP).

6. Those projections were published in Congressional Budget Office, *The Budget and Economic Outlook: An Update* (August 2007).

The Economic Outlook

Underlying CBO's baseline projections is a forecast that U.S. economic growth will slow in calendar year 2008 but pick up in 2009. Specifically, CBO anticipates that GDP will grow by 1.7 percent in real terms for 2008 as a whole, about half a percentage point less than the growth recorded last year. For 2009, CBO forecasts that GDP growth will rebound to 2.8 percent (see Table 2).

Problems in the housing and financial markets, along with high oil prices, triggered much of the recent slowdown. Between mid-2006 and the end of 2007, residential investment (which includes the construction of new housing units, improvements to existing units, and brokers' commissions) declined, but the drop was largely offset by growth in both consumer spending and business fixed investment (businesses' spending on structures, equipment, and software). Those two sectors are unlikely to provide as much support to economic growth this year. Residential investment is expected to continue to decline through much of 2008; in addition, the growth of consumer spending, sustained thus far by solid growth in people's real income as well as by their borrowing and use of savings, is likely to fall off, curtailed by a drop in housing wealth (home equity), increased costs for borrowing, the high price of oil, and slower growth of real income. The resulting weak domestic demand for goods and services in turn is expected to slow the growth of business fixed investment, which is likely to further diminish the pace of overall economic growth this year.

In contrast, the relative economic strength of the United States' major trading partners—in particular, developing countries with emerging market economies—when combined with the dollar's decline will partially offset the sluggishness in domestic demand expected in 2008 and support U.S. economic growth by stimulating exports. Emerging economies have become increasingly less dependent on demand in the United States to fuel their expansions and, as a result, have become less vulnerable to slowdowns in U.S. economic growth. Moreover, the pace of the decline begun in 2002 in the value of the dollar relative to the currencies of major trading partners—which helps make U.S. exports less expensive—has quickened. Those developments, accompanied by less domestic demand for imports, are likely to reduce the U.S. current-account deficit (broadly, the summary measure of the United States' trade with the rest of the world).

Inflation (as measured by the year-to-year change in the price index for personal consumption expenditures) is likely to be about the same this year as last year; in 2009, CBO forecasts, the rate will fall, to 1.8 percent, as inflation in energy and food prices eases. The unemployment rate, which was 4.6 percent last year, will average 5.1 percent in 2008 and reach 5.3 percent by the end of the year, CBO estimates. Interest rates on Treasury securities are expected to remain low this year and to increase in 2009 as the economy works through and emerges from its current difficulties. In CBO's forecast, the rate on 3-month Treasury bills averages 3.2 percent in 2008 and moves higher, to 4.2 percent, in 2009. Similarly, the rate on 10-year Treasury notes moves from an average of 4.2 percent in 2008 to 4.9 percent in 2009.

For 2010 to 2018, CBO projects that real growth will average 2.7 percent and the personal consumption expenditure price index, 1.9 percent. CBO also projects that in the latter years of the projection period, the unemployment rate will average 4.8 percent and that the interest rates on 3-month Treasury bills and 10-year Treasury notes will average 4.7 percent and 5.2 percent, respectively.

Chairman SPRATT. Let me start with what is in the context of what is happening right now, relatively good news, and ask you how confident you feel about it. You are projecting, as I understand, 1.7 percent real growth in GDP for this year. Are you comfortable with that projection?

Mr. ORSZAG. For the year as a whole, yes. We have weaker growth in the first half of the year, somewhat stronger growth in the second half of the year. I would note that that projection is below the most recent Blue Chip forecast. It is below a somewhat older administration forecast. We will continue to monitor economic conditions and adjust our thinking as warranted. But at this point, I would not—I would not adjust that.

Chairman SPRATT. Let me also go back to where we were at the outset of your testimony in trying to explain that this is a baseline budget projection and read what you say on the first page, just for reiteration: CBO's baseline budget projections for the next 10 years are not a forecast of future outcomes; they are based on the assumption that current laws and policies will remain the same. The projections themselves stem from long-standing procedures that were, until recently, made law—part of the law.

In other words, you are saying that you are not trying to predict the future here. You are taking the existing situation, assuming they will be carried forward into the future at least 5 years—in some cases 10 years—and showing us the cumulative and aggregate effects of that assumption?

Mr. ORSZAG. That is correct. This baseline is useful for legislative purposes for evaluating the cost of legislative changes relative to the baseline. But it is not a prediction of the future because policy will change.

Chairman SPRATT. Let's take the adjustments for the alternative scenario that you referred to in your testimony and lay out in your book. First of all, with respect to tax cuts, if we assume that the tax cuts that were affected—enacted in '01 and '03 were renewed and carried forward after expiring on December 31, 2010, what is the effect on the bottom-line of your budget?

Mr. ORSZAG. There is a roughly $2.2 trillion revenue effect from those provisions, and then there is also an interaction with the alternative minimum tax.

Chairman SPRATT. Okay. We will come back to the interaction then.

How about other extenders, not those that were enacted in '01 but tax provisions like the revenue—the research and development tax credit? If these are extended as they typically are, what is the impact on revenue of extending these tax measures—tax cut measures?

Mr. ORSZAG. $481 billion over the 10-year window.

Chairman SPRATT. $481 billion. Now the AMT, the alternative minimum tax, we fixed for 2 or 3 years running, and there seems to be a consensus in both parties amongst us all that it should not be applied to middle income taxpayers for whom it was never intended in the first place and comes down on pretty heavily. If we fix it to lock in place its current impact so that it affects 4 to 5 percent of all tax filers but no more, what is the impact on revenues of fixing the AMT in that fashion?

Mr. ORSZAG. Approximately $650 billion. And then, as I mentioned before, if you did that and also extended the 2001 and 2003 tax legislation, there is an additional $550 billion interaction effect.

Chairman SPRATT. Now, there are some other things that we are doing year to year as we try to find room in the budget for doing permanent solutions. One is a sustainable growth rate factor under physicians' reimbursement, under Medicare. Could you give us a rough back-of-the-envelope estimate of what it would cost if we were to simply dispense with that or at least mitigate its effect so it doesn't apply in the future years?

Mr. ORSZAG. Yes, it is a couple hundred billion dollars. But let me get you the exact figure in a second. Depending on how you did it, it would be somewhere between $250 and $325 billion. And, in fact, it could be slightly larger than that if you also held Medicare beneficiaries harmless from the increase in their Part B premiums that would follow.

Chairman SPRATT. Okay. Now, with respect to spending that we have the most control over, which we call NDD, nondefense discretionary spending, you have assumed, in my opinion, fairly stringent conditions for the growth of this spending over the next 5 to 10 years. You are assuming in your forecast that it will grow with the rate of inflation but not with the rate of GDP. Over 5 years, what is the impact of that on negative cumulative NDD, nondefense discretionary spending?

Mr. ORSZAG. I actually have the figure for total discretionary spending. We can get it for the split. For total discretionary spending over 10 years, it is approximately $1.4 trillion.

Chairman SPRATT. Okay. So you have already squeezed that much spending——

Mr. ORSZAG. You can divide that roughly in half.

Chairman SPRATT. Okay. You squeeze that much spending out of NDD. What about the war in Iraq and Afghanistan? What assumption do you make about its cost?

Mr. ORSZAG. The baseline takes whatever has been enacted as of our projections and projects that forward. So we have $88 billion in enacted appropriations for the war on terrorism, and that is spent out and projected forward in the baseline.

Chairman SPRATT. So the administration requested in a special supplemental $193 billion. Of that, $88 billion has been provided and appropriated thus far. That leaves 105 to go if the administration's full request is appropriated. You are backing both of those out? You are leaving the 88 in for 2008——

Mr. ORSZAG. Correct.

Chairman SPRATT. And assuming that the 105 will be forthcoming?

Mr. ORSZAG. No, sir. If the $105 billion occurs, there would be roughly another $30 billion in outlays that—in other words, if you provided another roughly $100 billion this year, about $30 billion would be spent this year with the remainder being spent largely next year. And that was the difference between our baseline deficit of $219 billion. If you provided the extra $105 or roughly $100 billion that the administration has requested, about $30 billion would spend out this year. That would bring the deficit to about $250 billion.

Chairman SPRATT. I think you have got a net sum impact of $981 billion for your baseline assumption—your modeled assumption about the cost of Iraq and Afghanistan?

Mr. ORSZAG. That is correct, sir.

Chairman SPRATT. Does that involve building down methodically to a level of about 75,000 troops in the two theaters and then continuing along a steady and safe basis at that level?

Mr. ORSZAG. No. Based on the rules that govern the baseline, you just take what has been enacted and project that forward. We also provide different policy scenarios that you can compare things to, and we do provide one in which the troop levels are reduced to 30,000 by 2010 and another in which they are reduced to 75,000 by 2013. In the scenario in which they are reduced to 75,000 by 2013, there would be an additional $120 billion of increased deficit as a result relative to the $981 billion that you pointed out.

Chairman SPRATT. Let me show you our notorious eye chart. It is back.

Could we get the eye chart on the screen? This tests your visual acuity. That is why we call it the eye chart.

CBO's Budget and Economic Outlook, January 2008

Billions of Dollars	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Total 2009-2018
CBO Baseline	-219	-198	-241	-117	87	61	96	117	95	151	223	274
Remove Repeating Supplemental	---	43	80	102	116	126	135	144	153	163	173	1,234
CBO Baseline w/o repeating supp	-219	-155	-161	-15	203	187	231	261	248	313	395	1,507
Bush Agenda												
Fiscal Stimulus	-116	-29										-29
Extend EGTRRA and JGTRRA	-0	-3	-6	-147	-254	-281	-292	-304	-316	-329	-344	-2,277
Extend Other Expiring Tax Provisions	-6	-14	-22	-31	-38	-44	-49	-53	-58	-63	-67	-438
Repair AMT*	-6	-75	-76	-89	-103	-118	-134	-151	-170	-191	-215	-1,322
Ongoing Military Operations	-30	-96	-128	-135	-120	-107	-93	-81	-79	-79	-79	-996
Debt Service	*-2*	*-10*	*-23*	*-40*	*-65*	*-94*	*-126*	*-161*	*-198*	*-239*	*-284*	*-1,240*
Total Changes	-160	-227	-254	-443	-580	-644	-694	-750	-820	-901	-990	-6,304
Resulting Deficits	-379	-382	-415	-457	-377	-458	-463	-489	-573	-588	-595	-4,796
ADDENDUM:												
CBO non-social security baseline deficit w/o repeating supps	-416	-354	-371	-241	-35	-58	-19	7	-7	61	146	-870
Non-social security deficit with additional items	197	199	210	226	238	244	250	253	254	253	249	2,378

Negative items make deficits worse
Baseline estimates assume tax cuts expire as written in law and emergency supplemental funding repeats every year and grows with inflation
*Includes interactive effect with EGTRRA/JGTRRA extension

Mr. ORSZAG. I am glad I got new glasses.

Chairman SPRATT. The main reason we do this is to show you the number we derive here isn't coming off the seat of our pants. We actually did some arithmetic. It may be a bit-back-of-the-envelope-ish, but nevertheless, after doing the things that we just ran through—assuming the renewal of the tax cuts, assuming your assumption about modeling the cost of continuing missions in Iraq and Afghanistan, assuming what you assume about NDD and everything—we come up with a net addition to the deficit of $4.7 trillion. I can't even see it myself. I think that is the number, $4.7 trillion.

Mr. ORSZAG. Yes, sir. Rounds to 4.8, but okay.

Chairman SPRATT. Are we in the same ballpark then?

Mr. ORSZAG. Yeah. The scenario that I showed was slightly different. I think—I am not sure that you have discretionary spending growing with GDP there. But in any case, yes, the numbers are, you know, somewhere $4 to $6.5 trillion under these alternative scenarios, depending on exactly what you assume.

Chairman SPRATT. If I picked up your testimony—walked in off the street and picked up your testimony and looked at table 1, I would say that, well, the near term looks a little dire; the bottom line is still pretty substantial, $219 billion this year, which is worse than last year, $163 billion. But by 2012, it appears that the budget will be in the black. But that is based upon some assumptions that are not likely to be obtained politically around here. And when we make those assumptions, instead of having an $87 billion surplus, we could have a 2 or 3 or $400 billion deficit easily by that point in time if we do indeed extend the tax cuts, extend the extenders, continue our mission in Iraq and Afghanistan and make the other policy decisions that are reflected in the total; is that correct?

Mr. ORSZAG. That is correct.

Chairman SPRATT. So it is a pretty dire forecast in that sense?

Mr. ORSZAG. With those set of policy changes—and even the medium-term fiscal outlook is not pretty. And I just come back again to, regardless of whether you use the baseline or an adjusted set of projections for the medium term, the long-term fiscal picture is quite dismal.

Chairman SPRATT. Thank you very much, Sir.

Mr. Ryan.

Mr. RYAN. Doctor—Director Orszag, let me just go with a couple of quick questions first and then some other maybe lengthier ones. In your macroeconomic forecast on GDP growth, I think—in your table 2.1, you have 3.1 percent nominal GDP growth in the first 5 years and then 2.5. In those growth forecasts, do you project any macroeconomic feedback from expiring—the expiration of tax cuts and the and the imposition of AMT?

Mr. ORSZAG. There is, especially after the expiration of the 2001 and 2003 tax legislation, some incorporation of the effects on labor supply.

Mr. RYAN. On labor supply?

Mr. ORSZAG. 2011, 2012.

Mr. RYAN. How does that effect growth, nominal GDP growth projections? Will it increase it or decrease it by much, if any?

Mr. ORSZAG. It has a relatively small effect because there are two offsetting things: Reduced marginal tax rates help to encourage work and that boosts GDP. On the other hand——

Mr. RYAN. So you are saying your GDP numbers don't reflect much change in your projection of economic growth based on the expiration of these tax cuts?

Mr. ORSZAG. They reflect our best estimates of the economic effects, which are small.

Mr. RYAN. Okay. So if we had the largest tax increase in the history of earth, largest tax increase in the history of our country, we don't think it is going to do much to change the economy?

Mr. ORSZAG. Again, there are two offsetting effects. There is the one that you are thinking about.

Mr. RYAN. The practical result, you are saying——

Mr. ORSZAG. On net. At least after—you know, after the system is sort of—after a few years, I would not expect a major—and I want to be clear about what we are comparing. We are comparing a world with larger deficits and tax—a lower level of taxes to a world with smaller deficits but higher revenue.

Mr. RYAN. But in the current law world, which current law says we are going to have about a $4.5 trillion tax increase for 10 years starting in 2010, in that current law world, you don't think it does much to affect the growth of the economy?

Mr. ORSZAG. That is our estimate, yes.

Mr. RYAN. Okay. Thank you. Your forecast on war supplemental spending—and I know you have to just basically peg this. You take—I am trying to understand what this year's baseline is. It is $88 billion in war spending, which is the last bridge fund; is that correct?

Mr. ORSZAG. Yes.

Mr. RYAN. And you carry that out for 10 years and have an inflation adjuster in it as well?

Mr. ORSZAG. Right.

Mr. RYAN. So you are projecting that we are going to spend $88 billion carried out through 2018 with inflation?

Mr. ORSZAG. Well, technically there is—we also have the spendout of previous appropriations that have not yet resulted in outlays. But conceptually, yes. That is correct.

Mr. RYAN. Does that figure include some of the one-time things like MRAD purchases? You know, we are not going to continually buy, you know, $8 billion of MRADs every year. Does that include these sort of one-time purchases in that figure?

Mr. ORSZAG. Yes. Whatever has been appropriated is included; and whatever hasn't, is not.

Mr. RYAN. Okay. Let me turn to this—the talk about a stimulus package. You are hearing a kind of a consensus emerge it seems on both sides of the aisle, both from the administration and leaders of both parties, that it ought to be timely, targeted and temporary, the three Ts. I think that is what—I think former Secretary Summers was the guy who coined that phrase. Is transportation and infrastructure good stimulus based on the three Ts?

Mr. ORSZAG. We ranked infrastructure spending in general as small cost effectiveness, i.e., not good stimulus, because in general those projects do not spend out very rapidly.

Mr. RYAN. What about State fiscal assistance, such as money through a Medicaid program or things like that? Does that—how does that rank in the three Ts?

Mr. ORSZAG. We rank that as medium in terms of cost effectiveness. And the reason is, it depends on what States do with the money. To the extent that providing a dollar to a State causes a State not to raise taxes or not to cut spending, that can turn out to be effective stimulus. But the States currently are in much different fiscal positions. And so to boost the cost effectiveness of State fiscal relief, you would have to target the States experiencing the most fiscal difficulty. And just a general program of fiscal relief would not really do that.

Mr. RYAN. Okay. What about food stamps? Some have advocated food stamp increases are necessary to spur the economy. Won't there be a temptation to make the food stamp increase permanent since that is kind of how we typically treat spending around here? And can it really be designed to be temporary? And is that, in your opinion, a great injection of timely, temporary economic growth?

Mr. ORSZAG. Let me answer that in two different ways. The first is, in terms of short-term stimulus, food stamp benefit increases are relatively cost effective because you can get the money out the door fast and the money will be spent.

You are raising a different set of considerations which are for you and not for me, which is whether it is plausible that having done that you would then reduce the benefit levels back down to their previous levels. My understanding is that that may be somewhat more plausible if it were done at the time when the benefit levels are adjusted each year so that you just don't increase them, for example. But I would have to defer to you on whether that is, from a political economy perspective, is viable.

Mr. RYAN. What about LIHEAP? Is that a good mechanism for fiscal stimulus?

Mr. ORSZAG. In general, no. And the reason is that it is difficult to significantly expand the program rapidly, especially where we are in the winter season. I have seen some proposals that very substantially expand it, and it seemed like they are almost off by a decimal point.

Mr. RYAN. Unemployment assistance, your report notes that extending unemployment assistance—assistance can keep unemployment levels high. Is this an effective way—putting aside the moral component of extending unemployment assistance from the economic standpoint, is this an effective way to address one of our major concerns in a weak economy, high unemployment? Is that a good way to create jobs?

Mr. ORSZAG. From the perspective of short-term stimulus, extending unemployment benefits or raising their level is relatively effective, again, because it gets cash to people who will spend the money quickly. There is a tension, though, as I tried to highlight, between what is good short-term stimulus and what is good long-term economic policy. And those kinds of proposals may illustrate that point clearly because—especially during periods of economic strength, extending unemployment benefits or raising their level does increase the level of unemployment. It is not so clear that that effect holds during periods of economic weakness to the same degree. But that illustrates the tension, something that might be good in terms of boosting an economy when it is weak and getting money out the door and having it spent rapidly may not be what you want to do over the long term.

Mr. RYAN. And then one last thing. The baseline—I am trying to get through the baseline. There is something that I want to get at. The baseline—last month, we passed a—the discretionary spending. We had the omnibus bill. And through yesterday, you—it was scored as the top line being $933 billion. So I think most of us who voted for the omnibus appropriations bill—I am not saying—I actually didn't vote for it. But those of us who watched this process occur believe that we spent $933 billion. However, my understanding is that your baseline report shows an FY 2008 regular nonemergency discretionary top line of $941 billion in budget authority, a difference in $8 billion. And then you inflate off this higher number in making out-year projections. Can you explain why there is an $8 billion difference between the $933 billion number CBO scored for FY 2008 appropriations and the amount you are now showing in your baseline?

Mr. ORSZAG. The difference has to do with changes in mandatory programs that are attached to appropriations bills. In 2008, those changes in mandatory programs, or what is called CHIMPS, totalled $7.8 billion. And that offset the discretionary spending amounts. The gross discretionary spending amounts, even the ones that were offset by those CHIMPS are projected out in our baseline, and they do increase our discretionary outlays over the next decade by about $85 billion.

Mr. RYAN. One of those bigger CHIMPS is highway authority; correct?

Mr. ORSZAG. That is correct.

Mr. RYAN. And when we expire highway authority, is there actually real cash savings to the government when that occurs?

Mr. ORSZAG. The savings are in the scoring process. They show up in the scoring process. But because that activity is actually governed by obligation limits, the practical impact is unclear.

Mr. RYAN. Well, I think I have been liberal with my time. I appreciate your indulgence, Chairman. But I think this is something we ought to look at here in the committee. I think we are plowing some hollow savings into this baseline and inflating from there on out. I understand you have rules that govern the way you do this. But I think this is something that this committee ought to be cognizant of.

Thank you. I yield.

Chairman SPRATT. Mr. Edwards.

Mr. EDWARDS. Thank you.

Dr. Orszag. I know your presentation today is focused on long-term economic and fiscal policy and budgets. But with the nation's eyes attuned to the present economic challenges we face, let me just be clear that—do you basically agree with Chairman Bernanke's testimony before this committee last week that a tax stimulus in the range of $100 to $150 billion could have a significant impact on minimizing or reducing the economic downturn or perhaps even preventing a recession? Is it large enough in a $14 trillion economy to have a significant impact?

Mr. ORSZAG. As I mentioned—I should say, it need not just be tax stimulus, but stimulus in general of about that magnitude, if well designed according to our estimates, would reduce the risk of recession from its elevated levels now to somewhat more normal levels. So in terms of recession insurance, that kind of magnitude, if that is what you wanted to do, would be appropriate.

Mr. EDWARDS. It could be significant. Okay.

Let me adjust to long-term policy. In 1981, the country was told during the Reagan administration we could have it all: We could have tax cuts, defense buildup and balanced budgets. At least David Stockman was honest enough, the architect of that budget proposal, to admit later in a book that he knew that was a dishonest promise to the American people. So what we got were tax cuts, defense buildup, which was positive, but a quadrupling of the national debt, I believe, in just over a decade.

Fast forward two decades later, the country is told essentially the same thing again: We can have massive tax cuts, a balanced budget and even fight a war in Iraq and Afghanistan as we have balanced budgets. The consequence is very similar to what we saw 20 years ago. We fought a war. We had tax cuts, and the promises of balanced budgets were so far off in their mark it is—it is not even a close call.

Let me get the facts on the table. During the Bush administration, this Bush administration, how much has the national debt been increased?

Mr. ORSZAG. The national—the publicly held debt at the end of 2007 was $5.0 trillion; at the end of fiscal year 2000 was $3.4 trillion.

Mr. EDWARDS. So the publicly held debt is $1.6 trillion increased during this administration. And the debt held to the government is a legal debt; isn't it? What is the gross debt today? Is it over $9 trillion?

Mr. ORSZAG. The gross debt is substantially higher, yes.

Mr. EDWARDS. What was—the gross debt today is $9 trillion. When President Bush was sworn in, in 2001, what was the gross national debt of the country?

Mr. ORSZAG. I don't know that I have that number. We will get it to you in a moment.

Mr. EDWARDS. So probably a $2 trillion-plus increase; is that correct?

Mr. ORSZAG. A significant increase, yes.

Mr. EDWARDS. All right. Let me assume it is approximately $2 trillion. What is the average interest on our national debt today? Is it 3 percent, 4 percent? What do we have to pay in interest——

Mr. ORSZAG. Somewhere between 3 and 4.

Mr. EDWARDS. So if we said 4 percent, if my math is correct, 4 percent times 2 trillion is an $80 billion a year cost in interest payments just on the national debt that has been accumulated by the economic promises and policies of the last 7 years.

For the record, Mr. Chairman, I think that is more than we spend on all student loan, Pell grant, public education programs. And now, as a result of these economic policies of the last 7 years, we now face a massive interest payment on the debt. And I think—am I correct that interest payments on the debt are some of the largest expenditures of our Federal Government, out of thousands of Federal programs?

Mr. ORSZAG. They amount to more than $200 billion a year.

Mr. EDWARDS. Now, let me ask you finally, with not much time left, some of those who were the architects of the economic policies that led to—despite their predictions of balanced budgets—a $2 trillion increase of the national debt over the last 7 years, they are saying we ought to make permanent all of the Bush 43 tax cuts. I want to ask your opinion. If we made—Congress today made permanent all of those tax cuts that are presently temporary and they were paid for by borrowing, what would be CBO's projection on what the impact would be on the national deficits and on the future economic growth of the country?

Mr. ORSZAG. As I told Mr. Spratt earlier, the revenue effect from extending the 2001 and 2003 tax legislation over the next 10 years is a reduction of about $2.2 trillion. And then, in addition to that, there is an interactive effect with AMT. So you are looking at, say, $2.5 trillion or so in terms of reduced revenue.

Mr. EDWARDS. Thank you.

Chairman SPRATT. Mr. Barrett of South Carolina.

Mr. BARRETT. Thank you, Mr. Chairman.

Dr. Orszag, thank you for being here today. Very sobering information, but we greatly appreciate it.

I know you talked a little bit about the design of the relief we are talking about—rapid, temporary, cost effective. Ranking Member Ryan talked about targeted, timely and temporary. And you really didn't mention anything specific, but you talked in general terms. If there was a way we could probably do some tax credits to stimulate immediately some, long-term tax policies, some fiscal stuff and also address spending in one package, does that make sense to address all of these areas in some type of stimulus package?

Mr. ORSZAG. Yes, if it is feasible. I think an important factor, though, is that we—we have seen significant reductions in the Federal funds rate and in interest rates with a lag that will start to affect the economy. In the meanwhile, there may be a bit of an air pocket. And the question is whether there can be an intervention that is timely in the meanwhile. So a grand package is desirable. And as I have mentioned, our long-term fiscal picture is not pretty. But there is a question of timing that is also involved.

Mr. BARRETT. I understand. But to address the long-term fiscal soundness of the United States, all three of those need to be addressed; correct?

Mr. ORSZAG. Yes. And, in fact, it would be desirable to do them all together if that were possible.

Mr. BARRETT. Gotcha. Thank you. You talked about health care spending. And one assumption that you and many people talk about is that policy will not change; the United States Government will always provide current levels of Medicare and Medicaid. And when you look at entitlement spending, it is one of the fasting growing. Do you have any thoughts about the relationship between government involvement in the health care system, i.e., a federalized program or anything like that, and the rapid inflating rate of the health care process?

Mr. ORSZAG. Rising health care costs are a problem in general. And if you look over the past several decades, the rate at which health care costs have grown in, say, Medicare has been roughly the same as in the rest of the health care system. I think a lot of the problems that face the public programs, including skewed incentives for providers and for beneficiaries and a lack of information, are also present in the private part of our health system. And the two are kind of interlinked in many ways.

Mr. BARRETT. But is it possible that granting Americans access to all of these could potentially give the demise of these programs, though?

Mr. ORSZAG. We are on an unsustainable path. So something is going to have to give. I don't know what it is. But something has to change.

Mr. BARRETT. Okay. Another assumption CBO makes in its baseline is that the expiration of the tax—of the Bush tax cuts in 2010. And again I know you said this about the taxes, but is it your contention that in order to balance the budget, the only viable solution is to raise taxes at this time?

Mr. ORSZAG. No, sir, I didn't say that, and I think, you know, mathematically, spending is above revenue and you need to bring them back—or projected to be significantly above revenue. You need to bring them back in line. There are many people on the outside who believe that—many analysts who believe that movement on both sides will be necessary. But that is a choice for you to make. And mathematically it can occur on either side.

Mr. BARRETT. So I guess, you know—and my last question is, I just feel like when we talk about the government, we try to be everything to everybody. And spending has to be reined in, in some degree, to bring some fiscal sanity. When you look at all the issues that we are looking with, Dr. Orszag, would you say that the one issue that is probably the most important is the amount of money that we spend as a Congress collectively?

Mr. ORSZAG. For our long-term——

Mr. BARRETT. Long-term fiscal sanity so to speak.

Mr. ORSZAG. Yes. Or—and I would focus it even more specifically on what we spend on health care, how much we are getting in exchange for that and the rate at which that is rising. That really dominates all else over the long term.

Mr. BARRETT. Mandatory spending is what you are saying?

Mr. ORSZAG. Medicare and Medicaid in particular.

Mr. BARRETT. Absolutely.

Thank you, Mr. Chairman.

Chairman SPRATT. Mr. Cooper.

Mr. COOPER. Thank you, Mr. Chairman.

Dr. Orszag, first the short term, as I understand it from your testimony, you are not forecasting a recession or a negative rate of growth; you are forecasting slow growth; right?

Mr. ORSZAG. Again, I would say the risk of recession is significantly elevated, but our central forecast is for weak growth. And I also would note I don't know that it matters that much in terms of thinking about policy whether growth in the first half of the year is plus .5 or minus .5 may not matter that much. I mean, it matters obviously for households, and it matters for other things. But in terms of thinking about policy responses, it may not be a material difference.

Mr. COOPER. In terms of using fiscal policy to try to fine tune the economy so that we will remain in a growth phase of the economy, one of the key variables is how quickly we can get money in people's pockets so that they can spend it. And as I understand it, the IRS is saying we can't possibly get the money there until June or July, and that would mean the money couldn't be spent probably for a couple of months after that. So that is a very remarkable policy lag in terms of implementing any policy; isn't it?

Mr. ORSZAG. Yeah. And let me just pause for a moment on this because I think some people look at the 2001 tax rebate experience and how quickly money went out the door there and conclude things about the current situation which may not work. In particular, at that time, the IRS was basically done with or was done with processing tax returns. It is currently in the middle of processing 2007 tax returns, the same IT system and the same people who process rebates are working on that. So, basically, until the 2007 tax season is closed, the IRS really can't turn in any significant way to processing rebates. That means you are talking about mid-May to early June at the earliest for checks to start going out, and then it takes 8 to 10 weeks to actually mail them.

Mr. COOPER. But that is using the government. Is there another way to do it? For example, what if we were to look at MasterCard or Visa or other credit cards? They have monthly contact with their card holders.

Mr. ORSZAG. I guess one can imagine different approaches. To the extent you are going to rely on tax information, which has been central to many of the proposals that I have seen, the IRS obviously then needs to be involved.

Mr. COOPER. How about the issue of offsetting? Does it make sense to try to pay for the stimulus package, or should we add it to our long-term deficit problems.

Mr. ORSZAG. As I noted, the Nation's long-term fiscal imbalance is large and serious, and one should be very careful to avoid exacerbating that. So, from that perspective, offsetting any short-term stimulus, especially if it were done out in year 5, 6, 7, what have you, would be desirable.

I would note, though, that if you are going to do a stimulus, it makes sense to do it as fast as possible. So if the cost of delay is offsetting $100 billion or $150 billion, that may not be worth the benefit to the long-term fiscal outlook to forgo a short-term economic opportunity.

Mr. COOPER. Shifting to the long term, you have described our long-term outlook as, I think you used the word "dismal." That is a pretty severe judgment. Many people in Congress have been critical of the rating agencies, as they did not anticipate the problems with the subprime lending crisis. But last Friday, Moody's joined Standard & Poor's, which had done this a year earlier in projecting that the U.S. Treasury bond itself, not any CDO or minor instrument, but the most important financial instrument in the world, might lose its AAA credit rating.

So these rating agencies now are projecting dire consequences, and now we are not wanting to pay attention so we fault them for being too lax. Now we are not paying attention when they are trying to focus our attention on our real, long-term fiscal problems, as you noted in your excellent slides, for example, focusing on the fiscal gap.

You point out that, as severe as the aging problem is, it is not our major problem. The uncontrolled rise in health care costs is a much larger component of our future problem. And, to my knowledge, no committee in Congress is working on that issue. None. You know, to the extent we are focusing on issues like Medicare, we are talking about increasing spending, not decreasing spending.

I know that you are emphasizing the CBO work in helping us focus on these important issues so that we can go into the health care sector and restrain this uncontrolled growth; but as I think you have correctly pointed out in your testimony, that is the central problem that we face, and this committee should be focused not only on the short-term, but on these dire, long-term issues. And it worries me when our good ranking member says that deficits have dramatically declined—you know, happy talk as if, hey, everything is fine for the time being, when it is clearly not either in the short run or in the long run.

And if my colleagues would focus on Director Orszag's excellent charts. For example, on page 2, if you look at our deficit, including the Social Security surplus that has been borrowed, you will see that the deficits are in fact not $163 billion or $219 billion, but more like $344 billion and $414 billion. And my colleagues need to remember that this is using cash accounting, too. This is not using the real accounting that we require everyone else in America to use, private business, State and local government, but that we have exempted the Federal Government from.

So I would hope that our colleagues could focus on the dismal situation that the Budget Director has described.

I see, Mr. Chairman, that my time has expired.

Mr. ORSZAG. Mr. Chairman, could I just quickly respond to an earlier question, and get back to Mr. Edwards that the increase in gross Federal debt—not public debt, but gross Federal debt—between the end of 2000 and the end of 2007 was $3.3 trillion.

Mr. SPRATT. Mr. Lungren.

Mr. LUNGREN. Thank you very much, Mr. Chairman. I will try and respect the admonition of Mr. Cooper to avoid happy talk.

I must take some small exception to Mr. Edwards' comment about the dishonesty of those of us who were here 20 years ago and working on an effort. As a matter of fact, the Reagan administration at that time attempted to have some structural changes with respect to mandatory spending, which were defeated in the House of Representatives. Virtually every single budget that was brought forth by that administration was exceeded by the Democratically controlled house.

So we were not being dishonest; we were working in earnest to try and solve the problems at that time. And I am not sure that kind of language helps at all.

Mr. Orszag, here is my question. I think the United States was established with a skepticism toward government so long as it is not cynicism. So I will try to be skeptical without being cynical.

Mr. ORSZAG. Okay.

Mr. LUNGREN. My question is this. If you have said that it is the position of our office that we are going to have sluggish growth and define that as 1.7 percent growth in GDP—and you say the other outsiders are talking about 2 percent—if in those instances it is necessary for us to have a stimulus package, we are not in a recession as you suggest. Is that a rule of thumb for the future, that when growth is only 1.7 percent to 2 percent, that we need a stimulus package?

Mr. ORSZAG. What I would say is that growth during the first half of 2008 is likely to be significantly weaker than that.

Mr. LUNGREN. But you said we are not going to be in a recession. That is your best judgment. If we are not going to be in a recession, is this establishing a new cornerstone for us that when we have weak growth, such as you suggested short of recession, that lays the groundwork for the necessity of a stimulus package?

Mr. ORSZAG. Let's hypothetically say that growth is going to be a half percent during the first half of 2008. That is substantially below the potential growth rate of the economy. It is up to you to decide whether you want to intervene in that situation. But if that is the central estimate, the risk of a recession is elevated relative to normal economic conditions.

I would make one other quick point, which is, it would be desirable, given that it takes a long time to decide these things, that if the Congress wanted to intervene in those kind of situations, to bulk up the automatic stabilizers so that things happen automatically, rather than requiring targeted fiscal stimulus, even if one wanted to intervene in those kinds of situations.

Mr. LUNGREN. But you are suggesting that even if we act quickly here, the process takes so long it would really take a while for a spendout to take place?

Mr. ORSZAG. There are only a limited number of options for you to affect economic activity during the first half of 2008.

Mr. LUNGREN. Maybe we ought to put General Petraeus in charge. He seems to get things done pretty quickly.

Mr. ORSZAG. There are a lot of options.

Mr. LUNGREN. I am trying to figure out where we are going with this in terms of the philosophy involved.

The suggestion that you have made is that we need to get that money spent and spent quickly. And I have heard others on the other side of the aisle to suggest that means that it ought to be in the hands of those who are in the lower economic sector rather than the upper sector, because they are more likely to spend the money rather than to save it.

And so I am trying to figure out, what is a stimulus package based on tax rebates that you think would be most effective in the short term?

Mr. ORSZAG. Again, if the objective is to boost aggregate demand—by the way, I should say, the experience with the 2001 rebates was actually more auspicious than previous studies would have suggested; that is, they resulted in a larger kick to short-term economic activity than I think we would have expected based on the experience with earlier rebates.

The evidence from that experience, though, also does suggest, which is in line with economic theory, that as you move down the income distribution of recipients, the share of the rebate that was spent went up. And among recipients who were more credit constrained, who had exhausted more of their credit card limits or had lower credit card limits, spending was also a higher percentage of the rebate.

Mr. LUNGREN. Now, let me ask you a question, just specifically economically. If I were to present you a plan to say, let's keep the current tax rates, marginal rates, at 10 and 15 percent, where they are, but adjust the 25 percent rate to 28 percent, the 28 percent rate to 31 percent, the 33 percent rate to 36 percent, and the 35 percent marginal rate to 39.6, would you call that a tax increase if I were to present that to you as a plan?

Mr. ORSZAG. That would be an increase relative to the alternative scenario that you were presenting.

Mr. LUNGREN. So, yes, that is a tax increase?

Mr. ORSZAG. Do you really want to drag me into this semantic game?

Mr. LUNGREN. Well, no. But I am trying to figure out—to me, that sounds like a tax increase. To the average person, it does. I want to know what an economist says.

Mr. ORSZAG. If you are comparing two scenarios, one with a 35 percent marginal tax rate and one with a 39.6 percent marginal tax rate, the 39.6 percent marginal tax rate is higher.

Mr. LUNGREN. Thank you.

Mr. SPRATT. Ms. Schwartz.

Ms. SCHWARTZ. Thank you, Mr. Chairman.

I wanted to follow up on, actually my colleague here, Mr. Cooper, some of his questions and comments about health care costs. And we have obviously had this discussion here in the Budget Committee with you a number of times. And I wanted to say that, clearly, I think many of us are concerned about, long term, the cost particularly of Medicare.

And I would just take a little bit of exception in the fact that we haven't done anything. Certainly, on Ways and Means, we did look to—it did not get done by the Senate yet, but we did look to try to take what we considered overpayments under Medicare Advantage to Medicare HMOs and redirect that in ways we thought would be smarter spending, prevention, and obviously some payment to physicians.

You don't need to comment on that, but I just wanted to say that we are certainly well aware of the need to tackle the rising costs and are having serious discussions about comparative effectiveness and ways that we can contain costs without limiting access to needed health services for our seniors. I would like to see us move in that direction, if we could; and there are some ideas, like electronic medical records and e-prescribing, that we know not only save lives but save money.

So I would hope that together we can work on some of those issues so that we can contain costs but still get quality care to people. But I did want to follow up on some of the concerns about health care.

Certainly, in the economic downturn—and I hear from families all the time in my district about the rising cost of health care to them, the fact that they are seeing a greater share of the premium that they have to pay, even in employer-sponsored health care. I certainly hear from businesses that are saying that they can't increase wages because of the costs of health benefits. We do know that we have seen employees have to pay almost $1,500 in their share when they are covered by the employers. And, of course, most recently, we have seen a report that says 700,000 to 1 million children could be uninsured as a consequence of the economic downturn that we are now in.

So given that you have, and certainly Ben Bernanke, the Fed Chairman, did last week make it very clear that what we ought to be doing if we do a short-term stimulus—not a long term now, but a short-term stimulus—is to put dollars in the pocket of low- and middle-income folks who will then spend it, as a short-term spending and increase in demand.

Could you comment on whether, in fact—as families are seeing the high costs of health care, whether they spend the dollars on, say, health care premiums, or whether they spend the dollars to keep their health coverage if they are doing without employer help; if they are spending it on COBRA because they have been laid off; or if they are spending it on other everyday needs that they have, mortgage payments, debt? Does that make a difference versus spending it on other kinds of goods and commodities?

Mr. ORSZAG. To a first approximation of what goods and services the money is spent on doesn't matter very much. There can be some differences. For example, one of the things we noted in our stimulus report is, to the extent that the additional spending disproportionately comes from imports, you attenuate the stimulative impact on domestic production. But to a first approximation, the mix of spending doesn't matter as much as the aggregate amount that you induce.

Ms. SCHWARTZ. That is good. That is exactly what Ben Bernanke said.

So we are good. So we are on the same page there, which is good, because I think a lot of families, actually, to the degree we might want to suggest that they may have to pay off credit card debt, pay mortgages, stay in their homes, be able to pay for health care costs, it is certainly something we want to do.

Let me just ask you for another comment, if I may, on the broader topic. You said this in your testimony. We are very clear—so this is something we are trying to work in a bipartisan way—that we want to not only target these dollars, however we get them out to families so they will use it on spending, but we also want to do enough to have an effect on spending in the economy in the short term. Again, this is only short term, not long term. But we also are committed to not adding to the debt, to the national debt.

Some of us are really quite concerned and have really spoken out about the need to balance the budget. And as we set an example for American families, we know that we have to pay down our debt, we have to be able to start to have our income match our spending, however we do that.

So might you want to talk about how much we—how far we could go, and the fact of whether or not we have to commit to paying for whatever economic stimulus package we put forward in the short term.

Mr. ORSZAG. Well, first let me say, if you were going to do economic stimulus, it doesn't make sense to offset the cost in that year, because that undermines the very purpose of what you are trying to do.

There is no reason why you couldn't, though, from a short-term stimulus perspective, offset the costs in year 6 or 7 or 8 or 9. That does not diminish the effectiveness of the stimulus in this year and, in fact, could under some scenarios help to accentuate it.

I would come back, though, to say time is of the essence here; and if you are going to act, it is important to act quickly so that you don't miss your window. And if the price of obtaining those offsets is a very substantial delay, that is probably a trade-off that, from an economic perspective, is not a good one to make.

Ms. SCHWARTZ. And I think my time is up. But certainly I think what has become very, very clear even as we talk about the short-term stimulus, is that in the long term any tax cuts, any kind of work we do on tax policy has to be paid for as well, that that has an effect on our budget and obviously has an effect on the economy.

Thank you, Mr. Chairman, and I yield back.

Mr. SPRATT. Mr. Campbell.

Mr. CAMPBELL. Thank you, Mr. Chairman.

Thank you, Dr. Orszag.

Looking at your projection, even with the slower economic growth that you are showing, we are showing slower revenue growth, but it still is revenue growth I think of 3.4 percent year over year. Does it follow then that if total Federal spending were held to 3.4 percent growth, that there would be no increase in the deficit in this coming year?

Mr. ORSZAG. Not quite, because you are starting off with spending higher than revenue, so it magnifies a little bit, but not a big increase.

Mr. CAMPBELL. Okay. If you were to hold Federal spending growth to 3 percent or 2.9 percent, then the deficit would decline?

Mr. ORSZAG. Something like that, yeah.

Mr. CAMPBELL. And if total Federal spending were held even, in other words, no increase over the prior year, we probably would be in surplus?

Mr. ORSZAG. Yes.

Mr. CAMPBELL. Is that correct?

Mr. ORSZAG. I would imagine so, yes.

Mr. CAMPBELL. Okay. Thank you.

Now, switching to the stimulus package. If we were——

Mr. ORSZAG. Actually, not quite.

Mr. CAMPBELL. Oh, not quite?

Mr. ORSZAG. Very close.

Mr. CAMPBELL. You are just doing the math on the back of an envelope?

Mr. ORSZAG. Yes. Very close. Not quite.

Mr. CAMPBELL. So at zero it would be—at no increase in Federal spending, if we held Federal spending the same as last year, then probably no deficit, or close to even?

Mr. ORSZAG. Yes. Again, this is keeping net interest, things that won't happen. But you would be certainly under $100 billion. Something like 70 or 80.

Mr. CAMPBELL. If we were to pass—if this Congress were to pass and the President were to sign a stimulus package that included revenue, tax provisions or spending provisions, or some combination thereof, in areas in which you felt they were reasonably effective, would you then be revising this estimate to increase GDP growth and/or lower unemployment and/or increase nominal revenue?

Mr. ORSZAG. What I would say is that in periods like today, where the economic conditions are potentially changing rapidly, we will monitor the situation carefully. And there have been times in the past when, during our reestimate of the President's budget, we have updated our economic projections; and will reach a judgment as to whether that is warranted in this situation.

Mr. CAMPBELL. Because I am sure you can tell where we are going here.

If we were to pass something that is intended to stimulate the economy, then one would presume we should project that it was going to, in fact, stimulate the economy or we wouldn't do it. And if it does stimulate the economy, GDP should go up, unemployment should go down, from your projections, and revenue from the nominal basis should be higher.

Mr. ORSZAG. I am sorry. Were you asking about the scoring of the proposals?

Mr. CAMPBELL. Yes.

Mr. ORSZAG. Oh, I see.

Mr. CAMPBELL. Well, the scoring of the proposal, but overall.

Mr. ORSZAG. Let's separate the scoring in which those kinds of feedback effects would not be taken into account, and then a subsequent evaluation by CBO, including potentially updating our economic baseline.

Mr. CAMPBELL. So when you score the proposal, you don't take that into account?

Mr. ORSZAG. That is right. That is correct.

Mr. CAMPBELL. But then would you then—which again, then, basically we are assuming that the stimulative package will have no stimulus; "if" is essentially what that assumes.

Mr. ORSZAG. In the scoring rules, that is correct.

Mr. CAMPBELL. In the scoring rules.

So would you then revise somewhere, so we could get some idea of what you think might happen?

Mr. ORSZAG. We have done dynamic analysis or basically the macroeconomic feedback effects of major proposals. And I suppose that if there were a major fiscal stimulus proposal and you wanted us to evaluate what the macroeconomic impact would likely be within some range, we could provide that information to you.

Mr. CAMPBELL. Okay. Then the last question I have is, there is all this talk now about a rebate package, and there has been a lot of discussion here this morning about how we can get consumers to spend it quickly.

This downturn we are in was not consumer led, it is credit led. And, arguably, you and others have said here, gee, our saving rate isn't high enough, that sort of thing. Arguably, you could say part of the credit leading is that some consumers at least borrowed too much, borrowed money they couldn't afford to pay back, et cetera, et cetera.

Why would we not want to do some stimulative package, where we are encouraging and telling people to save and invest that money or pay down debt on that money, because that is what caused the crisis, not a lack of spending?

Mr. ORSZAG. I guess I would say two things. I think most fundamentally there is this tension between what we need to do over the medium and long term, which is, we need to raise our national savings rate. And what is most appropriate where the economy is weak and we have goods and services that could be produced, but won't be because there is not sufficient demand for them, that is a very unusual circumstance for the economy to be in, or a relatively unusual circumstance. And the tension is that what is appropriate in that kind of unusual circumstance is often exactly the opposite of what we need to be doing in the medium and long term.

And figuring out how you would do what might be appropriate now and then transition to what would be appropriate in the long term is very tricky. How do you convince households that they should spend more now but, oh, no, you should start saving a lot more next year and the year after, is in some sense the ideal economic policy, but it is very difficult to do in practice.

Mr. SPRATT. Mr. Doggett.

Mr. DOGGETT. Thank you very much. I am impressed with the remarkable consistency of all of the economists who have come to testify about the stimulus; and I think that perhaps that is the result of the fact that, as you have referenced in your testimony, we do have substantial experience with what has an effective stimulative effect for the economy and what does not, and we have substantial academic studies now in that area.

First, is that correct, that there are many studies and experience with several different attempts to stimulate the economy?

Mr. ORSZAG. That is correct.

Mr. DOGGETT. And the first area in which every economist who has come to this committee has agreed, and you have reiterated it this morning, is that there is no reason we can't have substantial stimulative effect and pay for this within the PAYGO rules.

Mr. ORSZAG. That is correct.

Mr. DOGGETT. Indeed, you just indicated to Ms. Schwartz that it could actually increase—or "accentuate," I believe was your term—the stimulative effect to pay for it within the PAYGO requirements.

Mr. ORSZAG. That is correct also.

Mr. DOGGETT. And the only caveat you have offered is if we have some people who are so wed to their borrow-and-spend ideology that they refuse to pay for it, you say, don't let that hold you up; go ahead and get it approved, because it is important to act promptly if we are to get this recession insurance.

Mr. ORSZAG. Correct.

Mr. DOGGETT. As far as the size of the stimulus, there also seems to be some consistency in that area. The first people who urged that we take action, the Democrats, recommended something under $100 billion in the size of this stimulus. When I asked Chairman Bernanke last week what he saw as being too much, too excessive a stimulus, I think he put a cap of about $150 billion. I know the President has said about $145 billion.

If you begin to exceed $150 billion now, I am concerned that this will balloon out of control. Will it be counterproductive?

Mr. ORSZAG. It could be. And especially if you do things that are not only expensive, but don't really kick in until late 2008, early 2009, mid-2009.

Mr. DOGGETT. Too much and too late.

Mr. ORSZAG. Stimulus delayed is stimulus denied. You do not want to be adding fuel to an economy that may well be growing rapidly by 2009.

Mr. DOGGETT. And you have indicated in your testimony today and yesterday—and it has cut across the parties, but that some things that may fit an ideological framework, whether it is building a bridge or a tax cut for the rich, they just get there too late and they have too little stimulative effect to make much difference.

Mr. ORSZAG. We went through lots of different options in the stimulus report we prepared for this committee.

Mr. DOGGETT. And that report is very helpful, and just to highlight some of its findings: Based on all of the academic studies, if we really wanted to have the maximum bang for the dollar and stimulative effect, this afternoon we would approve an extension of unemployment benefits on a temporary basis and an expansion of food stamps on a temporary basis, wouldn't we? Isn't that what you found to be the most effective?

Mr. ORSZAG. Those were among the options that were ranked with large or high bang for the buck or cost effectiveness.

Mr. DOGGETT. And they will get the dollars out and stimulate the economy quicker and more effectively than any tax rebate scheme that you have heard of.

Mr. ORSZAG. The administrative challenges on the tax side for individuals are significant.

Mr. DOGGETT. Because even under the best scenario, those tax dollars are not going to flow until sometime—and begin to be spent until sometime in the middle of the summer. Unemployment benefits, food stamps could be spent now.

Mr. ORSZAG. The information we are receiving is that changes to that employment insurance system or to the food stamp program could result in additional benefits for households within, say, 2 months, and that is faster than a rebate.

Mr. DOGGETT. If, since the President wants nothing but tax rebates to date, that is the direction in which much of this stimulus goes, and we adopt a very inefficient tax stimulus and go in that direction. Chairman Bernanke said focus it on low- and moderate-income families. Some people have forgotten what that is and think that means buddies at $100,000, $200,000, $300,000 a year in income. He said that $49,000 is the median income, and perhaps you go into the mid-50s.

But do you believe, to be most effective, if you have tax rebates, they should be focused on low- and moderate-income families?

Mr. ORSZAG. That would get you more short-term demand for any dollar you spend.

Mr. DOGGETT. And as far as the various corporate tax breaks that some have advocated, who worship at the altar of tax cut salvation, those—of all the various schemes that have been advanced to give another tax break to corporations, which ones appear to be the least efficient and which ones have the most potential to stimulate?

Mr. ORSZAG. The least efficient options for short-term stimulus appear to be things like a reduction in the overall corporate tax rate, because a significant part of that is a payoff to existing investment or existing capital as opposed to an incentive for new capital investments.

The theory behind temporary investment incentives like bonus depreciation or a temporary investment tax credit is sound. It creates an incentive for firms to accelerate their investments that they were going to make in 2 or 3 years into the short term, and that can be beneficial.

The experience with the 2002 and 2003 bonus depreciation provisions was somewhat disappointing relative to what we had expected and hoped for and what we would have thought based on that theory, so at least some caution is warranted. Basically left with, there is a good theory and in fact you could even supercharge the incentives by applying it only to investments above some historical level so that it is an incremental incentive.

But the most recent experience didn't turn out so well in terms of encouraging more investment. It may be that the situation now is different, and you could get more impact from those provisions than we experienced several years ago.

Mr. DOGGETT. Just one clarification on that last point, just so that it is crystal clear.

If we have to—even though it is not as effective as the other approaches, but if we must include into this package in order to get bipartisan support for it, some type of business or corporate reduction, what is the best way to do it?

Mr. ORSZAG. The best way to do it, if it could be done administratively quickly, would be either an investment tax credit or bonus depreciation for new investment above some historical threshold—

I am making this up: 90 percent of the average over the past 3 years.

The question becomes whether the benefit of doing it incrementally is worth the administrative complexity. But generically, temporary investment incentives, either bonus depreciation or investment tax credit, rank among the highest options for cost effectiveness on the corporate side.

Mr. SPRATT. Mr. Hensarling.

Mr. HENSARLING. Thank you, Mr. Chairman.

One of the most renowned economists of our time, Nobel Laureate winner, Dr. Milton Friedman, in his writings, spoke of a permanent income hypothesis. And I see your head nodding; I assume you are familiar with the hypothesis, which essentially said that consumers do not fundamentally change their spending habits based upon small differentials in their income. In short, you cannot convince people they are richer than they are.

As I look at the histories of the 2001 tax rebate plan, which I believe was most important in helping consumers pay their bill—and I always champion the cause of giving taxpayers more of their tax money, but isn't it true that almost 2 years after that rebate plan, that the economy was still losing jobs, that the stock market had plummeted and business investment had still not turned around?

Mr. ORSZAG. Unemployment peaked in 2003.

Mr. HENSARLING. Wasn't it also true—my reading of the history is that it wasn't until the 2003 tax relief that signaled to the economy, that signaled to businesses, small businesses, entrepreneurs, that we actually cut rates, which was different from a temporary tax rebate?

We cut tax rates, we cut marginal tax rates, capital gains, dividends; and then what we saw was almost 5.3 million new jobs created within 18 months of those reductions, and a stock market leap of 32 percent.

I mean, doesn't the evidence suggest that you cannot fool enough people into thinking they are richer than they are, and that if you truly measure economic growth by, first, keeping your job and then, second of all, having even greater job opportunities with greater upside potential, that we need to signal to those who create jobs that they can count on lower tax relief as opposed to the threatened tax increases that we see today?

Mr. ORSZAG. Let me come back first to the 2001 rebate. We need to remember that the aggregate size of the rebate was under $40 billion, and the evidence does suggest that that $40 billion or so did cause a spike in economic activity. And on the permanent income hypothesis, one of the reasons, in fact, one of the leading——

Mr. HENSARLING. I am sorry, Dr. Orszag, but let me interrupt you on that point, because what I did, when I viewed the statistics, I saw that consumer spending did rise temporarily with the rebates.

But my reading is—is that capital investment spending fell by roughly a corresponding amount, leaving no net infusion into our economy. Do you have a different reading?

Mr. ORSZAG. Yes. My reading would be that there was this very substantial capital overhang that we went into 2000 and 2001 with, and that investment was going to be relatively weak and that the partial effect of the rebate was to boost economic activity.

And I want to just briefly mention, on the permanent income hypothesis, one of the reasons—in fact, the leading reason—why people believe, or economists believe, that targeting credit-constrained households is the most effective way of targeting a temporary tax change is precisely that for those households, the permanent income hypothesis doesn't apply because they can't borrow against their expected future income. And so changes in temporary income do result in changes in their spending pattern, more so than for permanent income hypothesis households.

Mr. RYAN. Would the gentleman yield?

Mr. HENSARLING. Yes. I would be happy to yield.

Mr. RYAN. Director Orszag, isn't it the case that in 2001 that was not a temporary increase?

Mr. ORSZAG. Yes.

Mr. RYAN. The rebates were forward; on permanent or long-term reductions in marginal income tax rates, you simply got the reduction of the tax rate forwarded. So it is kind of an apples-to-oranges comparison to today's proposals of temporary, one-shot rebates to 2001's lower permanent reduction, correct?

Mr. ORSZAG. Yes.

Mr. RYAN. So people more adequately thought their take-home pay would be higher, given they were going to experience lower tax rates going forward than what we are discussing today, correct?

Mr. ORSZAG. As we noted in the stimulus report we prepared, the experience with the 2001 rebate seems different from the studies of earlier rebates; and one reason may be that, as you note, it wasn't a purely temporary thing. It was basically an advance payment on tax changes that were scheduled to occur.

Mr. HENSARLING. I yield back. Thank you, Dr. Orszag.

Mr. SPRATT. Mr. Blumenauer.

Mr. BLUMENAUER. Thank you, Mr. Chairman.

I appreciate, Mr. Orszag, your description about the tension between the short-term stimulus and some of the long-term structural problems that the economy faces, one of which is clearly an entitlement deficit that we are concerned about.

There are other deficits that actually have severe consequences. A deficit in terms of infrastructure investment, where we probably have a gap as large as any in the world with our international competitors in China, Japan, European Union. We are also looking at some fundamental weaknesses, and this has come out in the hearings; I appreciate your help in sort of guiding us through.

But one of the things that concerns me is a fundamental weakness now because of what is happening with this spreading housing crisis, where we had regulatory sleepwalking, people asleep at the switch where housing in this frothy market was used as an ATM to drive spending. Gone now. Housing values are lower. They are likely to be lower still next year at this time, and we are going to have hundreds of thousands of people losing their homes.

I think it is appropriate that we do move forward with some stimulus activity, and I am mindful of what you said about that tension between the short-term and our long-term needs. In that connection, I guess I would like to put two items on the table for you to react to for us.

There is an emerging industry in this country where we are trying to—in alternative energy, wind energy for instance, we have a production tax credit scheduled to expire this year; and because it is scheduled to expire and we haven't renewed it, people are cutting, starting to cut back now on investments. And if you talk to the industry, they are basically going to shut down in the next 2 months because they can't make those long-term investments on the possibility that we are going to renew the production tax credit.

We are looking at, for the first time in history, a deficit in the highway fund—never happened before. There is no borrowing authority, so that means real reduction. And because of the slow payout rate, that means, say, a $5 billion reduction in the Highway Trust Fund, translates into maybe $20 billion in contract authority. Both of these can have significant ripple effects for the economy, are going to have significant ripple effects.

I am wondering about your assessment of whether we could include something like extending that production tax credit, which we are likely going to do before the year ends anyway, to avoid the slowdown in the economy. It would be in that window that you talked about, within 2 months and—the potential of an infusion in the highway fund to make sure that we don't have disruption of that engine machine in terms of infrastructure.

Could you comment on either of those: The impact that we are likely to see further economic downturn because of the uncertainty, and the potential of investments that could help strengthen what happens in the next 6 months?

Mr. ORSZAG. I guess, first, let me just say in general on the tax incentives side, trying to target the tax incentives to particular types of investments in the short term probably is not ideal from a short-term stimulus perspective. You may well have longer-term objectives that one could meet, but in terms of overall effectiveness, trying to pick out particular industries that you are going to try to encourage in the short term is probably not as wise as just providing a broad-based and, ideally, incremental, if it can be done administratively, investment incentive.

On infrastructure spending and especially on some highway spending, infrastructure spending, as I said before, in general, spends out very slowly and so is not an ideal short-term stimulus. There are some subcomponents of infrastructure spending, for example, road resurfacing, where the spendout rates tend to be higher. The challenge is whether you can pick out those specific projects or those specific types of spending quickly and get the money out the door quickly. And I think there is at least some skepticism among budget analysts in general about whether that can be done in a timely and effective manner.

Mr. BLUMENAUER. Mr. Chairman, I would like to work with your staff and Mr. Orszag to be able to zero in on the consequences of these items that I raised in terms of the depletion of the Highway Trust Fund and the disappearance of something like this production tax credit, in terms of what the economic impact is going to be if they are not remedied.

Mr. SPRATT. We will do that particularly in conjunction with the budget resolution, which is on a fast track this year.

Mr. BLUMENAUER. Thank you, sir.

Mr. SPRATT. Thank you.

Mr. Tiberi.

Mr. TIBERI. Thank you, Director. Mr. Cooper brought up Medicare, and you have talked about the costs associated with that, with Medicare and with health care. And this is not a "gotcha" question.

Today we are discussing SCHIP on the floor of the House. I have supported that bill, the Democrat bill.

A physician lectured me back in Ohio about Medicare and us not tackling Medicare; and that we were making matters worse with this SCHIP bill in the way that we were paying for it with tobacco taxes, and rather than solving problems in the health care area on costs, we were adding to our long-term fiscal problems on the health care side.

What is your view of that? I haven't heard you talk about SCHIP related to Medicare related to the costs.

Mr. ORSZAG. I guess I am a little bit confused. The assertion was that a higher tobacco tax exacerbates our——

Mr. TIBERI. Well, a higher tobacco tax is a revenue source that has been and will continue to deplete as there are fewer and fewer smokers in America, which is a good thing——

Mr. ORSZAG. Right. The Joint Committee on Taxation, when it does the revenue estimates, tries to take that into account, so the revenue streams that are associated with a change in policy include the behavioral response of people smoking less as a result.

Mr. TIBERI. But a broader picture, Dr. Orszag. You concur that we have not—as a society, as a government, as a health care industry—got our arms around the increasing costs of health care. Whoever is paying for those benefits, whether it is government, whether it is business, it continues to rise exponentially. And you continue to say—I don't want to put words in your mouth—but that will continue to occur in the future. And so if we struggle as policymakers here with that issue, and it complicates the future of Medicare funding, how does it complicate the future of Medicaid and SCHIP funding if we pass this bill, which I support?

Mr. ORSZAG. The legislation would raise SCHIP funding. I mean, I guess that is in some sense the objective.

Mr. TIBERI. How does that contribute to our long-term fiscal and—when the Federal Government is taking the largest responsibility for paying for that program?

Mr. ORSZAG. I guess I would say, at least officially, that that legislation is scored as having a net budget impact of roughly zero. There are questions that have been raised about the——

Mr. TIBERI. Long-term?

Mr. ORSZAG. The time profile in the outyears of the assumed SCHIP funding. In general, we are spending as—the policy community is spending a lot more time focused on covered questions in health care than on cost containment or trying to bend that curve; and ultimately, we are going to have to bend the curve.

Mr. TIBERI. You do think we will have to bend the curve?

Mr. ORSZAG. Something that can't go on forever won't.

Mr. TIBERI. Thank you.

With the issue of scoring, if you could clear this point up for me from your perspective, the question is, does CBO have a bias toward a pro-spending budget? An example, if you can answer this question, is in this document that you have.

You assume that the expiration of the tax cuts will occur, and it occurs. Yet, on the spending side, the Reconciliation Act that was passed last year dealing with Pell Grants expires in 2017, but you assume that that expiration will not occur, that it continues.

Why, on a program area, do you assume it will continue, but on a tax area, you assume it will not continue?

Mr. ORSZAG. Let me first say that in general I think a lot of the commentary about the imbalance between how revenue and spending is treated misses the observation that there is an integrity between the baseline and the scoring process.

However, the example that you cite is a good example of an imbalance. When you adopt a new program or a change in a program and that, even if it expires within the budget window, it is assumed to be extended. When the window rolls forward, that additional year of expenditure, to the extent it's included in the baseline, has not been part of the scoring process, but winds up in the baseline; and that does not occur on the revenue side, and that is an inconsistency in the rules that govern the scoring process.

That particular decision was made after consultation with the Budget Committees, and so I obviously leave up to your own internal deliberations how you decide the guidance that you give us on those particular cases where it is ambiguous what should happen.

Mr. TIBERI. And, in America, I assume that is a pro-spending bias?

Mr. ORSZAG. In that particular case, that spending program was treated more favorably than most revenue things would. I would note, though, there are things on the tax side that are treated similarly. In particular, taxes that are dedicated to trust funds have a similar type of system associated with them.

Mr. TIBERI. Thank you, Director.

Mr. SPRATT. Mr. Scott.

Mr. SCOTT. Thank you, Mr. Chairman.

Thank you, Dr. Orszag, for being with us. I just want to make a couple of observations to put things in historical perspective.

In 2001, we had a surplus that exceeded Social Security, and we were talking about a lock box to keep Social Security surplus for Social Security. This year, you have listed the deficit as $219 billion so far. Does that include spending almost $200 billion of Social Security surplus?

Mr. ORSZAG. Yes.

Mr. SCOTT. And then you go additionally another $219 billion in the hole?

Mr. ORSZAG. That is correct.

Mr. SCOTT. Now, in 2001, it looked like we were going to be able to pay off the entire national debt held by the public by 2008, and all debt paid off by 2013. Is that your recollection?

Mr. ORSZAG. Something like that, yes.

Mr. SCOTT. And that would mean we would be paying zero interest on the national debt by 2013. By 2013. You say we are starting off with about $200 billion a year in interest right now?

Mr. ORSZAG. A little bit above that. Yes, 230.

Mr. SCOTT. Okay. And if we continue, the Bush agenda would add almost $100 billion more interest on the national debt by 2013?

Mr. ORSZAG. It would add, I am sorry, how much?

Mr. SCOTT. 94. An additional $94 billion?

Mr. ORSZAG. That sounds plausible to me. I believe that is off Mr. Spratt's scenario. Yes. That includes a variety of policy changes beyond extending the tax legislation.

Mr. SCOTT. Right, but the expected agenda, you would add another—so that would be almost $300 billion in interest on the national debt by 2013 rather than zero?

Mr. ORSZAG. In our—you are comparing now to the 2001 projections? Okay, yes.

Mr. SCOTT. At $300 billion, how many people can you hire at $30,000 each? Is that about 10 million?

Mr. ORSZAG. Yes.

Mr. SCOTT. How many people are unemployed today?

Mr. ORSZAG. The unemployment rate is about 5 percent. So something—7.5 million.

Mr. SCOTT. Seven and a half million unemployed at $30,000 each. With the interest on the national debt, we can hire 10 million people, just putting the numbers kind of into perspective.

Mr. ORSZAG. But of course, that wouldn't actually occur.

Mr. SCOTT. That's right. Okay, but just to put the numbers in perspective.

Mr. ORSZAG. Okay.

Mr. SCOTT. Now, you exhibited a little reluctance to get into semantics about whether or not you cut taxes and then restore the taxes right back to where they were, whether or not the restoration would count as an increase.

How about if you lose 2 million jobs and then people get their jobs back, whether or not that counts as a creation of 2 million jobs?

Has any administration done worse in job creation since Herbert Hoover than this administration?

Mr. ORSZAG. Economists don't normally measure job growth by administration. Job growth has been relatively weak over the past few years for this stage of the business cycle.

Mr. SCOTT. Now, we heard about this robust stock market. If the stock market collapses and then comes right back to where it was, is that a robust stock market?

Mr. ORSZAG. I think I am just going to probably stay away from this whole line of questioning.

Mr. SCOTT. The Iraq war, if the surge is working and we actually need 150,000 troops to be there, would your alternative scenario be actually worse than it is?

Mr. ORSZAG. If you needed 150,000 troops in perpetuity for a significant period of time, like over the 10-year window, yes.

Mr. SCOTT. The chart would be worse than it is?

Mr. ORSZAG. That is correct, sir.

Mr. SCOTT. If the stock market doesn't do better than it has done in the last couple of days, what would that do to the capital gains part of your revenue projections?

Mr. ORSZAG. I can get you that number.

Mr. SCOTT. And you mentioned accelerated depreciation as part of a possible corporate tax. If it is incremental and actually—people actually buy things, would it pay itself back, short term?

Mr. ORSZAG. Most of the 1-year budget effect of things like accelerated depreciation are offset, or made up, if you will, in the remaining 9 years of the 10-year window.

Mr. SCOTT. So the cost is only time, value of money, in effect?

Mr. ORSZAG. Although the only part is exactly why firms are responding to the incentive. But, yes.

Mr. SCOTT. Your scoring of public projects scores that as weak because it is long term. If the public projects were required to be ready to go—that is, you don't have the planning, land acquisition, environmental studies. If the governor can represent that the project is ready to go, they can start laying asphalt as soon as they get the check, would your analysis change?

Mr. ORSZAG. It really depends on what you mean by "ready to go." There are many assertions that things are ready to go. The delays involved in the process are often longer than one would imagine.

But if there are literally projects that are on hold because funding is inadequate and then projects could get restarted immediately, yes, that money could spend out quickly. The challenge is isolating those things in an overall pot of infrastructure projects that might not have that.

Mr. SCOTT. One of the proposals is to fund projects that are ready to go, then that would be different than an overall public works project, significantly different in terms of stimulus effect?

Mr. ORSZAG. Yes. But it all comes down to defining "ready to go" and who decides that.

Mr. SCOTT. Mr. Chairman, just very quickly.

Summer jobs for teenagers and winterization programs and labor intensive, that could be—people could be on the job by this summer. Would that not qualify for timely, targeted and temporary?

Mr. ORSZAG. I think the question becomes whether—if you are talking about a new program, whether the various apparatus that need to be put in place in order to get that moving can actually be accomplished fast enough.

Mr. SCOTT. If the apparatus is there and the teenagers, all they need is a check to hire teenagers, that would be timely, targeted and temporary?

Mr. ORSZAG. It would. I would just caution that the more targeting you try to do in terms of specific programs, the less timely things may turn out to be.

Mr. SPRATT. Thank you, Mr. Scott.

Mr. Etheridge.

Mr. ETHERIDGE. Thank you, Mr. Chairman. And thank you for the hearing.

Dr. Orszag, thank you for being here again. And I guess we wouldn't be doing this today if it weren't a confidence factor. I mean, it is about the economy, but it is really about a confidence factor.

Last week, when the Chairman of the Federal Reserve was here—things changed a lot since he left, and they made significant changes in the discount rate early in the week.

My question—and I want to follow my colleagues' line here just a minute because I really believe it is a confidence issue. I agree, it is a whole lot different than when we would have had a stimulus in the 1960s or even in the 1970s, because today we are more a service-oriented economy than we were 30 years ago. Then, we looked to create jobs in manufacturing and move things; today, the manufacturing piece is a little bit harder to get our arms around than it was earlier.

So my question is, you talked a little bit about the short-term effect, the three Ts. And the three Ts have sort of been—well, I guess we got here because housing is—not only the financial markets get hit, but we are starting to see the real ripple effect on Main Street versus Wall Street when these people have lost their jobs who were building the houses and the people who were selling the houses lost them. So it is affecting Main Street a whole lot more today than it was even 3 months ago.

So, today, it really is about getting it into people's hands. But it is also about jobs. Simply put, people need jobs, to go to work so they can buy things to keep it going. So I want to get back a little bit to this issue of those things that you can put in place.

We have talked about roads and infrastructure, and I think it is important, but I want to expand it just a bit; and I would appreciate your comment on it.

If you can't fit this stimulus package, how important is it for the economic viability and I think the long-term consequences for this country of our overall infrastructure, because today we see movement of populations at a rate that we haven't seen in a long time. Schools are bursting at the seams. Communities are unable to cope with the growth patterns, and we have a bill in we have been trying to move for a long time.

With plans on the shelf, ready to go, if we could just get some money into people's hands, we can put a lot of people to work across this country and a whole lot of infrastructural pieces. You commented on it sort of generally, and I would appreciate your comments even beyond this, because Chairman Rangel and several of us, about 216, are on a piece of legislation to do just that.

And I would appreciate your comment in the short term and in the long term in terms of sustainability of the economy.

Mr. ORSZAG. Well, let me clearly delineate and separate those two.

In the short term, again the concern with infrastructure spending in general is that the spendout rates tend to be very slow. So you get very little of the aggregate amount that you would appropriate actually spending out during the short term or during the first 6 months or first year during a period of economic weakness.

It may be possible to improve upon that general conclusion by targeting particular kinds of infrastructure, but the challenge then is how you choose to rapidly and target those things.

Over the long term, infrastructure is one of the things that leads to economic growth. It is a component of our physical capital which improves productivity and improves economic performance, and I think there are concerns that have been raised not only about the level of investment in that kind of public infrastructure, but perhaps as importantly, or maybe even more importantly, how we allocate it and how we price it, whether we are using what we put in place as efficiently as we could.

Mr. ETHERIDGE. Thank you. And I do happen to believe we have got to do something about schools to put something in place. Last week, Dr. Bernanke said when he was seated there that—I raised a question on $3 a gasoline as high, and it has been sustained now for a good period of time, is having an impact on people, on the average person, just trying to get to work. And I have noted when I go to the station, a lot of them will buy $2, $3, $5 worth, just enough to get to work and back.

His point was, and I wonder if you would agree, he said apparently at $3-plus, it is taking about a half a point off our gross domestic growth in this country. Would you agree with that number, because of the additional cost for petroleum?

Mr. ORSZAG. Each $10 increase in the cost of a barrel of oil, which is what I have in my head, imposes a drag on the economy of perhaps $50 billion or so per year.

Mr. ETHERIDGE. Thank you, Mr. Chairman.

Mr. ORSZAG. So that is a little under half a percentage.

Mr. SPRATT. We have a vote at 12:00, so we would like to move ahead with dispatch so we can finish and adjourn by the time the bell rings, or at least by the time the vote is imminent.

We will move next to Mr. Berry of Arkansas.

Mr. BERRY. Thank you, Mr. Chairman. Thank you for having this hearing.

And, Dr. Orszag, we appreciate you and your great knowledge of this subject. I don't know how you keep up with all of this stuff. I continue to be amazed. I have noticed, and this is—you are the only Director of CBO that I have ever dealt with because I just came on this committee when you came—became Director of the CBO. But——

Mr. ORSZAG. We are both doing all right so far, huh?

Mr. BERRY. Sir?

Mr. ORSZAG. We are both doing okay so far.

Mr. BERRY. Well, I guess—we are still here.

Mr. ORSZAG. Yeah, we are still here.

Mr. BERRY. I notice that when you refer to the debt, that you always refer to the publicly held debt, and you don't include the debt that we owe ourselves basically. Is there a reason for that or——

Mr. ORSZAG. Yes, there is. And the reason for it is that the publicly held debt is a better measure of the interactions between the government and the rest of the economy. When the publicly held debt goes up, that is really the measure of the credit that the government needs to draw upon from other sources. The debt that is owed from one part of the government to another is very important for programmatic purposes, but does not have the same macroeconomic consequences as debt held by the public, which is why I focus on debt held by the public.

Mr. BERRY. I guess my exception to that would be that by what I consider to be understating the amount of debt that we owe, it makes the American people think that we don't owe as much as—that the future may be a little bit better than it actually is would be my impression of that.

Mr. ORSZAG. That is not the intention. And obviously I would say not only is our long-term fiscal imbalance severe, but $5 trillion, which is the level of publicly held debt, is still a significant sum.

Mr. BERRY. Yeah, I think so, too. In Arkansas we completely agree with that.

My other question to you is this. I remember back in '01, the administration was saying that if we just cut taxes and stimulated the economy, that things would be so good that we would pay off all of the debt, and that we wouldn't even have any government bonds to invest in, we wouldn't be worried about the—about the rating of the bonds; there just wouldn't be any, we would be so rich.

And I remember a little fellow named Mitch Daniels coming to the Blue Dogs and explaining to us—because we didn't understand it, and we still don't—that if we just vote for these tax cuts, that there would just be money running in the streets, and the only danger would be the—that we wouldn't have any national debt. And then again we—in '03, we heard these same arguments. And then I have heard my colleagues from across the aisle today talking about what a wonderful thing that was, and all the good that it has done, and what we need to do is more of it. If that is the case—and like I say, I still don't understand that. I missed it somewhere. If all of those things were such a wonderful idea and such great economic policy for this country, how come we are in the mess we are in today? It seems—would you agree we are in a mess? That may be a little bit too "one horse store" for you. But I——

Mr. ORSZAG. I would say that our fiscal—our long-term fiscal condition is undesirable, and short-term economic conditions are also problematic.

Mr. BERRY. If these tax cuts stem—work all this magic that we hear about, I just—I am mystified as to why we have got these problems. And that is all I will say about that.

Mr. ORSZAG. Okay, then.

Mr. BERRY. Thank you, Mr. Chairman.

Chairman SPRATT. Thank you, Mr. Berry.

Mr. Becerra.

Mr. BECERRA. Thank you, Mr. Chairman.

Dr. Orszag, good to see you again. Thank you very much for your testimony.

Actually let me ask us to step back for just a second and consider this conversation. I think it is actually stunning, it is breathtaking to think that here you are today. Last week we had Chairman Bernanke of the Federal Reserve talking to us about how we better do something because this economy is diving into the tank. And so I am assuming that you will agree that it is fair to say that the best of times of this economic period of growth—or this period of economic growth—the so-called good times are now behind us.

Mr. ORSZAG. We are in a period of significant economic difficulty during the short term.

Mr. BECERRA. I love the way economists say that. So the best of times in this period of economic growth are gone, and tomorrow the horizon for the economy and for the American people is not as bright. Some would say it is dim as compared to what it was in previous years.

Yet today after this period of economic boom, we have more Americans who have lost their health insurance coverage today. Forty-seven million Americans today don't have health insurance coverage. Six hundred million—600,000 more children became uninsured back in 2006. And in 2006, that number had reached almost 8.7 million kids. I suspect after 2007, the numbers will increase.

Poverty in America increased so that today one in eight Americans, some 36½ million Americans, live in poverty; one in every six American children lives in poverty today. That is some 13 million kids. And that is after the best of economic times.

But hold your breath, because the rest of the story was reported in the L.A. Times about a week or so ago—less than a week ago—when in an article they mentioned that Wall Street brokers made records amount of money.

Just some quick lines from the article: Wall Street's five largest investment firms paid record amounts of compensation in 2007 despite the fact that three of the five firms posted quarterly losses as a result of the souring investments in subprime mortgages. These five brokerage firms shelled out $65.6 billion in compensation and benefits last year. Sixty percent of those $65½ billion came in the form of year-end bonuses at the time that we saw things tanking. Merrill Lynch, which just reported a quarterly loss of $9.8 billion and in 1 year lost 43 percent of its value, is paying its top executives major bonuses. These bonuses—these numbers are based on calculations for about 186,000 employees in the Big Five firms. The average payout was $211,000 per executive. That is about four times the average household income in the U.S. That was just the bonus. Total compensation for these 185,000 employees averaged $353,000.

By the way, they make a little note here in another paragraph. These payouts they are talking about don't include the pays for the top executives of these firms, which have yet to be calculated. These are the middle managers, sales force guys that are making that kind of money.

It seems kind of strange that now that we are talking about difficult times, we forget that there are a lot of folks that never got to take advantage of this, and there were some folks that took drastic advantage of the good times. And so I think it is worth it for us to step back.

I wanted to also mention as we talk about—I keep hearing my colleagues on the Republican side talk about these tax cuts that are going to expire and how there will be a tax increase. And I appreciate that you are trying to be an economist in responding to questions about it, the so-called tax increase in 2011 and 2012. I think my Republican colleagues should remember that they are the ones that imposed this formulation that required these tax cuts to expire. So this Republican tax increase, if you want to call it a tax increase, should be called what it is. It was an automatic, prearranged return to the tax rates that we had before, any tax increases due to the Republican measures that gave us these tax cuts to begin with.

By the way, unless you disagree with this number, my understanding is that over the next 17 or so years, the cost of these tax cuts, were we to extend them forward beyond 2011 to, say, 2017, would cost us about $7.2 trillion. That is more than it would cost us to make sure that we take care of any shortfall in Social Security for the next 75 years. And so I think if we put it all in context, we get a sense of where we are.

And a final comment and perhaps a quick question is if we have a budget fight last year in December where we differed with the President to the tune of $22 billion—we wanted to give more money for NIH, for cops on the street, education—how does that compare to the amount of money that we may see now put out without paying for it in a stimulus package of somewhere between 100- to $150 billion.

Mr. ORSZAG. It is a lot smaller.

I would just note quickly on the other point you made, I am not sure about the 17-year figure, but a lot of the comparisons that I have seen that do that sort of thing compare nominal dollars to a present-value figure for Social Security, which would not be something I would want to do.

Mr. BECERRA. And just to make it clear for clarification, the present value of the shortfall in Social Security would be about 4.7 trillion, I am told. And the present value of the tax cuts extended for about 17 years would be about $7.2 trillion. And if it is incorrect, please—I appreciate——

Mr. ORSZAG. That sounds high to me. If extended over 75 years, you may get a figure of approximately that large. But 17, I don't think so.

Mr. BECERRA. Okay. Or perhaps that means it is the extension over—for a permanent period of time. Either way it is more than what it would cost us to stabilize Social Security.

Mr. ORSZAG. The present value of the Social Security imbalance over the next 75 years is somewhere—it depends on whose numbers you use, but it is well under 1 percent of GDP. The tax legislation, if it is not eroded over time by the alternative minimum tax, amounts to about 2 percent of GDP.

Mr. BECERRA. Thank you. So about twice as much it would cost for the Social Security shortfall to be taken care of?

Mr. ORSZAG. In present value.

Mr. BECERRA. Thank you, Dr. Orszag.

Chairman SPRATT. Ms. Moore of Wisconsin, who only 2 days ago was in Marion, South Carolina, where she appeared in Mount Pisgah Baptist Church out of nowhere like a swirling dervish. Welcome back to Washington from Marion, South Carolina. Ms. Moore, the floor is yours.

Ms. MOORE. Thank you so much, Mr. Chairman.

And thank you, Dr. Orszag.

Before I ask my question, I just wanted some clarifications. When Congresswoman Schwartz was talking to you about—about what would be an economic stimulus, you made a statement that it didn't matter where people spent the money. And I thought I heard an exchange where there was a suggestion that paying off credit card debt would be a stimulus. But I thought—and—that—I just want to clarify that that would not,

Mr. ORSZAG. By "spend the money," I did not mean paying off credit card debt.

Ms. MOORE. Right.

Mr. ORSZAG. I meant spend the money on—whether you buy food or you buy clothing——

Ms. MOORE. She also talked about paying a health care premium. Do you—is that a—is that a stimulus? She seemed to try to elicit that response from you. But I didn't——

Mr. ORSZAG. No, not really. When you purchase health care—yes, when you purchase health care——

Ms. MOORE. Well, people go to Target, Target and Payless Shoes and so on. Okay. Good clarification.

Now, Mr. Becerra and others—in your papers it really seemed to lay it out that the lower the income family, the greater the stimulus effect because they are bound to spend it right away. If you give it to—if I were to get one of these rebates, for example, I know I would pay off credit card debt, not an economic stimulus. Others might say that.

Do you—don't you find it ironic as you heard Mr. Becerra and others mention that really the lowest, lowest, lowest-income families really are not going to benefit by any of the strategies that are currently on the table? For example, unemployment insurance—the unemployment rate is 5.2 percent, but in my district, for example, those discouraged workers—we have 17 percent unemployment among white men, 22 percent unemployment among Hispanic men and 48 percent unemployment among black men. These are people who are not going to be eligible for unemployment insurance if they haven't been in the system.

Same thing with—like you talked about the 13 million poor children. These 13 million poor children are in families probably headed by women who, under the old system, AFDC—perhaps you could get some sort of check for them. They won't be eligible for the EITC. They are probably off TANF because it is time-limited, sanctioned off.

Don't you find it ironic that the people who could stimulate the economy most probably are outside of the reach of our targeting and timeliness?

Mr. ORSZAG. It is true that the unemployment insurance system has holes in it, especially for part-time and some lower-income workers. Food stamps tend to do somewhat better in reaching the very bottom of the income distribution.

Ms. MOORE. But the food stamps are very underutilized. Wouldn't you agree with that? I mean, if someone is on disability insurance, for example, they get $10 a month SSI. I mean, people don't even bother to show up and stand in line for the $10 a month.

So my question before I run out of time is, is—there is no definition in your book on automatic stabilizers, so I don't know what that means. But do you think that, given the economy moves in certain cycles, that it would be worth it for us to build some sort of infrastructure for identifying these poorest of the poor? Because there is all kinds of codewords within this Congress about who we want to help, workers and middle-class families, and help businesses trickle down, but there is no strategy for getting the money into the hands of the people who, in fact, would stimulate the economy the most.

Mr. ORSZAG. What I would say is in periods of economic weakness, which are again unusual, the normal tension between being warm-hearted and cool-headed evaporates because you can be both warm-hearted and cool-headed at the same time, the more money you can get to low- and moderate-income households. And you are right, that many of those households don't qualify for unemployment insurance under current eligibility, and there are, you know, various other imperfections in the existing system.

Ms. MOORE. So this economic stimulus—I mean, there are millions and millions of people—I guess I am calling them the want-to-be worker class, people who are eligible for work. We have basically put our children in a situation where if their parents don't work, they can't get any economic support by having ended the Aid to Families With Dependent Children program.

So this is a class of people that would spend the money. I mean, they would be in Wal-Mart the next day with their checks if they could get it. And I certainly hope that this Congress, this committee will really take the advice of the economists and try to figure out a way to get money in the hands of the people who need it the most.

And with that, my time unfortunately has expired.

Chairman SPRATT. Mr. Bishop.

Mr. BISHOP. Thank you, Mr. Chairman.

And I am sure, Dr. Orszag, you are anxious to move on.

Mr. ORSZAG. No, no, no. I was trying to answer a question. But, no.

Mr. BISHOP. We were all talking about this mantra of timely, targeted and temporary for the economic stimulus package, and it just seems to me so remarkably self-evident that two programs that fit all three of those criterions are unemployment benefits and extension of food stamps. And my understanding is that unemployment benefits have—are estimated to have an economic payoff of about 2 to 1 in terms of dollars spent, and food stamps of about 1½ to 1, and yet they are resisted by—certainly by our friends on the other side, resisted by the White House.

And so my question is, is there any nonideological argument that is rooted either in economic theory or in empirical evidence that says that those two programs would not be stimulative? Or is the opposition purely ideological?

Mr. ORSZAG. I wouldn't want to characterize opposition or support. What I would say is that from the perspective of short-term economic stimulus in a period of—these unusual periods of economic weakness, things like food stamps and unemployment insurance benefits were ranked by the Congressional Budget Office as having relatively high bang for the buck precisely because they can get money out the door fast to people who will spend most of it.

Mr. BISHOP. And infrastructure exists to handle the program.

The same question for providing tax rebates to those who pay payroll taxes, but do not pay Federal income tax. Is there any, again, argument rooted in economic theory that says that that would not be stimulative?

Mr. ORSZAG. The more that you target those types of households who tend to be lower income, the bigger bang for the buck you generally get.

Mr. BISHOP. And what would our mechanism be if the person does not pay Federal income tax? What would our mechanism be to give them a rebate? Would it be a rebate on payroll taxes? Would it be an extension of the Earned Income Tax Credit?

Mr. ORSZAG. There are a variety of ways in which it could be done. The vast majority—in fact, almost all people who have wage income file a tax return even if they don't owe income tax liability. And indeed if you were going to make a rebate refundable, you would probably want—and base it on 2007 tax information, you would probably want to limit it to those with wage income, because if not, you could get a very substantial increase in filing among people who don't have wage income in order to get a rebate. What you could do is—again using—once the IRS is done processing the 2007 tax returns, take anyone who reports—who files a tax return and has reported wage income, design whatever structure you want and basically mail them a check.

Mr. BISHOP. Okay. Thank you, Mr. Chairman.

Ms. MOORE. Would you yield some of your time to me?

Mr. BISHOP. Of course. I would be happy to.

Ms. MOORE. Did you just tell him that—you just said that you would want to limit it to people who had wage income, otherwise you would have all these other people filing. Wouldn't that help? I mean, if people filed, and they didn't have any wage income or very little, wouldn't that help reach the lowest of the low-income?

Mr. ORSZAG. Those nonfilers tend disproportionately to be elderly households.

Ms. MOORE. Why wouldn't we want to help them?

Mr. ORSZAG. Let me answer it in two ways. It is not that you wouldn't want to help them, but two answers. First, as I have already noted, there is a very substantial concern about timing involved here. If you had a massive increase in filing during the 2007 tax return season, I don't know that the IRS would be able to wrap it up even on time, and that would delay the sending of all of the checks.

The second thing is for whatever it is worth, and the evidence is not great on this, but for whatever the evidence is worth, at any given level of income, it appears that, if anything, elderly households have a lower marginal propensity to consume than nonelderly households. So all else being equal at the same level of income, sending the dollar to an elderly household may not have quite as much kick to it as a nonelderly household. But that is obviously—you may want to do it for other reasons anyway. I would, though, be very cautious about overloading the IRS system at this point if you want to get checks out in a timely fashion.

Ms. MOORE. Well, it would help primarily the elderly. But that other class that I just described to you of those people who just recently were kicked off TANF, for example, it would help those households tremendously to be able to file an income tax. I mean, there are a lot—I mean, I think your paper even described that there are many more households in that situation.

With 3 seconds left, let me ask this question. Is there any—in the long term, in the long run, don't you think we need to reform our unemployment metric system so that we can find a way to measure those people who are eligible for the workforce, but are not working? Because, you know, this 5.2 unemployment rate, I can tell you—I can look out the window of my home and know that that is not correct.

Mr. ORSZAG. Well, we actually have a system in place. We just don't tend to use those measures as much. But, for example, if you examine the ratio of employed people to the population rather than the number of unemployed people to the labor force, the labor market over the past few years looks much weaker. We basically have had a significant—we haven't yet had the employment population ratio rise back up to—or the share of the population working would be the simplest way of putting it—rise back up to the levels that we saw in the late 1990s, and that may be a better indication for many purposes of the overall state of the labor market than the official unemployment data which require that people be actively searching for a job in order to be counted.

Ms. MOORE. I just think it is worthless at a time like this, you know, if the economy were to get weaker than it is, if we were to actually move into a depression or a recession, we would actually be totally incompetent at delivering money to those people who are starving. Thank you.

Chairman SPRATT. Thank you.

And one final housekeeping term, the issue of—let me ask unanimous consent that all Members who did not have an opportunity to ask questions to submit the questions for the record.

Dr. Orszag, thank you for your clear and forthright and expert testimony. You have helped us tremendously. Let me thank you and CBO also for a fine piece of work on the budget and economic outlook for the forthcoming period. We look forward to working with you towards sensible budget policies, and we very much appreciate your help.

Can I ask one final question?

Mr. ORSZAG. Sure.

Chairman SPRATT. You have put three graphs on the front page. They have displaced the health care graph that we have been accustomed to seeing as your logo almost. The very top one indicates the percentage of mortgage delinquencies by different adjustable-rate mortgages.

Mr. ORSZAG. Yes.

Chairman SPRATT. One is subprime, and the others are conforming or prime——

Mr. ORSZAG. Right.

Chairman SPRATT [continuing]. ARM mortgages. If you look at that, it appears that as recently as '98, '99, 2000, 2001, the percentage of adjustable-rate mortgages which were subprime and delinquent was well above 15 percent, whereas the prime adjustable-rate mortgages were significantly below 5 percent. So for some time now, ARMs, subprime ARMs, have been three times—delinquencies have been three times as much or as frequent as under prime

ARMs. How do you account for the fact that we are now just seeing the markets get spooked by subprime mortgages when this problem has been with us for several years?

Mr. ORSZAG. One significant change is the volume of subprime ARM activity. So this is the share of the outstanding subprime ARMs. But the level of activity in subprime ARMs skyrocketed over the past several years, and so the aggregate amount went up substantially relative to, say, the late 1990s.

Chairman SPRATT. I know from the experience of running a small bank that the examiners would chew you out when your loans get more than 1 percent delinquent. And I don't know why it took us so long to get around to recognizing what was happening in the subprime market.

Mr. ORSZAG. And, Mr. Spratt, if I could just join you quickly in thanking the CBO staff not only for the work on the outlook, but also for that stimulus options report that was undertaken in a very compressed time schedule.

Chairman SPRATT. Thank you very much indeed. That concludes our hearing.

[Whereupon, at 12:18 p.m., the committee was adjourned.]

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