Three Things to Know About the CBO Budget Report

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It's Christmas in the geeky budget world today. While everyone else is thinking about the Florida GOP primary, DC budget and tax wonks are reading the annual "CBO Budget and Economic Outlook." Here's my three takeaways after reading the report. They are by no means exhaustive:

1. **If all scheduled tax increases are avoided, tax revenues will still come in at historical levels.** CBO has to use a "current services baseline," which means they have to assume that Congress will let the path of current law run its course. That means that Obamacare is implemented, the 2001/2003 tax relief goes away (raising everyone's marginal tax rate), and the AMT ensnares 30 million families. However, CBO also realizes this won't happen, so they provide an alternative scenario that assumes that present tax policies are extended (Table 1-7).

If (when) that happens, tax revenues at the end of the CBO budget window will equal 18.3 percent of the economy. This just happens to be the 50-year historical average. Therefore, if your goal is to keep the tax burden where it has been for the past half-century, the easiest way to do that is to prevent all scheduled tax hikes from taking effect. One caveat--these figures do not include the tax increases in Obamacare, repealing of which may actually take the number slightly-below the historical average.

2. **Spending can grow by 2.3% per year after 2013, and you'd still balance the budget without raising taxes by the end of the CBO baseline.** Dan Mitchell of the Cato Institute has been pointing this out for years, and it's just as (more?) true in this CBO report as all the others. Spending can actually grow every year, roughly at the rate of inflation, and the budget can be balanced without raising taxes. At the end of the window (2022), both taxes and spending would be 18.3 percent of GDP. Again, the Obamacare tax correction would alter this number slightly, but you could still grow spending every year and balance the budget.

This means it really is true when we say, "Washington, D.C. doesn't have an under-taxing problem--it has an over-spending problem."

3. **Faster economic growth of 1 percentage point per year would increase tax revenues by $2.8 trillion over the CBO budget window without raising taxes.** This is all laid out in Table B-1. If real GDP growth was 1 percentage point higher over this window, tax revenues generated would equal an additional $2.8 trillion.

CBO assumes that real GDP growth will average about 3% per year, which is about in line with the historical average. However, the economy has been through a very slow-growth period. There's every reason to believe that pro-growth tax policy, spending restraint, regulatory constraints, a more humble foreign policy, and entitlement reform would generate higher-than-average economic growth for the next decade. If America makes the right fiscal and regulatory choices, 4% annual growth is not a pipe dream.

If that were to happen, tax revenues in 2022 (the last year of the window) would be $570 billion higher, or about 0.2% of GDP. That's probably enough to offset the lost revenue from repealing Obamacare, or pretty close to it.