Statement of
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before the

Committee on Appropriations
United States Senate

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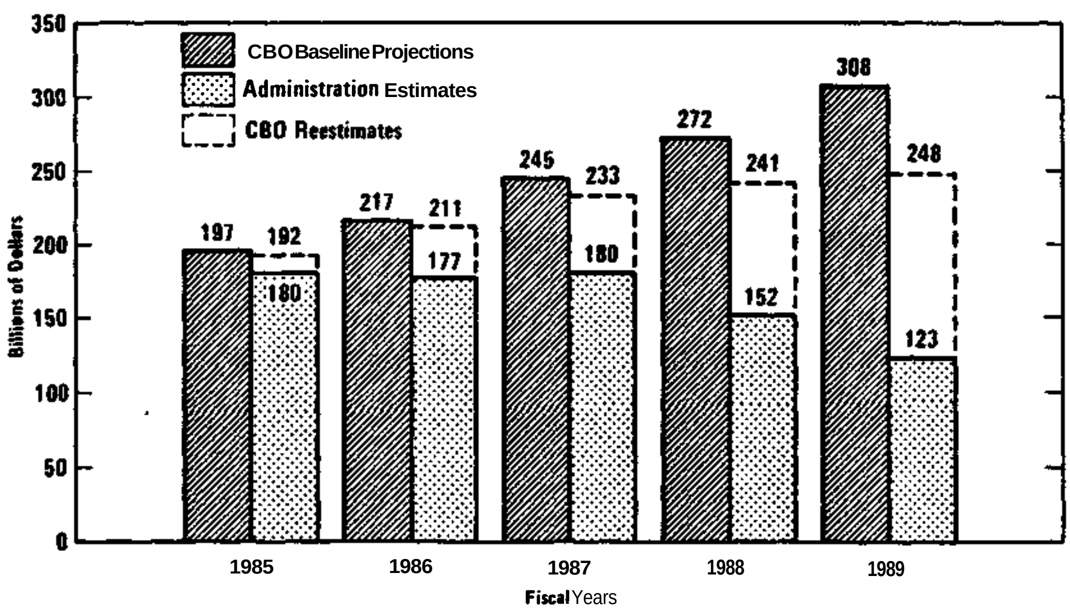
Mr. Chairman, I am pleased to have the opportunity to appear this morning before the Committee to present the Congressional Budget Office's (CBO's) analysis of the President's budget for the upcoming fiscal year. Copies of our analysis, which was prepared at the request of this Committee, have been distributed to Members and my statement this morning will summarize its findings.

The Administration's budget proposals for fiscal years 1985-1989, as set forth in the February budget documents, do not represent major changes in current policy, either in terms of revenues or in terms of expenditures. As a consequence, using our economic assumptions and estimating methods, CBO projects that the budget deficit under the Administration's proposals would rise steadily during the next five years to nearly $250 billion by 1989 (see Figure 1). The difference between our estimates of the budgetary impact of the Administration's proposals and those contained in the

Figure 1.
Federal Budget Deficit



President's budget document can be attributed largely to different economic assumptions for 1986-1989, particularly for interest rates.

THE ADMINISTRATION'S BUDGET PROPOSALS

Under current policies, the Congressional Budget Office projects very large and growing deficits, rising from nearly $200 billion in 1985 to over $300 billion in 1989. As a percent of gross national product (GNP), the baseline deficits would decline from 5.3 percent in 1984 to 5.0 percent in 1985 but rise thereafter, reaching 5.7 percent in 1989. The CBO baseline budget projections were presented in detail in our recent annual report to the Budget Committees, and are summarized in Table 1. 1/ The numbers shown in this table have been revised somewhat to reflect new information contained in the President's budget about spending programs, and also to reflect revised assumptions about inflation in the defense sector.

The President's budget for 1985 proposes relatively modest increases in revenues, and reductions in total spending from the levels projected by CBO under current policies. Proposed increases in defense spending would be offset more or less by reductions in nondefense spending. The Administration's budgetary proposals would hold the deficit-to-GNP ratio at about 5 percent during the next three years and reduce it to 4.6 percent by 1989. Thus, deficits would remain very high by recent historical experience. The deficit-to-GNP ratio for the 1980s would average 4.4 percent, as compared with 0.4 percent in the 1950s, 0.8 percent in the 1960s, and 1.9 percent in the 1970s.

1/ See the Congressional Budget Office, A Report to the Senate and House Committees on the Budget, Part I: The Economic Outlook, Part II: Baseline Budget Projections for Fiscal Years 1985-1989, and Part III: Reducing the Deficit: Spending and Revenue Options (February 1984).

TABLE 1. THE BUDGET OUTLOOK UNDER CURRENT POLICIES AND THE ADMINISTRATION'S 1985 BUDGET PROPOSALS (By fiscal year)

	1984	1985	1986	1987	1988	1989
	In Billions of Dollars					
CBO Baseline a/						
Revenues	663	733	795	863	945	1,016
Outlays	852	930	1,012	1,109	1,217	1,323
Deficit	189	197	217	245	272	308
Administration's Program as Estimated by CBO						
Revenues	665	741	807	878	964	1,039
Outlays	851	933	1,018	1,111	1,204	1,287
Deficit	186	192	211	233	241	248
	As a Percent of GNP					
CBO Baseline a/						
Revenues	18.6	18.7	18.7	18.7	19.0	18.9
Outlays	23.9	23.8	23.8	24.0	24.4	24.6
Deficit	5.3	5.0	5.1	5.3	5.5	5.7
Administration's Program as Estimated by CBO						
Revenues	18.7	19.0	19.0	19.0	19.3	19.3
Outlays	23.9	23.9	24.0	24.1	24.1	23.9
Deficit	5.2	4.9	5.0	5.1	4.8	4.6
Memorandum: Gross National Product (In billions of dollars)	3,563	3,910	4,251	4,612	4,987	5,379

a/ The CBO baseline figures are revisions of those appearing in Congressional Budget Office, *Baseline Budget Projections for Fiscal Years 1985-1989* (February 1984).

The Administration's 1985 budget reflects basically the same priorities as its 1984 budget proposal, although the size of the proposed policy changes has been scaled back. Proposed tax increases are substantially smaller than last year, primarily because the Administration is no longer proposing a contingent tax increase beginning in 1986. The Administration's defense program is somewhat smaller than that proposed a year ago, although the requested funding levels are still greater than those included in the Congressional budget targets last year. No new proposals are made for the Social Security and railroad retirement programs, which were subject to major legislative reforms last year. Finally, the Administration is no longer requesting or has reduced in size a number of cuts in entitlement programs and in nondefense discretionary spending that it has sought unsuccessfully in the past.

The estimated budget effect of the Administration's policy proposals would be to increase revenues by a total of $77 billion over the next five years, and to reduce projected outlays by $38 billion relative to the levels in our baseline projections. The total deficit reduction for 1985-1989 is estimated by CBO to be $115 billion, as shown in Table 2. Most of this reduction occurs in 1988 and 1989 under our projections. For the next three years, which will be the period covered by the next Congressional budget resolution, we estimate that the Administration's budget proposals would reduce projected deficits by only $24 billion compared with the CBO baseline. The Administration shows a greater reduction from its current services levels, but that is because its current services projections include the cost of last year's defense proposals as estimated in the Administration's 1984 Midsession Review. CBO uses as a starting point the lower targets for defense budget authority contained in last year's Congressional budget resolution.

TABLE 2. THE ADMINISTRATION'S DEFICIT REDUCTION PROPOSALS AS ESTIMATED BY CBO (By fiscal year, in billions of dollars)

	1985	1986	1987	1988	1989	Cumulative Five-Year Total
CBO Baseline Deficit	197	217	245	272	308	1,239
Proposed Changes						
Revenues						
Taxation of Health Insurance Premiums	-4	-6	-8	-10	-12	-40
Other Tax Increases	-6	-10	-12	-14	-17	-59
Tax Reductions	2	4	5	5	5	22
Subtotal	-8	-12	-15	-18	-24	-77
Outlays						
National Defense	10	21	23	20	11	85
Entitlements and Other Mandatory Spending	-4	-6	-9	-12	-15	-46
Nondefense Discretionary Spending	-2	-5	-7	-12	-17	-44
Offsetting Receipts	*	-1	-2	-4	-6	-13
Net Interest	-1	-2	-3	-5	-10	-20
Subtotal	3	7	2	-13	-36	-38
Total Policy Changes	-5	-5	-13	-32	-60	-115
President's Budget as Estimated by CBO	192	211	233	241	248	1,124

Revenues

The Administration's revenue proposals contain both tax reductions and tax increases. While contingency tax proposals in last year's budget are not repeated, a number of other tax proposals have been put forward again. This includes the largest revenue-raising item--a proposal to impose income and Social Security taxes on employer-paid health insurance premiums in excess of certain thresholds. This is projected to raise $40 billion in revenues over the next five years. Together with increased premium charges for Supplementary Medical Insurance (SMI) and spending reductions for Medicare and Medicaid, about $60 billion of the cumulative five-year deficit reductions proposed by the Administration would be targeted on the health sector.

Other revenue-raisers proposed in the President's budget include limitations on the use of tax-exempt bonds for private businesses and for students, substantially the same as those contained in H.R. 4170, and various proposals with regard to tax shelters, accounting procedures, and corporate tax abuses, many of which also have been discussed recently by the tax-writing committees. These and other revenue-raising proposals together are estimated to raise another $59 billion in revenues over the next five years.

The budget also contains a number of proposals that would reduce projected revenues by a total of $22 billion between 1985 and 1989. These include tax incentives for employers in economically distressed areas designated as enterprise zones, tuition tax credits for parents whose children attend private elementary and secondary schools, and changes in the tax treatment of life insurance companies. The largest revenue reduction proposal is the revision of the tax treatment of life insurance companies, which was considered by both the House Ways and Means and the Senate Finance Committees in 1983.

Defense Spending

The President's budget proposes $314 billion in budget authority and $273 billion in outlays for national defense programs in 1985. This is $16 billion higher than the budget authority target for these programs contained in last year's budget resolution, and $10 billion above our baseline defense outlay projections for 1985. Over the next five years, proposed funding for defense programs exceeds our baseline projections by a cumulative total of $83 billion in budget authority and $85 billion in outlays.

After adjusting for CBO's projection for inflation, we estimate that the current dollar value of the Administration's defense proposals for 1985 represent a 12 percent real increase in budget authority over 1984 appropriated levels, compared with a 3.1 percent real increase passed by the Congress last year. For 1986, the projected real increase is 7.7 percent, and for 1987-1989 about 2 percent per year. As a result of the much lower real growth projected for the period after 1986, annual real growth over the entire five-year period would average 5.1 percent. These real growth projections for defense programs are lower than those projected by the Administration because, over the next five years, we are assuming somewhat higher inflation in the economy, and more particularly in the defense sector.

The interplay of the dollar requests and defense prices is important. If the Administration's dollar requests are accepted but CBO's price assumptions prove to be correct, the amount of money budgeted would not be enough to buy all of the weapons requested or to support the force levels proposed. In this case, either the number of weapons purchased and the force levels planned would have to be scaled back, or additional funds would have to be appropriated. The estimated budget impact of CBO's higher defense price assumptions amounts to 5 percent of projected budget authority over the next five years. This potential additional cost, which works out to $94 billion in budget authority and $54 billion in outlays, is not included in our estimates of the Administration's 1985-1989 budget proposals.

Relative to last year's budget proposals, the Administration's defense program is lower by $16 billion in budget authority for 1985 and by $42 billion for the 1985-1988 period. The lower funding proposals can be attributed mostly to lower projected inflation by the Administration and to reductions in planned purchases of aircraft, missiles, and ships. Also contributing to the lower proposed funding levels is a projected real decline by the Administration in the cost of a number of weapons systems. (This is the first time we have observed such a projected decline in our analyses of defense budgets.)

Nondefense Spending Programs

We estimate that the Administration's proposals for nondefense spending programs would lower projected outlays by $103 billion over the next five years, or less than 3 percent. The reductions from our baseline projections for 1985-1989 consist of $46 billion for entitlements and other mandatory spending, $44 billion for nondefense discretionary spending, and $13 billion in increased offsetting receipts. The indirect effect of the revenue increases and spending reductions would be to lower net interest costs by another $20 billion.

Reductions in entitlement outlays would be achieved through such measures as freezing target prices in the farm price support program, delaying scheduled cost-of-living adjustments for federal retirement benefits, shifting more costs to Medicare and Medicaid beneficiaries, and raising pension guarantee premiums. Other cost-saving measures include some reductions in means-tested benefit programs and consolidation of the child care and summer feeding programs into a nonschool food program grant to states. Many of these proposals were in last year's budget, and a few received some legislative action. The only increase proposed for entitlement programs is a 15 percent increase in veterans' readjustment benefits to be effective next January.

Spending for nondefense discretionary programs under the latest Administration's budget plan would increase by about 3 percent annually in nominal terms, compared with roughly 5 percent per year to keep up with inflation under our baseline projections. The largest reductions relative to our baseline projections are in the areas of housing assistance, education and training programs, highway and mass transit grants, and various commercial activities such as postal subsidies, small business loans, and uranium enrichment. A few areas would receive more funds than projected under current policies, such as assistance to Central America, veterans' health care, space programs, and air traffic control activities. The budget shows a large increase in funds for foreign military sales assistance, but this is the result of shifting off-budget financing for this program to direct loans and grants that would be recorded in the unified budget.

The projected increase in offsetting receipts, which has the effect of lowering net outlays, results primarily from a proposed increase in premiums for the SMI program. Under current law, SMI premiums are set at 25 percent of program costs through 1985, and are to be increased by the growth in the Consumer Price Index (CPI) thereafter. The Administration proposes that premiums be increased gradually to 35 percent of program costs by 1990.

CBO REESTIMATES OF THE PRESIDENT'S BUDGET

CBO's projections for the budgetary implications of the Administration's proposals are significantly different from those contained in the President's February budget. We project that revenues will be slightly lower and outlays significantly higher, especially after 1986. As a consequence, we estimate that the Administration's budget plan would result in rising deficits over the next five years instead of declining deficits. The bulk of the estimating differences result from different economic assumptions, especially for interest rates. Table 3 compares the CBO and Administration projections for the President's budget program, and shows how much of the estimating differences can be attributed to economic assumptions and how much to technical estimating differences.

The CBO and Administration economic forecasts for 1984 and 1985 are very similar (see Table 4). Projected growth rates for real GNP are almost identical. The Administration's short-run forecast for inflation is only slightly more optimistic than CBO's. Interest rates are lower in the Administration's forecast, but by less than one percentage point.

However, the Administration's longer-run projections for the 1986-1989 period are considerably more optimistic than CBO's. The Administration's projections show growth rates averaging about half a percentage point higher than CBO's, and inflation lower by a similar amount. The largest difference between the two projections is in the area of interest rates. The Administration's projections show substantially lower interest rates than CBO's, with the differential growing over time. Because of the rapidly rising levels of federal debt that must be serviced, CBO's higher interest rate assumptions account for $75 billion out of the $124 billion higher deficit projected for 1989.

TABLE 3. CBO AND ADMINISTRATION ESTIMATES OF THE ADMINISTRATION'S BUDGET PROGRAM
(By fiscal year, in billions of dollars)

	1984	1985	1986	1987	1988	1989
Revenues						
Administration Estimate	670	745	815	888	978	1,060
CBO Estimate	665	741	807	878	964	1,039
Outlays						
Administration Estimate	854	925	992	1,068	1,130	1,184
CBO Estimate	851	933	1,018	1,111	1,204	1,287
Deficit						
Administration Estimate	184	180	177	180	152	123
CBO Estimate	186	192	211	233	241	248
Differences in Projections						
Revenues						
Economic	-1	-1	-2	-3	-6	-7
Technical	-4	-3	-6	-6	-9	-13
Total	-5	-4	-8	-10	-15	-21
Outlays						
Economic	2	8	17	32	59	87
Technical	-5	*	9	11	15	16
Total	-3	6	26	43	74	103
Deficit						
Economic	3	8	19	35	65	95
Technical	-1	3	15	17	24	30
Total	2	12	34	53	89	124

* Less than $500 million.

TABLE 4. COMPARISON OF CBO AND ADMINISTRATION ECONOMIC ASSUMPTIONS (By calendar year)

	1984	1985	1986	1987	1988	1989
GNP (billions of current dollars)						
CBO	3651.2	3994.8	4339.0	4703.7	5083.5	5480.5
Administration	3642.4	3973.8	4319.2	4681.2	5059.0	5444.9
Difference	8.8	21.0	19.8	22.5	24.5	35.6
Real GNP (1972 dollars, percent change, year over year)						
CBO	5.4	4.1	3.5	3.5	3.4	3.3
Administration	5.3	4.1	4.0	4.0	4.0	3.9
Difference	0.1	0.0	-0.5	-0.5	-0.6	-0.6
GNP Deflator (percent change, year over year)						
CBO	4.7	5.1	4.9	4.7	4.5	4.3
Administration	4.5	4.8	4.5	4.2	3.9	3.6
Difference	0.2	0.3	0.4	0.5	0.6	0.7
Consumer Price Index (percent change, year over year) a/						
CBO	4.5	5.0	4.9	4.7	4.5	4.3
Administration	4.4	4.6	4.5	4.2	3.9	3.6
Difference	0.1	0.4	0.4	0.5	0.6	0.7
Civilian Unemployment Rate (percent, annual average)						
CBO	7.8	7.3	7.0	6.8	6.6	6.5
Administration b/	7.9	7.7	7.5	6.9	6.2	5.8
Difference	-0.1	-0.4	-0.5	-0.1	0.4	0.7
3-Month Treasury Bills (percent, annual average)						
CBO	8.9	8.6	8.4	8.2	8.0	7.8
Administration	8.5	7.7	7.1	6.2	5.5	5.0
Difference	0.4	0.9	1.3	2.0	2.5	2.8
Inflation-Adjusted Interest Rates c/						
CBO	4.2	3.5	3.5	3.5	3.5	3.5
Administration	4.0	2.9	2.6	2.0	1.6	1.4
Difference	0.2	0.6	0.9	1.5	1.9	2.1

a. Consumer Price Index for urban wage earners and clerical workers.

b. The Administration publishes only the overall unemployment rate. The civilian adjustment is made by CBO.

c. Defined here as the Treasury bill rate minus growth in the GNP deflator.

The difference in interest rate assumptions apparently stems partially from budget assumptions. CEA Chairman Feldstein recently pointed out in testimony before the House Budget Committee that, if deficit-reduction measures beyond those proposed by the Administration are not enacted, interest rates are not likely to fall over the next five years as projected in the President's budget, and the growth of real GNP is likely to be slower than assumed. Thus, both the Administration and CBO seem to agree that, without substantial changes in fiscal policy, interest rates are likely to remain very high over the next several years.

Other estimating differences for revenues and outlays attributable to differing economic assumptions are relatively small compared with the differences in interest rates. CBO projects lower corporate income taxes as a result of lower corporate profits, and somewhat higher outlays as *a* result of slightly higher inflation and unemployment rates, particularly after 1986. These estimating differences account for another $20 billion of the higher deficit in 1989 projected by CBO.

Technical Estimating Differences

Technical estimating differences between CBO and the Administration affect the deficit estimates by only $1 billion in 1984 and $3 billion in 1985. After 1985, however, CBO's technical assumptions add substantially to the deficit estimates--$15 billion in 1986 and $30 billion in 1989. On the outlay side, the largest technical differences relate to defense spending and to receipts from oil and gas production activities on the Outer Continental

Shelf (OCS). CBO believes that the Administration has underestimated the rate at which requested increases in defense budget authority will show up in outlays. Because of higher CBO defense spending rates, particularly for procurement of weapons systems, estimated outlays increased by $5 billion in 1986 and $10 billion in 1989. CBO also concludes that the Administration has overestimated likely OCS receipts by an average of $4 billion per year over the 1986-1989 period. On the revenue side, most of the technical differences are in the individual income tax estimates; they reduce estimated revenues by $3 billion in 1986 and $13 billion in 1989.

CONSEQUENCES OF LARGE DEFICITS

Federal deficits of the magnitude shown in the CBO baseline projections and under the Administration's 1985 budget proposals would have major consequences both for the economy and for future budgetary choices. Most economists agree that federal deficits of the size projected by CBO keep interest rates higher than they would be otherwise.

This conclusion is contested by a few analysts who contend that there is no historical evidence for a link between deficits and interest rates. But one should not expect to find in historical data a simple association between deficits and interest rates. Previous deficits experienced during peacetime have been much smaller than those now projected, and their impact on interest rates has often been overwhelmed by recessions, Federal Reserve policies, or international capital flows.

The current and prospective deficits are extremely large relative to past history. In fiscal year 1983, the federal deficit was about 107 percent of domestic net private saving and 34 percent of gross private saving. Our reestimate of the President's budget implies that unified federal deficits would be 79 percent of net private saving and 29 percent of gross private saving during the fiscal year 1984-1985 period. Fortunately, very large capital inflows from abroad have so far limited the rise in interest rates.

It should be emphasized that these capital inflows are not a costless remedy for deficits. If the capital inflows continued for a long time, foreign claims on U.S. output could rise to such a level as to reduce our standard of living significantly below what it would be with less government borrowing and less reliance on foreign capital. Moreover, dependence on foreign capital flows leaves us vulnerable to changes in the psychology of foreign investors. If, for some reason, capital inflows should dry up before the deficit situation is improved, interest rates in the United States would rise and the dollar's value would fall, thereby exerting upward pressure on our inflation rate.

In the presence of such risks, more than the usual degree of uncertainty has to be attached to any economic forecast. There is, in fact, much talk of the deficit "aborting" the economic recovery. Our best judgment, however, is that this will not happen in the next two years. We believe that the harm done by deficits accrues over the long run as the absorption of savings by the federal government leaves less for private capital formation and so reduces long-run growth in labor productivity. As a result, future standards of living are lower than they would be otherwise.

Another aspect of high deficits is the growing cost of financing them. The most striking feature of the CBO budget projections is the extremely rapid growth in outlays for interest on the debt. Net interest costs, which were between 1 and 2 percent of GNP for decades, are projected to rise from 2.8 percent of GNP in fiscal year 1983 to 3.8 percent in 1989 in our estimate of the President's budget. As a consequence of continuing large budget deficits, the stock of federal debt outstanding rises dramatically over the next five years, approaching 50 percent of GNP by 1989. In these circumstances, major spending cuts or tax increases are necessary just to avoid the possibility of explosive growth in interest outlays.

The rapid rise in the debt-to-GNP ratio also means that projections of future deficits are highly sensitive to the assumptions about interest rates, which are one of the hardest economic variables to forecast. A one-percentage-point error in the forecast, if continued through the projection period, implies a $30 billion error in the projection of the 1989 deficit.

MAJOR OPTIONS FOR REDUCING THE DEFICIT

It is now widely agreed that policy actions are necessary to reduce projected budget deficits. Given the composition and dynamics of the federal budget, there is a broad consensus that these actions will have to include both spending cuts and tax increases, but still considerable differences over what proportions of each are appropriate.

On the spending side, one must start with the fact that a large portion of federal outlays occurs in only a few budget categories. Table 5 shows CBO's estimates of the Administration's spending program by major categories. Defense, entitlements, and net interest account for 90 percent of the total spending projected for the 1985-1989 period, and will exceed total projected revenues by more than $550 billion.

If changes in projected spending for defense and entitlements are to be accomplished, they must be undertaken soon. Cuts in defense procurement show up in reduced outlays only after a long time lag. Cuts in entitlement programs, such as Social Security, Medicare, and federal employee retirement benefits, ought to be phased in gradually so that beneficiaries and providers of services have time to adjust.

CBO recently completed its fifth annual report on options for reducing the deficit. This report, which is part of our annual report to the Budget Committees, presents 138 options--not recommendations--for cutting spending or raising taxes.

In national defense, the options discussed contrast the difficult trade-off between short-term readiness efforts and long-term buildup of conven-

TABLE 5. CBO ESTIMATES OF THE ADMINISTRATION'S SPENDING PROGRAM BY MAJOR CATEGORIES
(By fiscal year)

	1984	1985	1986	1987	1988	1989
			In Billions of Dollars			
National Defense	235	273	315	352	387	419
Entitlements and Other Mandatory Spending	396	423	449	479	514	549
Nondefense Discretionary Spending	157	162	166	174	179	183
Net Interest	109	125	143	164	188	207
Offsetting Receipts	-46	-49	-54	-58	-64	-71
Total Budget Outlays	851	933	1,018	1,111	1,204	1,287
Off-Budget Spending	15	14	9	8	8	6
Total Outlays	866	947	1,028	1,119	1,212	1,293
			As a Percent of GNP			
National Defense	6.6	7.0	7.4	7.6	7.8	7.8
Entitlements and Other Mandatory Spending	11.1	10.8	10.6	10.4	10.3	10.2
Nondefense Discretionary Spending	4.4	4.1	3.9	3.8	3.6	3.4
Net Interest	3.0	3.2	3.4	3.6	3.8	3.8
Offsetting Receipts	-1.3	-1.3	-1.3	-1.3	-1.3	-1.3
Total Budget Outlays	23.9	23.9	24.0	24.1	24.1	23.9
Off-Budget Spending	0.4	0.4	0.2	0.2	0.2	0.1
Total Outlays	24.3	24.2	24.2	24.3	24.3	24.0

tional and nuclear weapons systems, with the sobering conclusion that to bring the Administration's defense budget down to 5 percent real growth—the rate incorporated in last year's budget resolution--would require $92 billion in cuts from defense budget authority between 1985 and 1989 (using CBO's defense price assumptions). To freeze defense budget authority at the 1984 level--adjusting only for inflation--would take cuts amounting to $356 billion in the next five years.

In Medicare and Medicaid, the CBO report illustrates each of the variety of ways that federal costs could be held down: by restraining payments to hospitals and doctors, by making patients or taxpayers pay more, or by shifting more of the costs to state and local governments. A key factor in cost control and in the solvency of the Medicare program will be how well the new prospective payment system works. It is much too early to tell.

Social Security and other entitlements (including agricultural price supports) represent such a large part of budget outlays that a wide variety of proposals are already on the table. Our options cover limits on cost-of-living adjustments, reductions in eligibility for some entitlements, restraints on federal employee retirement, and significant reductions in crop price supports.

The remainder of the budget that is subject to annual appropriations is made up of hundreds of relatively small accounts. Correspondingly, each option discussed in the section of our report on these programs yields relatively small budgetary savings. To eliminate a substantial fraction of the deficit from cuts in nondefense discretionary programs would require moving on many fronts at one time.

Our study concludes with a discussion of revenue-raising options. Here we have made a distinction between relatively small, specific changes in the tax code that, even if packaged together, would raise only relatively small sums and the bigger steps that could be taken to modify our tax system so as to raise yields. These bigger steps include major base-broadening measures, surtaxes, dropping or modifying indexing, and consumption taxes.

The analysis brings out clearly the difficulty of resolving the budget dilemma. The fact is that all spending does some good for someone and all taxes do some harm to someone, so no spending cut or tax increase will please everybody. Nonetheless, our budgetary predicament requires that the Congress make difficult choices and that it search for the least damaging package of deficit-reduction options that can command majority support. I hope our discussion helps this search.