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**FIVE-YEAR BUDGET PROJECTIONS:
FISCAL YEARS 1979-83**

HEARING
BEFORE THE
JOINT ECONOMIC COMMITTEE
CONGRESS OF THE UNITED STATES
NINETY-FIFTH CONGRESS
FIRST SESSION

DECEMBER 5, 1977

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FIVE-YEAR BUDGET PROJECTIONS: FISCAL YEARS 1979-83

MONDAY, DECEMBER 5, 1977

CONGRESS OF THE UNITED STATES,
JOINT ECONOMIC COMMITTEE,
Washington, D.C.

The committee met, pursuant to notice, at 10:03 a.m., in room 5302, Dirksen Senate Office Building, Hon. William Proxmire (member of the committee) presiding.

Present: Senator Proxmire.

Also present: G. Thomas Cator, William A. Cox, and L. Douglas Lee, professional staff members; Mark Borchelt, administrative assistant; and Charles H. Bradford, minority professional staff member.

OPENING STATEMENT OF SENATOR PROXMIRE

Senator PROXMIRE. The committee will come to order.

We are honored and pleased to have Mrs. Alice Rivlin, Director of the Congressional Budget Office, to discuss with us the 5-year budget projections prepared by her Office.

In my judgment, these long-term budget projections are one of the most important features of the Budget Control Act of 1974. They provide Congress with the basic information needed to begin early consideration of budget matters and they show clearly the commitments we have made for budget resources in future years.

The CBO's report this year is particularly important. Normally on November 10, the President submits estimates of the current services budget for the coming year; the Joint Economic Committee reviews these estimates and reports to Congress.

This year, the chairman of the Joint Economic Committee, the chairman of the Budget Committee, and the chairman of the Appropriations Committee agreed to a request from OMB for a 1-year experiment.

This year, the President's current services estimates will be presented in January with his budget proposal and, therefore, will be based on the same set of economic assumptions.

We hope that this change will increase the usefulness of the document. The JEC will report on the current services estimates in March when we submit our annual report.

The Congressional Budget Office has been helpful to us in the past and I trust we can call upon you again if this is necessary.

The Congressional Budget Office projections have been more helpful than OMB's because they cover a longer time horizon. Since there will be no OMB report until late January, your report assumes added significance.

As you know, I have long supported the notion that the only way to effectively organize and gain effective control over budget expenditures is to plan several years in advance. I am very pleased to see that your report demonstrates how much we can increase budget control by increasing planning horizons.

I am also pleased to see you have improved your projection methodology so you now take into consideration the impact of the budget on the economy as well as the impact of the economy on the budget.

As I read this report, it is in part pessimistic and part rather optimistic. You project an unemployment rate of 4.5 percent in 1983, which I think most people regard as optimistic.

But, then, you project an inflation rate of 6 percent, which I regard as very unfortunate if realistic.

The growth path necessary is optimistic in that it assumes stronger than average growth in non-Federal demand coupled with substantial amounts of economic stimulus.

Your report seems to confirm the conclusions of the Joint Economic Committee staff study released earlier this year which said it would be virtually impossible to achieve all the economic goals President Carter set forth for 1980.

Mrs. Rivlin, please proceed with your statement. I look forward to discussing these and other issues with you.

STATEMENT OF HON. ALICE M. RIVLIN, DIRECTOR, CONGRESSIONAL BUDGET OFFICE, ACCOMPANIED BY JAMES L. BLUM, ASSISTANT DIRECTOR FOR BUDGET ANALYSIS; AND JAMES CAPRA, CHIEF, PROJECTIONS UNIT

Mrs. RIVLIN. Thank you very much, Senator Proxmire.

Before I proceed, let me introduce the two gentlemen with me, James Blum, on my left, who is the Assistant Director for Budget Analysis at the Congressional Budget Office, and James Capra, on my right, who is the Chief of our Projections Unit responsible for preparing this report.

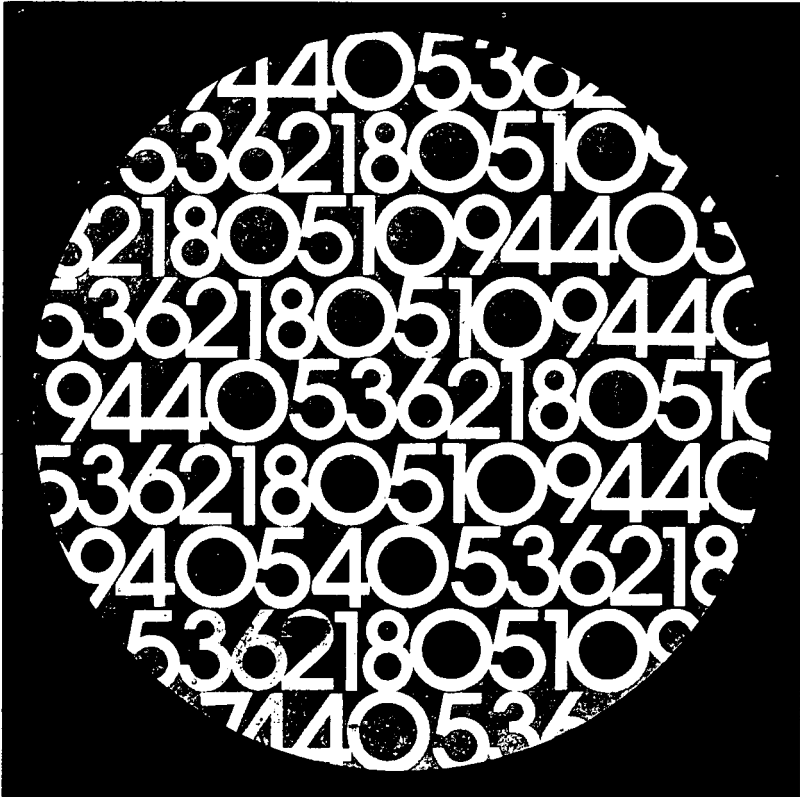
This morning we are releasing our report, "Five-Year Budget Projections: Fiscal Years 1979-1983." I ask permission that the report be entered in the record.

[The report referred to follows:]

December 1977

FIVE-YEAR
BUDGET
PROJECTIONS:
FISCAL
YEARS
1979-1983

As required by Public Law 93-344



CONGRESS OF THE UNITED STATES



CONGRESSIONAL BUDGET OFFICE

**FIVE-YEAR BUDGET PROJECTIONS:
FISCAL YEARS 1979-1983**

**The Congress of the United States
Congressional Budget Office**

NOTES

Unless otherwise indicated, all years referred to are fiscal years. For 1976 and before, fiscal years ran from July 1 through June 30 and were referred to by the years in which they ended. The Congressional Budget Act of 1974 changed the fiscal year to begin on October 1 and end on September 30. The interim between the old and new fiscal years, July 1 through September 30, 1976, is called the transition quarter; fiscal year 1977 began on October 1, 1976.

Details in the text, tables, and figures of this report may not add to totals because of rounding.

PREFACE

As required by section 308(c) of the Congressional Budget Act of 1974 (Public Law 93-344), this report by the Congressional Budget Office projects total new budget authority, outlays, and receipts for each fiscal year between 1979 and 1983. The act requires the report on federal budget projections to be issued as soon as practicable after the beginning of each fiscal year.

The primary purpose of these projections is to provide a neutral baseline against which the Congress can consider potential changes during its deliberations about the next annual budget. A longer-term framework is helpful in making annual budget choices because these decisions frequently have little impact on the budget in the short run but can significantly influence relative budget priorities over a period of several years.

The projections presented in this report are based on the estimated budget revenues and outlays specified in the Second Concurrent Resolution on the Budget for Fiscal Year 1978 (H. Con. Res. 341). This report contains estimates of expenditures and revenues under a current policy, or "no new policy change" concept for 1979-1983. In addition, the report includes estimates of the fiscal stimulus that would be required if the economy is to grow at an annual rate of 4.8 percent until the unemployment rate reaches 4.5 percent in 1983.

The Congressional Budget Act also requires the Congressional Budget Office to project tax expenditures for each of the next five fiscal years. A separate report on tax expenditure projections will be issued at a later date.

Alice M. Rivlin
Director

December 5, 1977

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SUMMARY

This report presents projections of federal spending and revenues over fiscal years 1979-1983. Federal spending and revenues are projected under the assumption of the continuation of current policies. In addition, estimates are made of the tax cuts or spending increases that would be needed in order to sustain the economic growth objective contained in the Second Concurrent Resolution on the Budget for Fiscal Year 1978.

Under current tax laws, projected receipts rise by 13.2 percent per year, from \$457 billion in fiscal year 1979 to \$751 billion in fiscal year 1983. As a percent of the gross national product (GNP), receipts rise from 20 to 22 percent. This increase is dominated by individual income tax receipts. Current policy outlays rise more slowly, from \$495 billion in fiscal year 1979 to \$655 billion in fiscal year 1983. Social security, medicare, and medicaid are responsible for almost half the increase in outlays. As a percent of GNP, outlays decline from 22 to 19 percent. This disproportionate rise in receipts as compared to outlays occurs because of the progressive nature of individual income taxes.

The projections of current policy receipts and outlays were estimated assuming real GNP growth of about 4.8 percent per year until the unemployment rate reaches 4.5 percent. If current policies are followed unchanged during the next five years, however, the federal budget will exert a restrictive influence on the economy because the receipts the government is taking out of the economy will rise much faster than the outlays it is putting back into the economy in the form of wages, purchases, and payments to individuals. For the economic assumptions to be realized, therefore, fiscal and monetary policy would in all likelihood have to be used to offset the fiscal drag exerted by the projected current policy budgets.

The magnitude of tax cuts or spending increases needed to offset the fiscal drag would depend on the strength of demand in the nonfederal sectors of the economy. Stronger nonfederal demand would mean that smaller tax cuts and spending increases would be needed to achieve the assumed growth rates. Under the assumption that nonfederal demand is slightly stronger than the average since World War II, roughly \$120 billion annually in additional budget stimulus -- tax cuts or spending increases -- would be needed by fiscal year 1983.

The projected budget deficit is estimated by comparing the additional budget stimulus needed to offset fiscal drag to the current policy margin

generated by the excess of current policy receipts over outlays. As long as the fiscal drag offset is greater than the current policy margin, the budget is projected to remain in deficit. As shown in the table, the fiscal drag offset would be greater than the current policy margin throughout the five-year period. By fiscal year 1983, the projected deficit would be \$19 billion.

(By fiscal years, in billions of dollars)

	1978 Second Concurrent Resolution	Projections				
		1979	1980	1981	1982	1983
Current Policy Receipts	397.0	457	519	590	668	751
Current Policy Outlays	458.25	495	529	565	606	655
Current Policy Margin	-61.25	-38	-10	25	62	96
Fiscal Drag Offset	--	29	51	74	101	115
Deficit (-) or Surplus	-61.25	-67	-61	-49	-39	-19

The projection of the deficit described above assumes nonfederal demand that is slightly stronger than the average over the past thirty years. This is not the only possible outcome. For example, if a business investment boom developed, either spontaneously or in response to expansionary monetary policy, or if growth in economic activity in the rest of the world stimulated United States exports, the need to offset the fiscal drag would be smaller and the size of the deficit would decline more rapidly, perhaps to a point of budget balance. On the other hand, if nonfederal demand grew very slowly, more expansionary policies and an increasing budget deficit might be needed to reach the assumed output and unemployment goals.

CHAPTER I. INTRODUCTION AND OVERVIEW

As a preparatory step toward the review of new budget proposals for fiscal year 1979, it is important to consider the probable future size and shape of the federal budget for fiscal years 1979 through 1983 if current policies are not changed. This report includes fiscal years 1979-1983 projections of federal spending and revenues under the assumption that current policies will continue. The current policy projection for fiscal year 1979 provides a baseline against which to measure the budgetary effects of policy changes proposed by the President or the Congress. The projections for fiscal years 1980-1983 provide insight into the long-run implications of current policies. In addition, this report illustrates the additional spending or tax cuts likely to be required to sustain the economic growth objectives adopted in the Second Concurrent Resolution on the Budget for Fiscal Year 1978.

The budget totals presented in this paper should not be construed as recommendations. Rather, they are intended to provide a glimpse of the probable long-run shape and direction of the budget under current policies, and to indicate approximately how much new spending or tax cuts will be needed if the economy is to continue to grow and move toward full employment.

ECONOMIC ASSUMPTIONS

Inflation, unemployment, and other levels of economic activity have major effects on revenues and outlays. For example, a declining unemployment rate will lead to lower outlays for unemployment compensation. On the receipts side of the budget, under current law a high rate of economic growth will lead to a more than proportional increase in revenues, because of the progressive nature of individual income taxes. In order to develop budget projections, therefore, explicit assumptions must be made about economic trends over the next several years.

The major economic assumption underlying the five-year budget projections in this report is a continuing recovery with declining unemployment. For 1977 and 1978 the economic assumptions, shown in Table 1, are taken from the conference report on the second concurrent resolution for 1978. For 1979-1983, the assumptions represent an extrapolation of the economic growth objectives in the second concurrent resolution, with real

economic growth -- as measured by the rate of growth in the gross national product (GNP) in constant dollars -- holding at approximately 4.8 percent through 1982 and dropping to 3.7 percent in 1983 as the unemployment rate reaches 4.5 percent (see Figure 1).

TABLE 1. AGGREGATE ECONOMIC ASSUMPTIONS: BY CALENDAR YEARS

Selected Economic Variables	1977	1978	1979	1980	1981	1982	1983
Gross National Product (GNP)							
Current dollar GNP (in billions of dollars)	1,898.0	2,107.0	2,333.8	2,582.2	2,853.9	3,156.4	3,465.2
Real GNP (in billions of 1972 dollars)	1,338.0	1,402.7	1,467.9	1,538.4	1,612.2	1,688.3	1,751.4
Growth rate of real GNP	5.0	4.8	4.7	4.8	4.8	4.7	3.7
Unemployment Rate (percent)	7.0	6.5	6.2	5.7	5.2	4.7	4.5
Consumer Price Index (percent change)	6.5	5.6	6.0	5.7	5.5	5.7	5.9

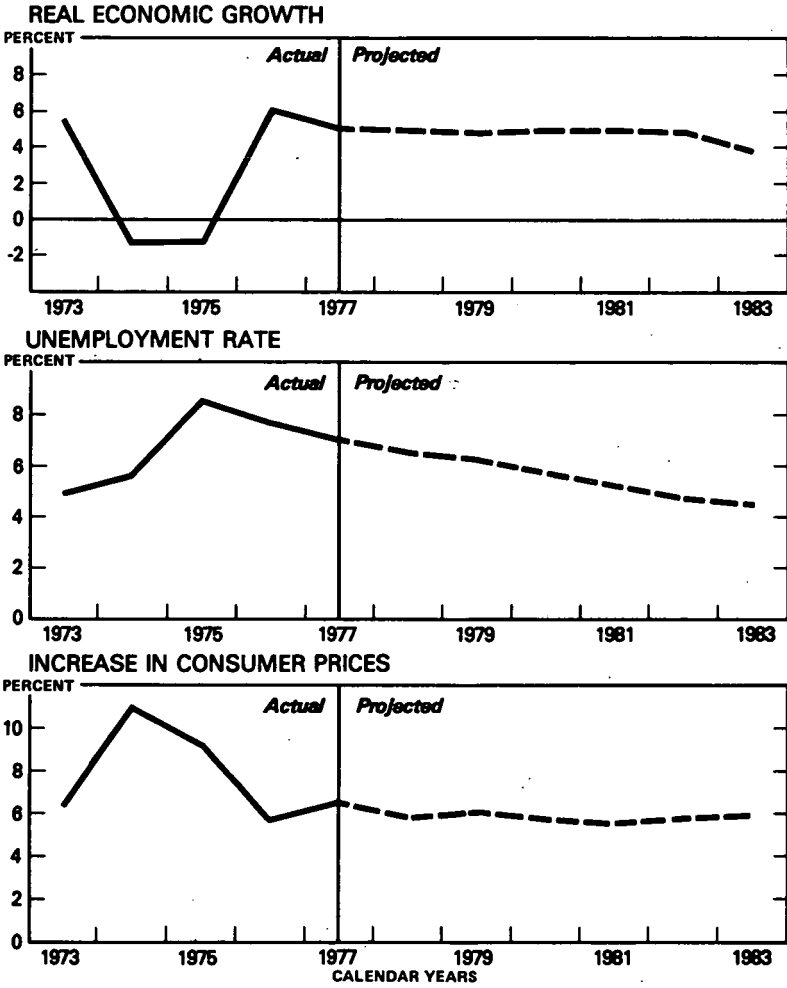
This growth path is consistent with the economic assumptions used for the previous budget projections of the Congressional Budget Office (CBO). With respect to inflation, the consumer price index (CPI) is assumed to rise at an annual rate of 5.5 to 6.0 percent between 1977 and 1983. The assumed inflation rates do not include the possible effects of pending energy or social security legislation.

The economic assumptions for 1979 through 1983 should not be construed as an economic forecast in the sense of being the best estimate of how the economy is likely to behave. Rather, they should be viewed as one of many possible long-run targets for the economy. The assumed growth path could be described as optimistic, but not unrealistic. The average rate of growth sustained since World War II has been 3.3 percent. During 1961 to 1966, the economy grew at an average annual rate of 5.4 percent. The assumed inflation rates might also be described as moderately optimistic. They are considerably above long-run historical experience but lower than the average inflation of the last several years.

BUDGET IMPLICATIONS OF THE ECONOMIC ASSUMPTIONS

Under current spending and tax policies, the budget implications of the economic assumptions are shown in Table 2. Receipts increase by about 13.2 percent per year under current law from \$457 billion in fiscal year 1979

Figure 1.
MAJOR ECONOMIC ASSUMPTIONS



to \$751 billion in fiscal year 1983. Current policy outlays rise at about half that rate, approximately 7.3 percent per year, from \$495 billion in fiscal year 1979 to \$655 billion in fiscal year 1983. As a percent of GNP, current policy receipts increase from 20 to 22 percent, while outlays decline from 22 to 19 percent. The dramatic rise in receipts as compared to outlays occurs because of the progressive nature of individual income taxes.

TABLE 2. FIVE-YEAR BUDGET PROJECTIONS a/: BY FISCAL YEARS, IN BILLIONS OF DOLLARS

	1978 Second Concurrent Resolution	Projections				
		1979	1980	1981	1982	1983
Current Policy Receipts	397.0	457	519	590	668	751
Current Policy Outlays	458.25	495	529	565	606	655
Current Policy Margin	-61.25	-38	-10	25	62	96
Fiscal Drag Offset	-- <u>b/</u>	29	51	74	101	115
Deficit (-) or Surplus	-61.25	-67	-61	-49	-39	-19

a/ For definitions of current policy margin, fiscal drag offset, and deficit, see page 5 of this report.

b/ It is assumed that the spending ceiling and revenue floor in the second concurrent resolution are consistent with the fiscal stimulus needed for the economy to grow at the rate of 4.8 percent in fiscal year 1978. If more or less fiscal stimulus is required, corresponding adjustments would have to be made in the estimates of the fiscal drag offset for fiscal years 1979-1983.

Under current policy assumptions, the receipts that the federal government would take out of the economy would be rising much faster than the outlays it would be putting back into the economy in the form of wages, purchases, and payments to individuals. Hence, the federal budget would be exerting a fiscal drag on the economy, making it unlikely, if not impossible, to achieve the growth assumptions shown in Table 1. For the target growth

assumptions to be realized, therefore, fiscal and monetary policies would, in all likelihood, have to be used to offset this natural tendency of projected current policy budgets to move in a restrictive direction.

If tax cuts or spending increases were used to offset the fiscal drag, their necessary magnitude would depend on the strength of the nonfederal sectors of the economy -- namely, the four major components of nonfederal demand: consumption, investment, state and local government purchases, and net exports. Stronger nonfederal demand would mean that smaller tax cuts or spending increases would be required to achieve the assumed economic growth rates. Conversely, weaker nonfederal demand would require larger tax cuts or spending increases to achieve the growth rates. To illustrate the requirement for additional spending or tax cuts, this report chooses one possible scenario for the growth in nonfederal demand, which is assumed to be moderate by historical standards -- stronger than the average of the post-World War II years, but somewhat weaker than the peak period of 1961-1966. ^{1/}

THE PROJECTED DEFICIT

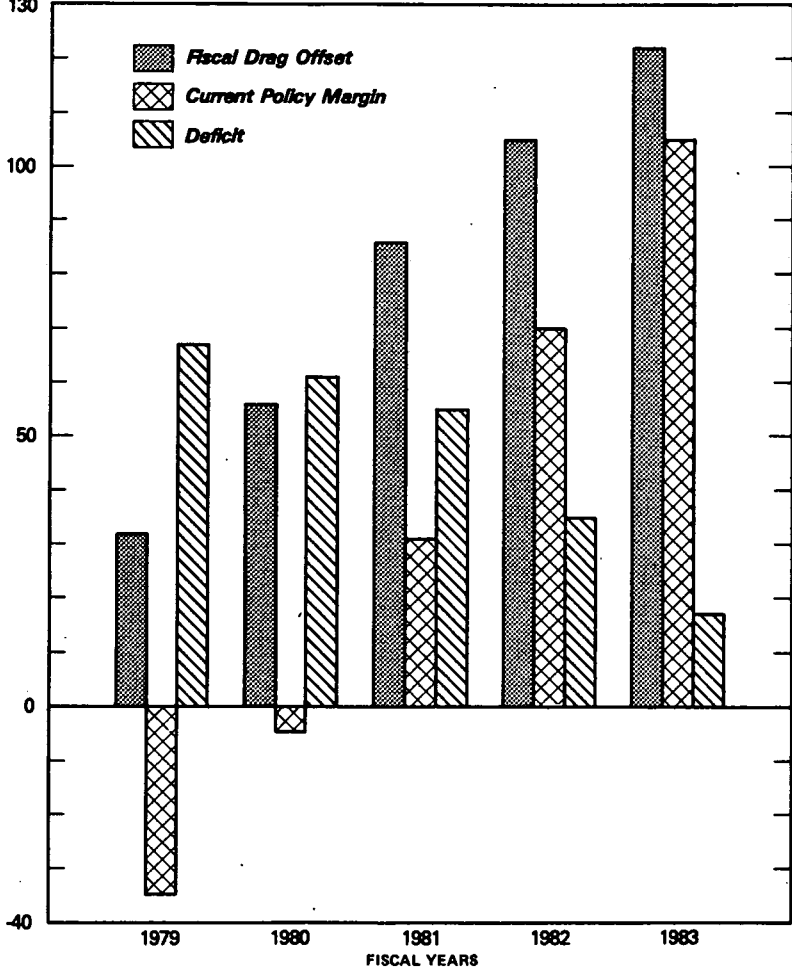
As noted earlier, if the economy were to follow the growth target assumed in this report, receipts would rise faster than outlays, exerting a drag on the economy that would itself tend to reduce economic growth. Assuming moderate nonfederal demand, approximately how much would taxes have to be cut or expenditures increased to offset the drag and keep the economy on the target growth path?

Rough answers to this question are shown in Table 2 and in Figure 2. The current policy margin indicates the excess of receipts over outlays that would develop if the target growth path were realized. The fiscal drag offset indicates a rough estimate of the amount by which taxes would have to be cut or spending increased to keep the economy on the growth path, if

^{1/} The personal saving rate (a reflection of consumption behavior) is assumed to average 5.9 percent. Real investment is assumed to grow at an average of 7 percent. State and local government purchases in real terms are assumed to grow at an average annual rate of 3 percent. Net exports are assumed on average to be nearly balanced over the five-year period. (See Closing the Fiscal Policy Loop, CBO Technical Analysis Paper, December 1977, for a detailed discussion of these major components of nonfederal demand.) Monetary policy is assumed to be sufficiently accommodative so as not to preclude the attainment of the nonfederal demand scenario.

Figure 2.

THE FISCAL DRAG OFFSET, CURRENT POLICY MARGIN, AND DEFICIT

\$ BILLIONS
130

the nonfederal demand were "moderate" as defined earlier. As long as the current policy margin is less than the fiscal drag offset, the budget would remain in deficit. For example, in fiscal year 1981 the current policy margin would be \$25 billion, the required fiscal drag offset would be \$74 billion, and the projected deficit would be \$49 billion. In fact, the current policy margin would be less than the required offset throughout the projection period. Consequently, under the economic assumptions specified earlier, the budget is projected to be still in deficit by fiscal year 1983.

The scenario just described is a plausible set of projections of the deficit over the next five years; it is by no means the only possible outcome. If monetary policy became more expansionary, if a business investment boom developed spontaneously, or if growth in economic activity in the rest of the world stimulated exports from the United States, the need to offset the fiscal drag in a current policy budget might be much less than under the above assumptions. This, in turn, could lead to a more rapid decline in the deficit than shown here. On the other hand, if the economy were subject to shocks of the kind it experienced in the early 1970s, or if business investment failed to grow sufficiently, more expansionary policies and an increasing deficit might be needed to reach the output and unemployment goals assumed earlier.

Furthermore, even if the assumptions about nonfederal demand turned out to be correct, the dollar amount of fiscal action required to meet the output and unemployment goals could vary, depending on which items in the budget were altered to meet the needs of fiscal policy. Generally speaking, purchases of goods and services have more impact per budget dollar on output and employment than broadly based tax changes or changes in income support programs. Public employment programs tend to have more impact on jobs than other instruments of fiscal policy. Specially designed tax changes, such as the investment tax credit, can have powerful effects on output and jobs after a lag of one or two years. These and many other special characteristics of the budget need to be taken into account in designing a detailed fiscal policy strategy. Not surprisingly, consideration of all the alternative economic assumptions and combinations of fiscal instruments leads to a range of possible budget outcomes in the next five years. For example, as shown in Appendix B, if nonfederal demand became strong -- comparable to the rapid growth of the early 1960s -- the budget could be balanced by fiscal year 1982 and still attain the economic growth assumed above.

MULTIYEAR TARGETS

At present, budget resolutions are adopted by the Congress for one year at a time. Since a large part of any given year's budget is determined

by decisions made in prior years, the Congress is faced each year with a budget largely composed of spending and receipts that have not been subject to review within an integrated framework. As suggested in a recent CBO report on advance budgeting, ^{2/} one way of dealing with this problem is to have budget targets set by the Congress in advance. Five-year budget projections shed light on how the Congress might proceed with formulating multiyear targets. Projections such as those found in this report provide a baseline on which to build plans for future spending and receipts. In addition, they provide a rough estimate of how much room is available for net increases in spending or tax reductions.

Several key questions are involved in the setting of multiyear targets. What are the goals for the economy and for the deficit? How much should be allocated for tax cuts or spending increases? What is the appropriate level for federal spending and receipts in relation to the economy?

Many possible goals exist for the economy and the deficit. The projections in this report suggest that an unemployment rate of 4.5 percent and a deficit of \$19 billion could be achieved by 1983, assuming an accommodative monetary policy and slightly above average performance by the nonfederal sectors of the economy. If the Congress were to adopt the 4.5 percent unemployment target, but to set a more ambitious goal of a balanced budget by fiscal year 1983, performance by the nonfederal sectors would have to be stronger than assumed here.

In addition to setting goals for the economy and the deficit, the Congress might want to set goals for the level of spending or for the level of receipts in relation to the economy. For example, the Congress might set as a goal a level of federal spending as a percent of GNP. At present, spending is 21.2 percent of potential GNP (defined as the value of GNP if the economy were at a 4.5 percent unemployment rate). Current policy projections of outlays in this report show the federal government's share of potential GNP falling to 18.8 percent by fiscal year 1983. If the Congress were to set as a goal the maintenance of the current federal share of potential GNP, a sizable part of the fiscal drag offset alluded to earlier would be used for spending increases. As an alternative to maintaining the current federal share of potential GNP, the federal income tax system might be indexed, so that effective rates would not rise because of inflation. This would cut taxes below current policy from year to year, since the progressive income tax system implicit in current policy has a more than proportional response to inflation. As a result, indexing would commit a

^{2/} Advance Budgeting: A Report to the Congress, CBO Report, February 1977.

portion of the fiscal drag offset for these automatic tax cuts. The remainder would be available either for further tax cuts or for spending increases.

An important element in decisions about multiyear targets is program needs and costs. These range from welfare reform to national health insurance to the integration of corporate and individual income taxes. The needs and costs for new programs will be discussed in the context of multiyear budget targets in the forthcoming CBO annual report, Budget Options for Fiscal Year 1979.

CHAPTER II. PROJECTIONS OF CURRENT POLICY SPENDING

In addition to considering the size of the federal budget over the next five years, the Congress will also address the question of the appropriate long-run composition of the budget to reflect national needs and priorities. Before the Congress begins to consider these problems, it is important to review the composition of the federal budget under the assumption of a continuation of current policies. This chapter presents details on the current policy projections of federal spending.^{1/} The chapter opens with a presentation of the specific assumptions and methodologies used for the projections, followed by a discussion of the major components of the projected increases in current policy spending. The next section on advanced budgeting shows what fraction of future spending is basically predetermined under alternative assumptions about advanced budgeting. The chapter ends by comparing the projected composition of federal spending under current policy assumptions and the composition of the budget in the past.

SPENDING PROJECTION ASSUMPTIONS

Projections of spending rely on a specific set of assumptions about the meaning of current policy for federal spending programs. The guiding principle is to maintain current programs in a manner consistent with the Second Concurrent Resolution on the Budget for Fiscal Year 1978. Implementation of this principle results in several different methodologies being used in preparing projections. For example, economic stimulus programs are projected by different methods than are ongoing energy or defense programs. In addition, federal spending for the past two fiscal years has fallen well below the levels in the concurrent resolutions on the budget. For this reason, the components of the spending shortfall for fiscal year 1977 have been enumerated and its effects on the projections, if any, identified.

^{1/} The discussion in this chapter is confined to the unified budget. It should be noted, however, that certain activities of the federal government are not reflected in the unified budget. Outlays for so-called off-budget agencies were over \$8 billion in fiscal year 1977.

Methodological Assumptions

The following are the major methodological assumptions underlying the spending projections 2/:

- o The costs of a few federal programs (notably general revenue sharing) are specified by existing law. There are also statutory ceilings on outlays for some programs, such as social services grants. For these programs, the projections are based on current laws.
- o Some federal programs -- such as social security, medicare, unemployment insurance, and interest on the public debt -- are open ended; that is, their costs are determined primarily by population changes or economic factors and are not reviewed annually by the Congress through the appropriations process. Other federal programs -- such as medicaid, public assistance, and veterans' pensions -- are also open ended in the same sense, even though funds are appropriated annually. Projections for these programs are based on specific economic assumptions (shown in the first chapter) and anticipated population changes.
- o Although the statutory authority for many federal programs will expire during the five-year projections period, authorizations are assumed to be renewed routinely, except for programs that are clearly of a one-time nature, such as temporary study commissions. In general, for federal programs with authorizations that expire during the projection period, the projections extrapolate into fiscal years 1979 through 1983 the same level of resources assumed for the second concurrent resolution. In most cases, the provision of the same level of real resources was interpreted to mean the same level of real budget authority. Outlays for these discretionary programs were estimated by applying spendout rates to the budget authority levels. 3/ With

2/ A detailed discussion of projections methodology, on a program-by-program basis, can be found in Five-Year Budget Projections: Fiscal Years 1978-1982, Technical Background, CBO Staff Working Paper, December 1976. Any methodological changes since the publication of that report will be treated in the forthcoming Five-Year Budget Projections: Fiscal Years 1979-1983, Technical Background, CBO Staff Working Paper, December 1977.

3/ For programs that do not receive new budget authority every year, the "same level of resources" was interpreted to be the same level of obligations. Outlays were estimated by applying spendout rates to the obligation levels.

few exceptions, the projections do not include funding for specific needs or projects, such as the cruise missile. Rather, they hold constant the resources, such as procurement funds, that are devoted to general needs, like national security. No attempt was made in this analysis to determine what specific projects could be funded under these assumptions. ^{4/}

- o The major exceptions to the above rule are programs that are assumed to be of a temporary nature and are projected to be phased out over the projections period. For example, the temporary employment assistance program, which provides funds for public service jobs at state and local government levels, is assumed to phase down as the unemployment rate falls.
- o The projections assume no change in military or civilian federal employment. Federal pay scales are assumed to be adjusted annually in accordance with the Federal Pay Comparability Act of 1970. The costs for such pay increases each year are initially estimated under the category "allowances for payraises" and then are distributed among federal programs the following year, as is customary in federal budget presentation.
- o Existing laws provide for various automatic cost-of-living adjustments of some sort for virtually all federal programs providing direct benefit payments to individuals. (Veterans' benefits are a major exception.) The benefit levels for some programs, such as public assistance and unemployment insurance, are set by state and local governments under federal guidelines. It is assumed that the benefits under these programs will also keep pace with inflation. Outlays for certain other programs, such as medicare and medicaid, are indirectly indexed for inflation since the federal government pays part of the costs. Together, benefit payment programs that respond automatically to inflation comprise nearly one-half of the federal budget.
- o As discussed above, for most federal programs with authorizations due to expire during the projections period, the projections contain a constant real funding level. For these programs,

^{4/} CBO is in the process of estimating alternative defense force structures that fit within current policy constraints, using the Defense Resource Model. A discussion of the model can be found in Real Growth and Decline in Defense Operating Costs: Fiscal Year 1978, CBO Staff Working Paper, July 1977.

however, the funding level is discretionary; that is, outlays depend on the amount the Congress chooses to authorize and appropriate. There is no statutory requirement that appropriations for such programs receive inflation adjustments. Since much of the budget responds automatically to inflation, however, it seems useful to show the costs of inflation adjustments for these programs as well in order to have a relatively consistent baseline against which to measure changes in both discretionary and nondiscretionary programs. Thus, for programs in which funding levels are discretionary, two projections are made. The first holds funding constant in current dollar terms, while the second holds it constant in real terms.

Economic Stimulus Programs

In the spring of 1977, the Congress enacted a number of economic stimulus programs for fiscal years 1977 and 1978. In making budget projections, estimates were made for three types of programs: one-time programs, countercyclical programs, and permanent programs.

No new budget authority was projected in fiscal year 1979 for one-time programs. Any fiscal year 1979 outlays for these programs represent the spendout of fiscal year 1977 budget authority. An example of a one-time program is the local public works program, for which \$6.0 billion was appropriated for fiscal year 1977.

Countercyclical programs are for the most part those stimulus programs that are assumed to decline as the unemployment rate falls. New budget authority and outlays have been projected for these programs. Since the national unemployment rate is projected to decrease, the current policy budget authority and outlays for temporary programs, such as countercyclical revenue sharing and temporary employment assistance, decrease.

Permanent stimulus programs were projected to remain at their 1978 levels in real terms in fiscal years 1979-1983. These are programs that were interpreted as being designed to fight structural unemployment.

The following list of the individual programs includes a description of how the programs were handled in the current policy projections:

- o Local Public Works -- one-time. No new budget authority is projected for fiscal year 1978. The outlays in 1979 through 1981 represent outlays from 1977 budget authority.

- o Antirecession Fiscal Assistance -- countercyclical. The program decreases in fiscal years 1979 and 1980 as the unemployment rate declines. Using formulas in the authorization for this program, outlays drop to zero by 1981.
- o Temporary Employment Assistance (TEA) -- countercyclical. As the assumed unemployment rate falls, projected outlays for TEA, Title VI of the Comprehensive Employment and Training Act (CETA), are phased down from \$4.4 billion in fiscal year 1978 to \$40 million in 1983. Title VI was enacted in December of 1974 as a response to dramatic increases in the national unemployment rate. It has been extended as the unemployment rate remained at high levels, and funds have been targeted for the chronically unemployed and low-income individuals. If Title VI were extended in the future primarily as a structural unemployment program, and funding were to remain at fiscal year 1978 levels adjusted for increases in the minimum wage, outlays would be \$800 million higher in fiscal year 1979 than projected in this report, and would rise to \$5.7 billion in 1983. Title VI, or some similar program, is an obvious candidate for additional fiscal stimulus to achieve the assumed economic growth, as discussed in Chapter I.
- o Employment and Training Assistance (ETA), other CETA titles -- permanent. The remaining CETA titles were interpreted as permanent programs to combat structural unemployment. For these titles, budget authority was held constant in real terms at levels consistent with the second concurrent resolution. Outlays were estimated by spending out new and prior budget authority.
- o Older Americans Community Service Employment -- permanent. The funds for this program were interpreted to be for structural unemployment problems. Consequently, they were carried into fiscal years 1979-1983.

The Shortfall in Spending for Fiscal Year 1977

Total spending for fiscal year 1977 was \$401.9 billion. This total was well below the level of \$417.45 billion contained in the Third Concurrent Resolution on the Budget for Fiscal Year 1977, passed in February of this year, and the \$409.2 billion level contained in the amendment of the third concurrent resolution, adopted in May. A spending shortfall of this magnitude calls into question estimates of projected outlays.

Table 3 shows the components of the changes that account for the differences between the 1977 third concurrent resolution, that resolution as amended, and actual spending. Over \$3 billion of the \$15 billion difference between the third resolution and actual spending was because of the withdrawal of the \$50 rebate proposal. The remaining \$12 billion in changes was composed of the following (in billions of dollars):

Financial Transactions	-1.0
Farm Price Supports	1.8
Economic Stimulus Programs	-2.0
Payments for Individuals	-2.3
Construction Programs	-2.0
Department of Defense, Military	-2.3
Other Changes	-4.5

TABLE 3. CHANGE IN FISCAL YEAR 1977 OUTLAYS FROM THIRD CONCURRENT RESOLUTION THROUGH ACTUAL SPENDING: IN BILLIONS OF DOLLARS

Major Programs	Third Resolution/ Resolution As Amended	Resolution as Amended/ Actual Spending	Total Change
Withdrawal of \$50 Rebate	-3.2	--	-3.2
Financial Transactions:			
Farmers Home Administration	--	1.4	1.4
Net interest	--	0.5	0.5
Military sales trust fund	-0.7	-- a/	-0.7
GNMA special assistance functions fund	-0.5	-0.2	-0.7
Export-Import Bank	-0.3	-0.3	-0.6
Federal Home Loan Bank Board	-0.4	-0.1	-0.5
Federal Housing Administration	--	-0.3	-0.3
OCS rents and royalties and other	0.5	-0.6	-0.1
Subtotal	-1.4	0.4	-1.0
Farm Price Supports (CCC)	1.5	0.3	1.8

a/ Less than \$50 million.

(Continued)

TABLE 3. (Continued)

Major Programs	Third Resolution/ Resolution As Amended	Resolution as Amended/ Actual Spending	Total Change
Economic Stimulus and Related Programs			
Employment and training program	-1.2	0.1	-1.1
Antirecession financial assistance	--	-0.5	-0.5
Local public works	-0.1	-0.3	-0.4
Subtotal	-1.3	-0.7	-2.0
Payments for Individuals			
Social security	0.6	-0.3	0.3
Unemployment compensation	-1.4	-- a/	-1.5
Medicare and medicaid	-0.3	-0.4	-0.7
Public assistance and related	-0.3	0.1	-0.2
Veterans' compensation, pensions, and benefits	--	-0.3	-0.3
Other	0.1	0.1	0.2
Subtotal	-1.3	-1.0	-2.3
Department of Defense, Military	-0.5	-1.9	-2.3
Construction Programs			
EPA construction grants	--	-0.7	-0.7
Major water and power projects	-0.4	-0.3	-0.6
Community development grants and urban renewal	-0.2	-0.3	-0.5
Other	-0.1	-0.1	-0.1
Subtotal	-0.7	-1.4	-2.0
All Other Outlay Changes			
Military assistance and foreign aid	-- a/	-1.0	-1.0
HEW Education Division	-0.3	-0.5	-0.8
Agriculture -- general operations and receipts	--	-0.7	-0.7
Federal Energy Administration	-0.1	-0.4	-0.5
ERDA	-0.5	0.2	-0.4
Disaster relief	--	-0.2	-0.2
Social services grants	-0.2	-- a/	-0.2
Other	-0.2	-0.6	-0.7
Subtotal	-1.4	-3.1	-4.5
TOTAL	-8.3	-7.3	-15.6

a/ Less than \$50 million.

The change in the category of financial transactions is composed of a number of increases and decreases. One of the significant decreases was in the foreign military sales trust fund. For estimating trust fund gross outlays and receipts, CBO has recently devised a new methodology, which is reflected in the most recent estimates for fiscal year 1978 and in the projections for fiscal years 1979-1983. ^{5/} Most of the other changes reflect the difficulty in estimating outlays for agencies involved in the financing and credit activities of the federal government. Estimates for this category will probably continue to be a problem in the future.

The change in farm price supports reflects the problem of large crops and falling market prices, as well as the higher dairy support rate effected by the Administration on April 1, 1977. Most of this change was anticipated in the amendment to the third concurrent resolution.

Changes in the economic stimulus programs are the result of several factors. First, the appropriation for the programs was approved later than anticipated in the third concurrent resolution. Also, original estimates for these programs were overly optimistic about the time necessary for actual implementation. Finally, part of the change in antirecessional fiscal assistance stems from the lower than anticipated unemployment rate in the first quarter of 1977. CBO's scorekeeping estimates for fiscal year 1978 and projections for 1979-1983 have been adjusted somewhat to reflect these factors. For all of the economic stimulus programs, CBO estimates for 1978 are less than or equal to those of the Administration.

Changes in the unemployment compensation category, explained by the unexpectedly rapid rate of economic growth and the decline in the unemployment rate in the first half of 1977, account for the difference in payments for individuals. If the economy performs better in 1978-1983 than has been assumed in Chapter I, projected outlays for unemployment benefits would be too high. If the economy does not grow at the assumed rate of 4.8 percent per year, however, actual outlays would exceed the estimates.

The changes in construction programs, Department of Defense, Military, and other spending programs reflect the pervasiveness of shortfall phenomena throughout the budget. In July 1977 CBO reestimated outlays for fiscal year 1977 at \$402.6 billion. Since July, CBO has reestimated total

^{5/} For details on the projections methodology for the foreign military sales trust fund, see the forthcoming Five-Year Budget Projections: Fiscal Years 1979-1983, Technical Background, CBO Staff Working Paper, December 1977.

outlays for 1978 downward by over \$2 billion. Outlays for 1978 are reestimated downward by another \$3.5 billion in the CBO Scorekeeping Report Number 5 for 1978, released the same week as this projections report. These reestimates reflect widespread adjustment of the spendout rates used to estimate outlays for most accounts, and were used for the estimates in this report.

Based on analysis of past trends, spending for 1978 may fall below current scorekeeping estimates. 6/ Outlays for fiscal year 1978 will again be reestimated shortly after the submission of the President's budget. New spending projections will be made in the early spring of 1978 and will reflect the fiscal year 1978 reestimates.

PROJECTED INCREASES IN FEDERAL SPENDING

Current policy outlays are projected to increase to \$655 billion by fiscal year 1983. The average rate of increase is approximately 7.3 percent annually. Table 4 shows the components of the increases in federal spending from CBO's current estimate for fiscal year 1978, given current policy assumptions. The largest component of the increase is social security payments, which by fiscal year 1983 would total \$156 billion, \$60 billion above the current estimate for fiscal year 1978. The next largest increase is for medicare and medicaid benefits (\$33 billion by fiscal year 1983). These increases would be tempered, however, by cost-control legislation anticipated in the second concurrent resolution. As shown in the table, this legislation is projected to save \$10 billion by fiscal year 1983.

For many federal programs the funding levels are discretionary. The Congress may choose not to index these programs to inflation, in contrast to others like social security for which indexing is specified by law. The cost of inflation increases for discretionary programs is demonstrated in Figure 3. Of the discretionary inflation increases, over 40 percent is for defense while the remainder is for grants to state and local governments, veterans' benefits increases, and other federal operations.

6/ Since the 1950s, year-to-year increases in federal outlays have averaged about 8 percent. The increase implicit in the current CBO scorekeeping estimate is almost 13 percent. Although it is likely that the increase for 1978 may be above the average, with some of the economic stimulus programs beginning to spend out, there is some chance that the percent increase in outlays will be only about 11 percent, which would mean a shortfall of \$6 to \$8 billion from the current estimate.

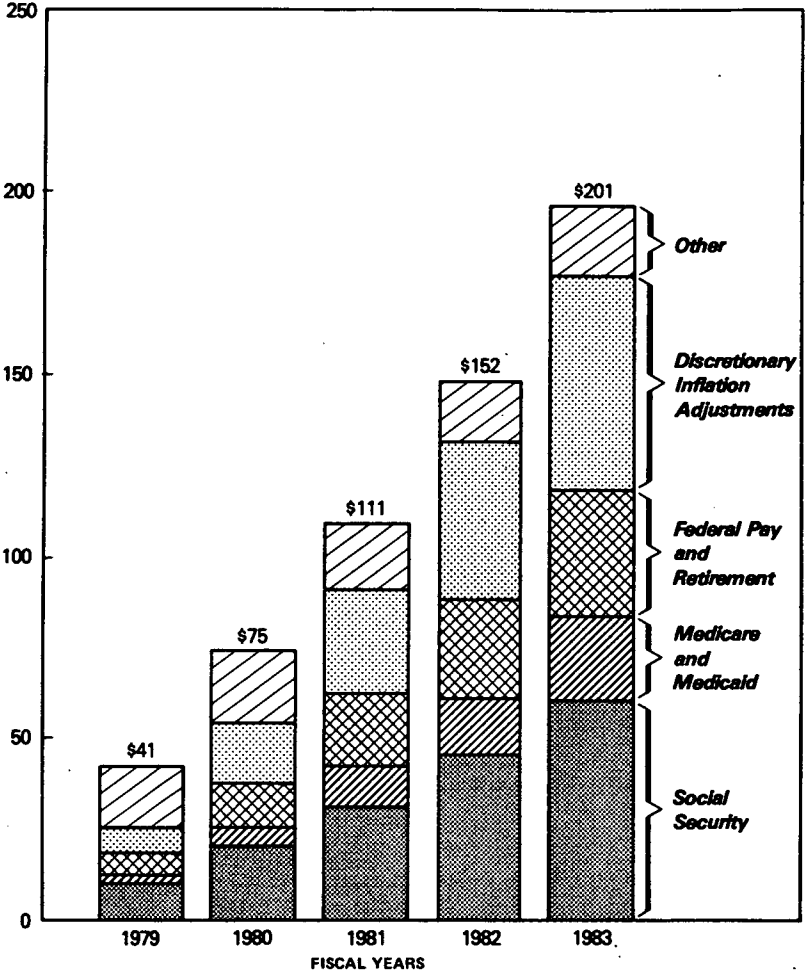
TABLE 4. PROJECTED INCREASES IN FEDERAL OUTLAYS: BY FISCAL YEARS, IN BILLIONS OF DOLLARS

	1979	1980	1981	1982	1983
CBO Current Estimate for 1978	454	454	454	454	454
Add: Increases Mandated under Existing Law					
Social security	10	20	31	44	60
Medicare and medicaid	5	10	18	25	33
Pay increases for federal employees	4	9	13	18	23
Retired military and civil service retirement	2	4	7	9	12
Net interest	3	6	8	9	9
Defense purchases	2	4	6	7	8
All other spending (net)	9	7	1	--	--
Subtotal	489	514	538	566	600
Add: Further Adjustments for Inflation					
Maintain 1978 level of defense purchases	2	6	11	17	23
Maintain 1978 level of grants and other federal purchases	3	9	16	27	36
Cost-of-living increase for Veterans' benefits	1	2	2	3	4
Subtotal	495	531	567	613	663
Add: Legislation Anticipated in Second Concurrent Resolution					
Medicare and medicaid cost control	-3	-4	-6	-9	-10
Other legislation	2	2	2	2	2
TOTAL	495	529	565	606	655

Figure 3.

COMPONENTS OF INCREASES IN CURRENT POLICY OUTLAYS

\$ BILLIONS



MULTIYEAR BUDGETING AND PROJECTIONS OF FEDERAL SPENDING

A considerable amount of federal spending over the next five years is mandated by current law. In the absence of changes in these laws, the outlays fall outside the control of the annual budget process. For example, benefit payments for social security are determined by formulas in the authorizing legislation for the program. Table 5 shows committed outlays for permanent appropriations, trust funds, offsetting receipts, and entitlements; these comprise approximately 50 percent of current and projected outlays. A second source of commitments is outlays resulting from appropriations made in fiscal 1978 and prior years. Unless the Congress were to rescind the budget authority for these previously funded programs, the outlays shown in Table 5 would have to be considered as uncontrollable when reviewing spending in fiscal years 1979-1983. Finally, Table 5 shows the outlays from legislation for fiscal year 1978 that was anticipated in the second concurrent resolution. If this legislation is enacted as assumed, the outlays shown will be determined before the start of fiscal year 1979. Outlays mandated under current law become the base for consideration of new spending commitments in fiscal years 1979-1983.

If the Congress does not change commitments made in 1978 and prior years, the outlays subject to control under current procedures in fiscal years 1979-1983 are those from new commitments. This represents only 28 percent of projected outlays for fiscal year 1979; the percent rises to about 45 percent for fiscal year 1983. In the absence of other changes in the budget reviewing procedures of the Congress, however, the increase in control would not occur unless the Congress adopts an advanced budgeting or advanced targeting approach to federal spending. As shown in Table 5, the portion of the budget that is subject to control in fiscal year 1979 is only about \$140 billion because of commitments made in fiscal year 1978 and prior years. If the Congress waits until next year to review the fiscal year 1980 budget and continues to use a one-year planning horizon, the outlays from 1979 commitments will be, for all practical purposes, beyond the control of the budget process, and only about \$150 billion will be subject to control.

Table 6 shows the percent of budget outlays that fall under the control of the budget process under alternative assumptions about advanced targeting. As shown in the table, if the Congress continues to set spending targets for one year at a time, a constant 28 percent of outlays falls under the control of the budget process. On the other hand, if the Congress were to set five-year targets starting with fiscal year 1979, an increasing share of projected outlays would fall under the control of the budget process. The table also demonstrates that a large part of the increased control resulting from advanced targeting can be derived by using a two-year planning horizon.

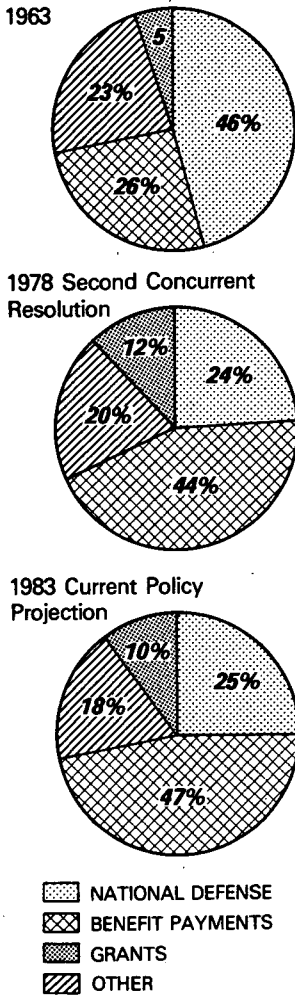
TABLE 5. CURRENT POLICY PROJECTIONS BY YEAR OF COMMITMENT:
BY FISCAL YEARS, IN BILLIONS OF DOLLARS

	1979	1980	1981	1982	1983
Amounts Committed in 1978 and Prior Years					
Permanent appropriations, trust funds, offsetting receipts, and entitlements	252	270	293	318	347
Outlays from 1978 and prior year authority	103	51	32	26	26
Net outlays from anticipated legislation assumed in the second concurrent resolution	-1	-2	-5	-8	-9
Subtotal	354	319	320	336	364
Amounts Assuming Current Policy for New Commitments in 1979	140	61	23	9	6
Amounts Assuming Current Policy for New Commitments in 1980-1983	--	149	221	261	285
TOTAL	495	529	564	606	655

TABLE 6. PERCENT OF OUTLAYS CONTROLLABLE THROUGH THE
BUDGET PROCESS, UNDER ALTERNATIVE ASSUMPTIONS
ABOUT MULTIYEAR TARGETING: BY FISCAL YEARS

	1979	1980	1981	1982	1983
One-year Planning Horizon	28	28	28	28	28
Five-year Planning Horizon (starting in 1979)	28	40	43	45	45
Two-year Planning Horizon (starting in 1979)	28	40	40	40	40

Figure 4.
RELATIVE SHARES
OF TOTAL
FEDERAL OUTLAYS



THE COMPOSITION OF FEDERAL SPENDING

In fiscal year 1963, outlays for national defense comprised 46 percent of federal spending, while benefit payments for individuals represented 26 percent of the total. Grants to state and local governments for other than benefit payments were only 4.5 percent of total federal outlays.

Major Spending Components

During the past 15 years, the composition of the budget has changed considerably. Of the \$458 billion ceiling in the 1978 second concurrent resolution, only 24 percent is assumed to be for national defense, while 44 percent is for benefit payments. The dramatic rise in the share for benefit payments seen in Figure 4 results primarily from increases for contributory benefit payment programs like social security. The share of the budget appropriated for grants to state and local governments has more than doubled since 1963 as new grant programs such as Environmental Protection Agency construction grants, general revenue sharing, and antirecession grant programs have been enacted.

Under current policy assumptions, the composition of federal spending would change slightly by fiscal year 1983. The increase in national defense generally corresponds with inflation increases. The share of the budget for benefit payments for individuals would increase to 47 percent because, in the absence of policy changes, these programs would be influenced both by inflation and by changes

in the size and characteristics of the population receiving benefit payments. The share for grants would decline to about 10 percent, primarily because of the phaseout of antirecession programs as the unemployment rate declines. Because the rate of change of interest on the public debt is related to the deficit (projected to decline through 1983), the share for other parts of the budget declines to 18 percent.

In addition to showing the composition of current policy outlays by year, Table 7 also shows current policy outlays as a percent of current dollar or nominal GNP. On a current policy basis, federal outlays would decrease as a percent of GNP from 22.3 percent in fiscal year 1978 to 19.3 percent in fiscal year 1983. The decline would occur because GNP is assumed to increase with both inflation and real economic growth, while current policy outlays increase with inflation only, except for the real growth caused by population changes in benefit payments programs. As discussed in Chapter 1, some combination of spending increases above current policy or tax cuts below current policy would be necessary if the economy were to grow at the rates assumed for these projections.

Major Functional Categories

Another important classification of federal spending is by the major functions. The functional classification is a means of presenting budget authority and outlays in terms of the principal purposes that federal programs are intended to serve, regardless of the methods used to carry out the activities. The Congressional Budget Act of 1974 requires the Congress to include estimates of budget authority and budget outlays for each function in its annual budget resolutions.

The relationship between the six spending categories used above and the functional classification is as follows:

- o The national defense category is the same for both classifications.
- o The bulk of the health, income security, and veterans' benefits functions are carried out through benefit payments to individuals (that is, the sum of contributory and noncontributory benefit payments).
- o Grants to state and local governments (other than grants for payments to individuals) are concentrated largely in functions 300, 400, 450, 500, and 850.

TABLE 7. MAJOR COMPONENTS OF BUDGET OUTLAY PROJECTIONS: BY FISCAL YEARS

Major Component	1977 Estimate	1978 Second Concurrent Resolution	Current Policy Projections				
			1979	1980	1981	1982	1983
In Billions of Dollars							
National Defense	97	110	119	128	139	130	161
Contributory Benefit Payments for Individuals	136	148	161	176	194	213	238
Other Benefit Payments for Individuals	46	49	53	57	60	64	68
Grants to State and Local Governments	47	57	57	58	58	60	63
Net Interest	30	33	37	39	41	42	42
Other Federal Operations	47	62	68	72	73	77	82
TOTAL	402	458	495	529	565	606	655
As a Percent of Total Outlays							
National Defense	24	24	24	24	25	25	25
Contributory Benefit Payments for Individuals	34	32	33	33	34	35	36
Other Benefit Payments for Individuals	11	11	11	11	11	11	10
Grants to State and Local Governments	12	12	12	11	10	10	10
Net Interest	7	7	7	7	7	7	6
Other Federal Operations	12	13	14	14	13	13	13
TOTAL	100	100	100	100	100	100	100
As a Percent of GNP							
TOTAL	21.8	22.3	21.8	21.0	20.3	19.7	19.3

- o Net interest consists of the interest function and the interest received by trust funds, which comprise approximately one-half the undistributed offsetting receipts function.
- o Other federal operations are distributed throughout all functional categories except national defense and interest.

Tables 8 and 9 present the projections of outlays and budget authority by the 17 major functions used for the Congressional budget resolutions in fiscal years 1976 through 1978. The projections for 1979-1983 include discretionary inflation adjustments.

Since the inflation adjustments used for the projections are relatively uniform for most federal programs, the percent breakdown of projected total outlays by functional category changes little between fiscal years 1978 and 1983. Increases for social security in the income security function are offset by projected decreases in unemployment compensation. The projected declining shares for the general revenue sharing and the education, training, employment, and social services functions are caused by the phasing out of certain antirecession programs. The declining share for veterans' benefits and services results from the projected decline in the number of veterans receiving benefits.

TABLE 8. BUDGET AUTHORITY PROJECTIONS BY FUNCTION: BY FISCAL YEARS, IN BILLIONS OF DOLLARS

Function	1978 Second Concurrent Resolution	Current Policy Projections				
		1979	1980	1981	1982	1983
National Defense (050)	116.4	128	138	148	158	169
International Affairs (150)	8.0	9	10	11	11	12
General Science, Space, and Technology (250)	4.9	5	6	6	7	7
Natural Resources, Environment, and Energy (300)	24.6	22	21	20	23	25
Agriculture (350)	2.1	5	7	7	6	7
Commerce and Transportation (400)	20.4	21	24	26	27	28
Community and Regional Development (450)	8.2	10	11	11	12	12
Education, Training, Employment, and Social Services (500)	26.3	26	28	29	30	32
Health (550)	47.7	53	58	68	77	85
Income Security (600)	178.6	193	210	225	242	261
Veterans' Benefits and Services (700)	19.9	21	22	23	24	26
Law Enforcement and Justice (750)	3.8	4	4	5	5	5
General Government (800)	3.8	4	4	4	5	5
Revenue Sharing and General Purpose Fiscal Assistance (850)	9.6	9	9	9	9	10
Interest (900)	41.7	47	50	53	55	56
Allowances (920)	0.9	1	1	1	1	1
Undistributed Offsetting Receipts (950)	-16.8	-18	-19	-21	-23	-24
TOTAL	500.1	541	582	624	669	717

TABLE 9. OUTLAY PROJECTIONS BY FUNCTION: BY FISCAL YEARS, IN BILLIONS OF DOLLARS

Function	1978 Second Concurrent Resolution	Current Policy Projections				
		1979	1980	1981	1982	1983
National Defense (050)	110.1	119	128	139	150	161
International Affairs (150)	6.6	7	8	8	9	9
General Science, Space, and Technology (250)	4.7	5	6	6	6	7
Natural Resources, Environment, and Energy (300)	20.0	22	24	21	23	24
Agriculture (350)	6.3	7	6	7	7	7
Commerce and Transportation (400)	19.6	21	22	23	24	26
Community and Regional Development (450)	10.6	11	10	11	11	11
Education, Training, Employment, and Social Services (500)	26.4	27	28	28	29	30
Health (550)	44.2	48	52	58	63	71
Income Security (600)	146.1	161	175	190	208	230
Veterans' Benefits and Services (700)	20.2	21	22	23	24	25
Law Enforcement and Justice (750)	4.0	4	4	5	5	5
General Government (800)	3.85	4	4	4	5	5
Revenue Sharing and General Purpose Fiscal Assistance (850)	9.7	9	9	9	9	10
Interest (900)	41.7	47	50	53	55	56
Allowances (920)	1.0	1	1	1	1	2
Undistributed Offsetting Receipts (950)	-16.8	-18	-19	-21	-23	-24
TOTAL	458.25	495	529	565	606	655

CHAPTER III. PROJECTIONS OF CURRENT POLICY REVENUES

Equally as important as the composition of federal spending is the composition of federal revenues over the next five years. What share of federal revenues should be raised by individual income taxes as opposed to corporate income taxes? How would the composition of revenues over the next five years be affected by legislation to increase social insurance taxes and make the social security trust fund solvent? As a prelude to Congressional consideration of the long-run makeup of federal taxes, this chapter discusses projections of federal revenues assuming the continuation of existing laws. The chapter opens with a discussion of the assumptions underlying the revenue projections and then moves on to the current policy projections of federal revenues. The basic result shown by the projections is that under current law the share of revenues raised by individual income taxes would increase, because of the progressive nature of federal individual income tax, from 44 percent in fiscal year 1978 to 52 percent in 1983.

REVENUE PROJECTION ASSUMPTIONS

Current policy revenue projections assume a current dollar gross national product (GNP) that grows at an average rate of 10.5 percent annually under the economic assumptions in Chapter I. It is also assumed that wages and salaries grow at an average annual rate of 10.5 percent, corporate profits at an average annual rate of 10.6 percent, and taxable personal income at an average annual rate of 10.7 percent. These assumptions reflect a gradual approach to 4.5 percent unemployment by 1983, with real economic growth of 4.8 percent annually through 1982 and 3.7 percent for 1983, as discussed in Chapter I.

The current policy assumptions under which the revenue estimates are made include extension of those provisions of the Tax Reform and Simplification Act of 1977 that would expire if not renewed. The only exception to this assumption is the jobs credit, which is assumed to expire without extension in 1978. The earned income credit is treated as a revenue reduction, and is assumed to be extended through fiscal year 1983. Social security tax revenues are forecast assuming steady increases in the wage base from \$15,300 in 1977 to \$25,800 by 1983. Social security tax rates are assumed to rise from 5.85 percent in 1977 (employees share only) to 6.3 percent for 1981 and subsequent years as specified in current law.^{1/} In addition, the projections assume the scheduled 1978 increase in the wage base for unemployment insurance payroll taxes.

^{1/} The social security wage base and tax rates apply to calendar years, although the revenue estimates are presented by fiscal year.

Both the House and the Senate have passed energy tax bills that would affect revenues significantly during the projection period. One of their common features is the extension throughout the projection period of the excise tax on gasoline. This extension is assumed in the revenue projections. In most other respects, the bills have major unresolved differences. The House bill combines energy tax credits and excise taxes that have not been included in the five-year revenue projections. The Senate bill contains a substantial number of refundable energy tax credits that have also not been included in the five-year revenue projections. The conference probably will produce a bill that compromises the differences between the two bills. Table 10 shows the separate five-year revenue impacts of the House and Senate bills on the revenue projections contained in this chapter.

TABLE 10. EFFECTS OF HOUSE-PASSED AND SENATE-PASSED ENERGY BILLS ON FIVE-YEAR PROJECTIONS: BY FISCAL YEARS, IN BILLIONS OF DOLLARS

	1978	1979	1980	1981	1982	1983
House Version	-1	--	9	12	4	1
Senate Version	-2 <u>a/</u>	-5	-6	-7	-7	-7

a/ Individual provisions of the Senate bill add to -\$2.014 billion for fiscal year 1978, but the bill contains a provision that the total revenue loss should not exceed \$972 billion for fiscal year 1978.

Congressional action on social security tax revision is not yet complete, but the general outlines of the likely changes have begun to crystalize. The House and Senate have separate measures to deal with the problem of the solvency of the trust fund; the differences have not yet been resolved in conference. Although each house has separate measures, the revenue impact will probably fall within a range bounded by the two alternatives. If the conference reaches agreement on some proposal between the two alternatives, the effect from social security changes would be an increase in revenues for the social insurance category in the range shown in Table 11.

TABLE 11. EFFECTS OF SOCIAL SECURITY LEGISLATION ON TOTAL REVENUES: BY FISCAL YEARS, IN BILLIONS OF DOLLARS

1979	1980	1981	1982	1983
6-8	8-10	17	21-23	23-26

REVENUE PROJECTIONS

The total federal receipts projections by source are shown in Table 12. Total federal revenues under current law are projected to rise at an average annual rate of 13.2 percent, from \$356.9 billion in fiscal year 1977 to \$751 billion in fiscal year 1983. The projected revenue increase of \$394.1 billion from 1977-1983 is primarily attributable to individual income taxes (59 percent), corporate income taxes (13 percent), and social insurance taxes (24 percent). Together, individual income and social insurance taxes are expected to provide 79 percent of fiscal year 1983 receipts. Of the projected \$394.1 billion in revenue growth from 1977 to 1983, more than half reflects increases caused by inflation.

Under current law, all three major tax sources are projected to yield revenues that rise more rapidly than the growth rate for GNP. Individual income taxes grow most rapidly. After adjusting for changes in the standard deduction and personal credits, the estimates of individual income tax liabilities have an elasticity of 1.4; that is, each percent growth in GNP is associated with 1.4 percent growth in individual income tax liabilities. Under current law, both corporate income and social insurance taxes grow slightly faster than corporate profits and GNP, respectively.

FEDERAL REVENUES: A HISTORICAL PERSPECTIVE

Federal revenues have grown more than fourfold since 1958 -- from \$79 billion in fiscal year 1958 to nearly \$360 billion for fiscal year 1977. Relative to the size of the economy, federal taxes have increased very little -- from 17.7 percent of GNP in 1958 to 18.8 percent of GNP in 1977. While there has been some fluctuation in receipts, stability of taxes as a

TABLE 12. PROJECTIONS OF CURRENT POLICY RECEIPTS BY SOURCE: BY FISCAL YEARS, IN BILLIONS OF DOLLARS

Source	1977 Estimate	1978 Second Concurrent Resolution	Current Policy Projections				
			1979	1980	1981	1982	1983
Individual Income Taxes	156.7	175.0	213	250	290	338	389
Corporation Income Taxes	54.9	59.0	67	76	86	95	106
Social Insurance Taxes and Contributions	108.6	124.4	137	150	166	186	203
Excise Taxes	17.5	20.3	20	21	22	24	25
Estate and Gift Taxes	7.3	5.6	6	7	8	8	8
Customs Duties	5.2	5.4	6	7	8	9	10
Miscellaneous Receipts	6.5	7.3	8	8	8	8	8
TOTAL	356.9	397.0 a/	457	519	590	668	751

a/ The Second Concurrent Resolution on the Budget for Fiscal Year 1978 assumed energy legislation would add \$1.1 billion in receipts in fiscal year 1978.

percent of GNP is the most apparent feature over the last two decades. This result has not been automatic, but rather has been achieved only through legislative action to reduce taxes from time to time. These reductions have offset the tendency of the progressive tax system to take an increasing share of income, as inflation and real economic growth produce higher incomes. The variations in taxes as a share of GNP since 1958 are shown in Table 13 and Figure 5. Under current policy assumptions total receipts would grow to \$750.6 billion -- or 21.7 percent of GNP -- by fiscal year 1983. This is well above the average over the past twenty years. Thus, long-run stability of federal taxes as a percent of GNP over the projection period will be maintained only if the Congress acts to reduce taxes. In addition, as pointed out in Chapter I, tax cuts or spending increases or both are needed if the budget projections are to be consistent with the economic assumptions.

Table 13 also shows the share of revenues provided by each source. With the help of several tax policy changes, the share of revenues provided by individual income taxes has remained nearly constant since 1958. The share of total revenues provided by corporate income taxes has fallen over the last two decades. Since 1958 corporate profits have declined as a share

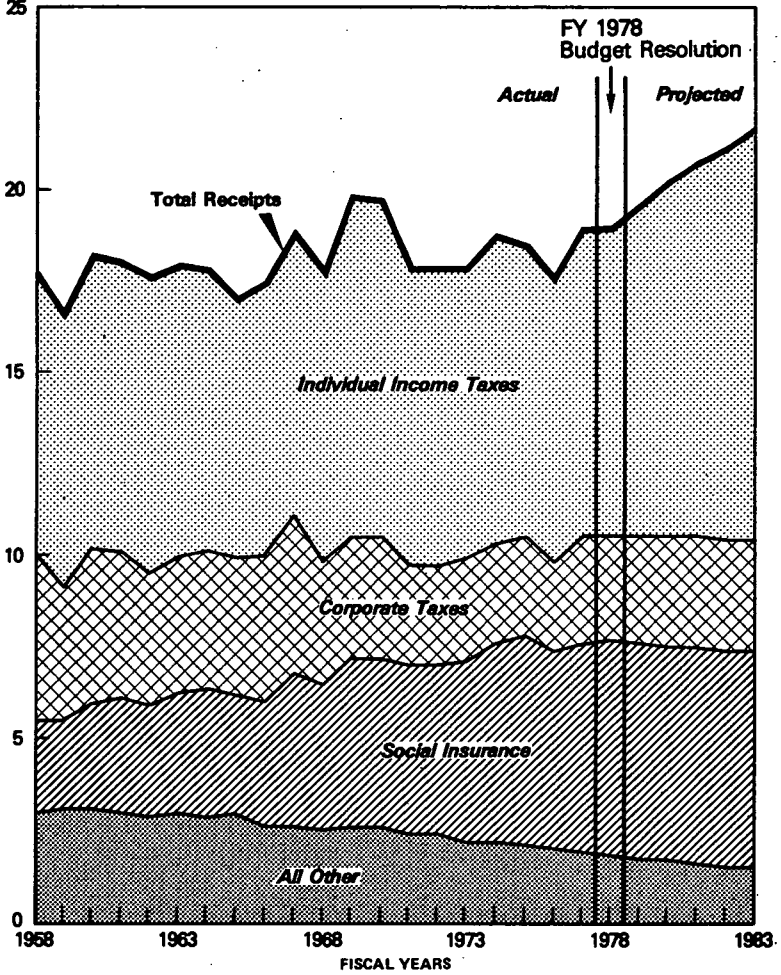
of GNP, and business tax credits and deductions have expanded. Social insurance taxes have contributed an increasing share of total revenues and will exceed 30 percent by 1978.

TABLE 13. COMPOSITION OF FEDERAL RECEIPTS: BY FISCAL YEARS

Source	1958	1963	1968	1973	1978	1983
	As a Percent of GNP					
Individual Income Taxes	7.7	8.0	7.9	7.9	8.3	11.2
Corporate Income Tax	4.5	3.6	3.3	2.8	2.8	3.0
Social Insurance Taxes and Contributions	2.5	3.3	4.0	4.9	5.9	5.9
Other Taxes and Receipts	3.0	3.0	2.5	2.2	1.8	1.5
TOTAL	17.7	17.9	17.7	17.8	18.8	21.7
	As a Percent of Total Budget Receipts					
Individual Income Taxes	43.6	44.6	44.7	44.5	44.1	51.9
Corporate Income Tax	25.2	20.2	18.6	15.6	14.9	14.1
Social Insurance Taxes and Contributions	14.1	18.5	20.7	28.0	31.3	27.0
Other Taxes and Receipts	17.0	16.5	14.0	12.2	9.7	7.0
TOTAL	100.0	100.0	100.0	100.0	100.0	100.0

If tax policies are not changed, the individual income tax will continue to take a larger share of personal income as inflation and real growth propel taxpayers into higher tax brackets. In the absence of policy changes, corporate taxes will remain at about the same share of GNP as in 1977. Without changes in present policy, social insurance taxes will rise to a slightly larger share of GNP. It should be noted that all three major tax categories are likely objects of significant revision within the five-year forecast period. While it is not possible to predict the form of specific

Figure 5.
FEDERAL REVENUES AS A PERCENT OF GNP
 PERCENT OF GNP



proposals, there are actuarial deficits in the social insurance trust funds. If these deficits are to be reduced through increased social insurance taxes, it is likely that social insurance taxes will become a larger share of total revenues. Revisions in corporate and individual income taxes are also likely, probably resulting in net tax reductions, especially if tax cuts are used to generate the economic stimulus needed for the economy to grow at a 4.8 percent annual rate.

APPENDIXES.

APPENDIX A. THE EFFECTS OF LESS VIGOROUS ECONOMIC GROWTH

As pointed out in Chapter I, inflation, unemployment, and other levels of economic activity have a major impact on revenues and outlays. This appendix presents the effects of less vigorous economic growth on projections of the budget. The results show that current policy receipts are affected much more by alternative assumptions about real economic growth than are current policy outlays. The results also suggest that it might be possible to balance the budget by fiscal year 1982 if a lower target were assumed for real economic growth.

BUDGET IMPLICATIONS OF LESS VIGOROUS ECONOMIC GROWTH

The target for economic growth in Chapter I was relatively optimistic in light of historical experience. Suppose a less optimistic target of a 4 percent annual rate of growth in real gross national product (GNP) were assumed (see Table A-1). What would be the effect on projected current policy revenues and outlays?

TABLE A-1. AGGREGATE ECONOMIC ASSUMPTIONS UNDER LESS VIGOROUS ECONOMIC GROWTH: BY CALENDAR YEARS

Selected Economic Variables	1977	1978	1979	1980	1981	1982	1983
Gross National Product (GNP)							
Current dollar GNP (in billions of dollars)	1,898.0	2,107.0	2,321.7	2,547.1	2,787.0	3,047.2	3,329.5
Real GNP (in billions of 1972 dollars)	1,338.0	1,402.7	1,460.9	1,519.3	1,580.1	1,643.3	1,709.0
Growth rate of real GNP	5.0	4.8	4.2	4.0	4.0	4.0	4.0
Unemployment Rate (percent)	7.0	6.5	6.3	6.1	5.9	5.7	5.4
Consumer Price Index (percent change)	6.5	5.6	6.0	5.6	5.3	5.2	5.1

If the economy were to grow at only 4 percent per year from fiscal years 1979 through 1983, current policy receipts would increase by 12 percent annually -- from \$456 billion in fiscal year 1979 to \$722 billion in fiscal year 1983. As a share of GNP, receipts would grow from 20 to 22 percent. As shown in Table A-2, current policy outlays would grow from

\$493 billion in fiscal year 1979 to \$651 billion in fiscal year 1983. As a percent of GNP, outlays would decline from 21 to 20 percent. The projections of current policy receipts and outlays demonstrate that, while the level of current policy receipts is highly sensitive to the rate of real economic growth, the level of current policy outlays changes very little. The sensitivity of receipts exists because of the progressive nature of the individual income tax; the lack of sensitivity of outlays is the result of offsetting changes. Under less vigorous economic growth, the unemployment rate would decline more slowly. Therefore, outlays for programs like unemployment compensation and various income supplements would be higher than they would be under more optimistic economic assumptions. The lower inflation rates assumed in Table A-1, however, indicate that projected cost-of-living increases would be smaller.

TABLE A-2. FIVE-YEAR BUDGET PROJECTIONS, UNDER LESS VIGOROUS ECONOMIC GROWTH: BY FISCAL YEARS, IN BILLIONS OF DOLLARS

	1978 Second Concurrent Resolution	Projections				
		1979	1980	1981	1982	1983
Current Policy Receipts	397.0	456	514	579	648	722
Current Policy Outlays	458.25	493	529	565	605	651
Current Policy Margin	-61.25	-37	-15	14	43	72
Fiscal Drag Offset	-- a/	11	21	41	63	70
Deficit (-) or Surplus	-61.25	-48	-36	-27	-20	2

a/ It is assumed that the spending ceiling and revenue floor in the second concurrent resolution are consistent with the fiscal stimulus needed for the economy to grow at the rate of 4.8 percent in fiscal year 1978. If more or less fiscal stimulus is required, corresponding adjustments would have to be made in the estimates of the fiscal drag offset for fiscal years 1979-1983.

THE PROJECTED DEFICIT UNDER LESS VIGOROUS ECONOMIC GROWTH

Under current policy assumptions, the receipts the federal government would be taking out of the economy would rise faster than the outlays it would be putting back into the economy in the form of wages, purchases, and payments to individuals. The fiscal drag exerted by the federal budget would itself tend to reduce economic growth. Consequently, for the economic assumptions to be realized, fiscal and monetary policy would, in all likelihood, have to be used to offset the fiscal drag.

As discussed in Chapter I, if tax cuts or spending increases were used to offset the restrictive effects of current policy budgets, the size of the offset would depend on the strength of nonfederal demand. Under the so-called "moderate" scenario for nonfederal demand used in that chapter, approximately \$74 billion in tax cuts or spending increases would be required by fiscal year 1983 to offset the fiscal drag and keep the economy on the growth path. As seen in Table A-2, the current policy margin is approximately equal to the fiscal drag offset by fiscal year 1983, which implies that, under less vigorous economic growth and the moderate scenario for nonfederal demand, it might be possible to balance the budget by fiscal year 1983.

APPENDIX B. ALTERNATIVE SCENARIOS FOR NONFEDERAL DEMAND

The so-called "moderate" scenario for nonfederal demand assumed in Chapter I and Appendix A represents a plausible set of economic conditions over the next five years. It is by no means, however, the only possible outcome. Expansionary monetary policy or autonomous factors could give rise to a boom in the nonfederal sectors. On the other hand, external shocks such as an oil embargo or other factors might result in weaker growth in nonfederal demand than is assumed for the moderate scenario. This appendix provides rough estimates of the effect of alternative assumptions of nonfederal demand on projections of the deficit.

NONFEDERAL DEMAND: A MORE OPTIMISTIC SCENARIO

As discussed in Chapter I, stronger nonfederal demand would require less budget stimulus in the form of tax cuts or spending increases to achieve the assumed 4.8 percent growth rate. Table B-1 shows the effect of more optimistic assumptions of nonfederal demand on the fiscal drag offset. 1/ By fiscal year 1983, the offset would be only \$64 billion, compared to about \$115 billion under the moderate scenario. Because of the smaller fiscal drag offset, the budget is projected to be in balance by fiscal year 1982, when the current policy margin would be equal to the required offset.

NONFEDERAL DEMAND: A MORE PESSIMISTIC SCENARIO

If nonfederal demand were weaker than in the moderate scenario, larger tax cuts or spending increases would be required to offset fiscal drag. Table B-2 shows the effect of more pessimistic assumptions about nonfederal demand 2/ on the tax cuts and spending increases needed to

- 1/ For this scenario, the personal saving rate is assumed to average 5.8 percent, and the annual growth in real investment to average 8.0 percent. The assumed annual increase in real state and local government purchases is 3.5 percent per year and real net exports are assumed to average \$3 billion annually.
- 2/ Under the weaker nonfederal demand scenario, the personal saving rate is assumed to average 6.3 percent, and the annual growth of real investment to average 5.6 percent. The assumed growth rate of real state and local purchases is 2.25 percent annually. Net exports are assumed to be nearly balanced over the five-year period.

achieve the growth path used in Appendix A. ^{3/} Under this weaker nonfederal demand scenario, the current policy margin would be smaller than the fiscal drag offset throughout the projection period. The deficit would remain between \$60 and \$70 billion between fiscal years 1979 and 1983.

TABLE B-1. FIVE-YEAR BUDGET PROJECTIONS, ASSUMING STRONG NONFEDERAL DEMAND: BY FISCAL YEARS, IN BILLIONS OF DOLLARS

	1978 Second Concurrent Resolution	Projections				
		1979	1980	1981	1982	1983
Current Policy Receipts	397.0	457	519	590	668	751
Current Policy Outlays	458.25	495	529	565	606	655
Current Policy Margin	-61.25	-38	-10	25	62	96
Fiscal Drag Offset	-- a/	17	31	46	62	64
Deficit (-) or Surplus	-61.25	-55	-41	-21	--	32

a/ It is assumed that the spending ceiling and revenue floor in the second concurrent resolution are consistent with the fiscal stimulus needed for the economy to grow at the rate of 4.8 percent in fiscal year 1978. If more or less fiscal stimulus is required, corresponding adjustments would have to be made in the estimates of the fiscal drag offset for fiscal years 1979-1983.

^{3/} If nonfederal demand were as weak as in this scenario, it is unlikely that the economy would grow at the 4.8 percent rate assumed in Chapter I. Consequently, the results are only reported for the 4.0 percent growth path used in Appendix A.

TABLE B-2. FIVE-YEAR BUDGET PROJECTIONS, UNDER LESS VIGOROUS ECONOMIC GROWTH, ASSUMING WEAK NON-FEDERAL DEMAND: BY FISCAL YEARS, IN BILLIONS OF DOLLARS

	1978 Second Concurrent Resolution	Projections				
		1979	1980	1981	1982	1983
Current Policy Receipts	397.0	456	514	579	648	722
Current Policy Outlays	458.25	493	529	565	605	651
Current Policy Margin	-61.25	-37	-15	14	43	71
Fiscal Drag Offset	-- a/	32	53	81	110	136
Deficit (-) or Surplus	-61.25	-69	-68	-67	-67	-64

a/ It is assumed that the spending ceiling and revenue floor in the second concurrent resolution are consistent with the fiscal stimulus needed for the economy to grow at the rate of 4.8 percent in fiscal year 1978. If more or less fiscal stimulus is required, corresponding adjustments would have to be made in the estimates of the fiscal drag offset for fiscal years 1979-1983.

APPENDIX C. FEDERAL EXPENDITURES ON A NATIONAL INCOME ACCOUNTS BASIS

The unified budget and the federal sector of the national income accounts (NIA) both measure receipts and expenditures of the federal government. The national income accounts, however, focus on current income and production, and are, therefore, the most widely used indicator of aggregate economic activity.

The distinction between the unified budget and the NIA federal sector arises principally from netting and grossing differences, coverage differences, timing differences, and the NIA exclusion of financial transactions. Thus, both additions to and subtractions from the unified budget are required to obtain the national income accounts measure. The federal government's expenditures on a national income accounts basis are divided into several categories: defense and nondefense purchases, domestic and foreign transfers, grants-in-aid to state and local governments, domestic and foreign interest, and subsidies less the current surplus of government enterprises.

DIFFERENCES BETWEEN THE UNIFIED BUDGET AND FEDERAL EXPENDITURES ON A NATIONAL INCOME ACCOUNTS BASIS

Since the national income accounts focus on current income and production, they exclude transactions such as lending and borrowing that are merely asset and liability transfers. These activities certainly influence production and income but are not appropriately included in their measurement. The interest expended or earned as a result of financial transactions is, however, included in the NIA under the net interest category.

Just as lending and borrowing are excluded as exchanges of assets, so are bonuses paid on Outer Continental Shelf (OCS) oil leases and the purchase and sale of land. The unified budget treats OCS bonuses as proprietary receipts which are offset against outlays. This and other procedural differences mean that the federal surplus or deficit varies, depending on whether it is measured in unified budget or NIA terms.

Other differences between the federal sector of the NIA and the unified budget arise from certain netting and grossing adjustments. All such adjustments involve the subtraction or addition of identical amounts to both unified budget outlays and receipts. Thus, while netting and grossing operations affect the magnitude of receipts and outlays, they have no

impact on the surplus or deficit. One example of a grossing adjustment involves government contributions for employee retirement. In the unified budget, these contributions are not reflected in the totals since they are offset by intragovernmental transactions. In the NIA, however, government contributions for employee retirement are included as part of employee compensation, a practice comparable to private sector accounting. On the expenditure side of the budget, these payments fall into nondefense purchases unless they are made by government enterprises, in which case they are reflected in the current deficit of government enterprises. On the receipts side, they are included in contributions for social insurance. Other netting and grossing items include imputed contributions for social insurance for unemployment compensation and for workman's compensation, receipts for certain government life insurance programs, and other transactions that are more properly classified as budget receipts rather than as budget expenditures or offsets to these. Finally, expenditures for the earned income tax credit, which appear as negative receipts in the unified budget, are treated as transfers in the NIA.

Timing differences account for another class of adjustments. Except for interest on the public debt (which is recorded on an accrual basis) unified budget outlays are recorded on a cash basis. In the NIA, various timing bases are used. In general, transfers and grants are recorded on a cash basis; interest, subsidies, and the current surplus/deficit of government enterprises are recorded on an accrual basis; and purchases are recorded on a delivery basis. Major timing differences occur in the defense area, in which the unified budget records outlays as they are made but the NIA record them at time of delivery.

Coverage differences comprise a final category of adjustments. Such differences involve the NIA geographical exclusion of transactions with Puerto Rico, the Virgin Islands, and other U. S. territories, and inclusion of certain foreign currency transactions not in the budget. Also included here are transactions of off-budget entities.

For an indication of the magnitude of the various kinds of adjustments, Table C-1 shows adjustment values for 1977 through 1983. ^{1/}

^{1/} It is important to note that the adjustment categories given in Table C-1 are not directly comparable with those given in the Survey of Current Business (SCB). The principal difference arises from the methods used to include the transactions of off-budget entities. The SCB tables usually reflect total outlays of off-budget entities under "Coverage -- other"; adjustments to these totals then appear in the appropriate categories. The CBO method involves the addition of the relevant off-budget transactions only.

The projected growth in the adjustments for government contributions is reasonable, since these adjustments are heavily dependent on federal wage levels. Among other things, the growth in the other netting and grossing category reflects a projected increase in rents and royalties from the Outer Continental Shelf, treated in the NIA as budget revenues rather than as offsets to expenditures. Though the negative adjustment for net lending is projected to grow, it is important to note that the actual adjustment for a given year could easily deviate from the expected pattern if loan repayments or other transactions that have a positive impact upon net lending are higher than anticipated. The adjustment for defense timing is extremely volatile and can be expected to change. Likewise, variations in the OCS bonuses may occur. Though the "Other" category remains relatively stable, it includes two offsetting trends: an increase in geographical exclusions (a negative impact) and an increase in the estimated outlays of off-budget entities, mainly the Postal Service.

TABLE C-1. ADJUSTMENTS BETWEEN THE UNIFIED BUDGET AND FEDERAL EXPENDITURES IN NATIONAL INCOME ACCOUNTS: BY FISCAL YEARS, IN BILLIONS OF DOLLARS

	1977 Estimate	1978 Second Concurrent Resolution	Current Policy Projections				
			1979	1980	1981	1982	1983
Unified Budget Outlays	401.9	458.3	494.8	529.3	564.9	606.1	654.9
Lending and financial transactions	-1.7	-4.2	-6.1	-6.9	-7.1	-7.4	-7.5
Government contribution to employee retirement (grossing)	6.6	7.0	7.7	8.4	9.1	9.9	10.7
Other netting and grossing	3.3	3.8	4.0	4.4	4.8	5.3	5.9
Defense timing adjustment	3.1	0.4	0.3	0.3	0.3	0.3	0.3
Bonuses on Outer Continental Shelf land leases	1.7	2.0	1.7	1.7	1.9	2.3	1.3
Other ^{a/}	-2.8	-2.3	-2.2	-2.0	-2.1	-2.0	-1.8
Federal Sector, NIA Expenditures	412.1	465.0	500.2	535.2	571.8	614.4	663.8

^{a/} Includes nondefense timing adjustments, geographical adjustments, the appropriate transactions of off-budget entities, and so forth.

THE CBO NIA MODEL

The CBO national income accounts model is a simple tabulator which basically makes adjustments to the unified budget at the account level. A new feature of this model is a bridge component that enables it to keep track of the various reasons behind each adjustment that is made.

In general, four operations are carried out for each account: (1) a numerical adjustment (a fixed percentage of the unified budget) is calculated; (2) the adjustment is added or subtracted from the unified budget number to produce outlays on an NIA basis; (3) the resulting NIA number is spread by fixed percentages over the appropriate categories (purchases, transfers, and so forth); and (4) the adjustment is divided by fixed percentages among the relevant bridge items (lending, netting and grossing, and so forth).

The fixed percentages used in these calculations are based on detailed information describing the adjustments and spreads for 1974 and 1975. Wherever possible this adjustment pattern has been updated with the information provided in the 1977 and 1978 budget appendix, as well as with information from CBO program specialists. Items that are included in the NIA but not in the unified budget are computed by hand.

The basic NIA model has been functioning for slightly over a year; the bridge component was only recently completed. The model has been used to translate many different "budgets": the President's budget, House and Senate resolutions, and CBO budget estimates. In those instances in which the same budget is translated by the Bureau of Economic Analysis (BEA) or the Office of Management and Budget (OMB), the validity of the CBO model is measured by its ability to produce translations that are close to those of BEA and OMB. In this respect, the model now appears to be operating at a relatively high level of accuracy.

FEDERAL EXPENDITURES, NATIONAL INCOME ACCOUNTS, FISCAL YEARS 1978 TO 1983

Table C-2 displays national income account expenditures produced with the aid of the CBO NIA model. The underlying unified budget numbers, as well as the reconciliation between unified budget and NIA totals, are those presented in Table C-1. It is important to note that estimates of NIA totals and their distribution among categories are sensitive to numerous economic and budget assumptions. Variations in such assumptions can produce quite different NIA estimates.

The projected growth in purchases is close to the inflation rate that has been assumed for the projection period. The projected expenditures for transfers reflect both inflation and an increase in the number of social security recipients. The relatively small growth in grants is due to an assumed phaseout of the antirecession programs. The lack of change in the net interest category is attributable to the assumption that the budget deficit will decline during the projection period and the large increase in

TABLE C-2. ESTIMATES OF FEDERAL EXPENDITURES IN NATIONAL INCOME ACCOUNTS: BY FISCAL YEARS, IN BILLIONS OF DOLLARS

	1978 Second Concurrent Resolution	Current Policy Projections				
		1979	1980	1981	1982	1983
Purchases	160.9	172.0	184.7	196.0	211.3	226.7
Defense	101.7	109.5	118.4	128.3	138.3	149.0
Nondefense	59.2	62.5	66.3	67.7	73.0	77.7
Transfer Payments	183.9	201.3	218.2	238.1	259.2	286.3
Domestic	180.6	197.5	214.0	233.7	254.5	281.3
Foreign	3.3	3.8	4.2	4.4	4.7	5.0
Grants	78.1	78.0	79.8	81.4	84.6	88.9
Net Interest	33.7	36.6	39.0	40.5	41.7	41.9
Subsidies less Current Surplus	8.4	12.3	13.5	15.8	17.6	19.9
Subsidies	7.3	10.3	11.3	13.3	14.7	16.6
Less: current surplus	-1.1	-2.0	-2.2	-2.5	-2.9	-3.3
TOTAL	465.0	500.2	535.2	571.8	614.4	663.8

subsidies less the current surplus is influenced by, among other things, assumptions about the outlay pattern of the Commodity Credit Corporation, the Postal Service, and housing payments. Clearly, variations in assumptions about inflation, the size of the recipient population for transfer programs, the continuation of antirecession programs, and so on, would produce somewhat different estimates than those given in Table C-2.

THE SHORTFALL IN THE NATIONAL INCOME ACCOUNTS

Table C-3 compares BEA's translation of Carter's February budget (also the Third Concurrent Resolution on the Budget for Fiscal Year 1977) with an average of BEA's quarterly translations for fiscal year 1977. Based on this comparison there has been a significant shortfall in expenditures. This shortfall is most pronounced in transfers and grants, but is also quite evident in both defense and nondefense purchases.

TABLE C-3. FISCAL YEAR 1977 SHORTFALL ON A NATIONAL INCOME ACCOUNTS BASIS: IN BILLIONS OF DOLLARS

	Carter Budget/ Third Concurrent Resolution <u>a/</u>	1977 Actuals <u>b/</u>	Shortfall
Unified Budget Outlays	417.4	401.9	15.5
NIA Totals	426.3	412.1	14.2
Purchases	145.0	140.9	4.1
Defense	94.8	91.9	2.9
Nondefense	50.2	49.0	1.2
Transfer Payments	174.5	170.3	4.2
Domestic	171.2	167.1	4.1
Foreign	3.3	3.2	0.1
Grants	70.3	65.8	4.5
Net Interest	29.1	28.8	0.3
Subsidies less Current Surplus	7.4	6.3	1.1

a/ Numbers taken from U. S. Department of Commerce, Survey of Current Business, May 1977, p. 2.

b/ This column represents an average of the quarterly translations prepared by the Bureau of Economic Analysis. Data for the first three quarters of fiscal year 1977 were obtained from the Survey of Current Business, September 1977, Table 12, p. 12. Data for the final quarter are those that were released October 17, 1977.

Mrs. RIVLIN. The primary purpose of CBO's current policy projections is to provide a neutral baseline for evaluating the effects of new proposals on the long-run size and shape of the budget.

As you know, the projections are estimates for 5 years ahead of Federal spending and revenues under current policies, adjusted for demographic and economic changes in those 5 years.

The impact of new legislation on spending or revenues can be added to or subtracted from this current policy base. This year, in addition to estimating the effects of economic change on the budget, CBO has made estimates of the amount of additional spending or tax cuts likely to be required to sustain for 5 years the economic growth objectives adopted in the Second Concurrent Resolution on the Budget for Fiscal Year 1978.

My testimony today will focus on three areas: (1) A summary of the CBO current policy projections of receipts and outlays; (2) estimates of the tax cuts or spending increases that would likely be required if the economy were to continue to grow at the rates assumed in the second concurrent resolution; and (3) a brief discussion of how 5-year projections might be useful in the formulation of multiyear budgetary targets.

CURRENT POLICY PROJECTIONS

Economic assumptions

Inflation, unemployment, and other levels of economic activity have a major effect on revenues and outlays; hence, projections require assumptions about the state of the economy during the projection period.

In the CBO report, "Five-Year Budget Projections: Fiscal Years 1979-1983," the major economic assumption is a continuing recovery with declining unemployment.

The economic assumptions for 1977 and 1978 are taken from the conference report on the second concurrent resolution on the budget. The assumptions for 1979 through 1983 represent an extrapolation of the economic growth objective for 1978 contained in the conference report, with real economic growth—as measured by the rate of growth in the gross national product (GNP) in constant dollars—holding at about 4.8 percent through 1982 and dropping to 3.7 percent in 1983 as the unemployment rate reaches 4.5 percent.

The economic assumptions for 1979 through 1983, which are shown in table 1, should be viewed as one of the many possible long-range targets for the economy. The rate of growth assumed is optimistic by historical standards, but not unrealistic.

[Table 1 follows:]

TABLE 1.—AGGREGATE ECONOMIC ASSUMPTIONS

[By calendar years]

Selected economic variables	1977	1978	1979	1980	1981	1982	1983
Gross national product (GNP):							
Current dollar GNP (in billions of dollars).....	1, 898. 0	2, 107. 0	2, 333. 8	2, 582. 2	2, 853. 9	3, 156. 4	3, 465. 2
Real GNP (in billions of 1972 dollars).....	1, 338. 0	1, 402. 7	1, 467. 9	1, 538. 4	1, 612. 2	1, 688. 3	1, 751. 4
Growth rate of real GNP.....	5. 0	4. 8	4. 7	4. 8	4. 8	4. 7	3. 7
Unemployment rate (percent).....	7. 0	6. 5	6. 2	5. 7	5. 2	4. 7	4. 5
Consumer Price Index (percent change).....	6. 5	5. 6	6. 0	5. 7	5. 5	5. 7	5. 9

Senator PROXMIRE. Could I interrupt; you said "long-range targets."

Mrs. RIVLIN. Yes; I think one could view them as targets.

Senator PROXMIRE. Rather than projections of what you would expect was the realistic likelihood?

Mrs. RIVLIN. We are using these as assumptions. We have to assume something.

Senator PROXMIRE. Right.

Mrs. RIVLIN. They are fairly optimistic assumptions about what would happen to the economy and I think could be viewed as targets for economic growth.

Budget implications of economic assumptions

Under these assumptions, current policy receipts would rise faster than outlays. Projected receipts would increase from \$457 billion in fiscal year 1979 to, \$751 billion in 1983. As a percent of GNP, current policy receipts would increase from 20 to 22 percent. Current policy outlays would rise from \$495 billion in fiscal year 1979 to \$655 billion in fiscal year 1983, declining from 22 to 19 percent of gross national product. The disproportionate rise in receipts as compared with outlays occurs because of the progressive nature of individual income taxes.

The receipts the Government would be taking out of the economy would thus rise much faster than the outlays it would be putting back into the economy in the form of wages, purchases, and payments to individuals. Hence, if current policies are followed unchanged during the next 5 years, the Federal budget would exert a restrictive influence on the economy. Consequently, for the optimistic assumptions for economic growth to be realized, fiscal and monetary policies would have to be used to offset this fiscal drag exerted by the projected current policy budgets.

PROJECTED FISCAL DRAG OFFSETS¹ AND DEFICITS

As a new feature of this year's 5-year projections report, estimates have been included of the approximate amount in tax cuts or spending increases that would be needed to offset this fiscal drag.

The size of the needed Federal offset depends, of course, on the strength of non-Federal demand; namely, consumption, investment, State and local government purchases, and net exports.

Stronger non-Federal demand would decrease the tax cuts and spending increases needed to achieve the assumed growth path, whereas weaker non-Federal demand would increase the necessary offset.

For the 5-year projections reports, CBO assumed a scenario for non-Federal demand that is moderate by historical standards—stronger than the average of the post-World War II years, but somewhat weaker than the peak period of 1961 through 1966.

Using this assumption for non-Federal demand, roughly \$115 billion in additional budget stimulus—namely, tax cuts or spending increases—would be needed by fiscal year 1983 to offset the fiscal drag implicit in current policy projections of receipts and outlays.

¹ "Fiscal drag offset" is defined here as the stimulus needed to achieve the desired economic goals, given non-Federal demands.

In order to determine what projected Federal budget deficit or surplus is consistent with realization of the economic assumptions, this \$115 billion that is needed to offset the fiscal drag and achieve economic goals must be compared with the current policy margin, which is the amount generated by the excess of current policy receipts over outlays.

As long as the fiscal drag offset is greater than the current policy margin the budget is projected to remain in deficit. As shown in table 2, this would happen throughout the 5-year period under the moderate assumption about non-Federal demand. By fiscal year 1983, the projected deficit would have declined to about \$19 billion, but the budget would still not be in balance.

[Table 2 follows:]

TABLE 2.—5-YEAR BUDGET PROJECTIONS

[By fiscal years; in billions of dollars]

	1978 2d concurrent resolution	Projections				
		1979	1980	1981	1982	1983
Current policy receipts.....	397.0	457	519	590	668	751
Current policy outlays.....	458.25	495	529	565	606	655
Current policy margin.....	-61.25	-38	-10	25	62	96
Fiscal drag offset.....	(1)	29	51	74	101	115
Deficits (-) or surplus.....	-61.25	-67	-61	-49	-39	-19

¹ It is assumed that the spending ceiling and revenue floor in the 2d concurrent resolution are consistent with the fiscal stimulus needed for the economy to grow at the rate of 4.8 percent in fiscal year 1978. If more or less fiscal stimulus is required, corresponding adjustments would have to be made in the estimates of the fiscal drag offset for fiscal years 1979-83.

Mrs. RIVLIN. The scenario just described is a plausible one, but it certainly is not the only possible outcome. If a sustained business investment boom developed, either spontaneously or in response to expansionary monetary policy, or if growth in economic activity in the rest of the world stimulated U.S. exports, the need to offset the fiscal drag would be smaller and the budget deficit would decline more rapidly.

For example, using more optimistic assumptions about non-Federal demand, comparable to the kind experienced in the early 1960's, the required fiscal drag offset would equal the current policy margin by fiscal year 1982—which means the budget would be balanced by that date.

On the other hand, if non-Federal demand were to grow very slowly, more expansionary policies and an increasing budget deficit might be needed to reach the assumed output and unemployment goals.

For example, under weaker assumptions about non-Federal demand, it might take deficits of \$60 billion to \$70 billion through fiscal year 1983 just to sustain a 4-percent economic growth rate.

MULTIYEAR TARGETING

As you know, budget resolutions are now adopted by the Congress for 1 year at a time. Since a large part of any given year's budget is determined by decisions made in prior years, the Congress in each year is faced with a budget largely composed of spending and receipts that have not been subject to review within an integrated framework.

As part of its responsibility under section 502(c) of the Congressional Budget Act of 1974, CBO conducted a study on the feasibility and advisability of advancing all or some budget decisions so that, instead of making them just before the start of a fiscal year, they could be made at least 12 months in advance.

In that study, CBO recommended that the Congress begin formulating advance budget targets, with the eventual goal of annually adopting targets not only for the budget year, but for the 4 following years.

Projections like those found in the report are a useful baseline on which to build plans for future spending and receipts. In addition, estimates of the budget stimulus needed to offset fiscal drag provide a rough idea of how much room will be available for net increases in spending or tax reductions, under various economic assumptions.

Several key questions are involved in setting multiyear targets. What are the goals for the economy and for the deficit? How much should be allocated for tax cuts or spending increases? What should be the level for Federal spending and receipts as a percent of GNP?

The CBO 5-year-projections report suggests that an unemployment rate of 4.5 percent and a deficit of about \$19 billion might be achieved by fiscal year 1983, assuming an accommodative monetary policy and slightly above average performance for the non-Federal sectors of the economy.

In order to balance the budget by fiscal year 1983, however, the performance of the non-Federal sectors would have to be stronger than that.

On the other hand, if the initial assumptions about non-Federal demand were borne out, but a more optimistic goal was set for unemployment rates, the budget stimulus required would be greater than that estimated here, and the budget deficit would decline more slowly.

In addition to setting goals for the economy and the deficit, the Congress might want to set goals for the level of spending or for the level of receipts in relation to the economy.

For example, the Congress might set as a goal the maintenance of a specified level of Federal spending as a percent of GNP. At present, spending is 21.2 percent of potential GNP—defined as the value of the gross national product if the economy were at a 4.5 percent unemployment rate—but current policy projections show the Federal Government's share of potential GNP falling to 19.3 percent by fiscal year 1983.

If the Congress were to set as a goal the maintenance of the current 21.2 percent Federal share, a sizable part of the fiscal drag offset alluded to earlier would have to be used for spending increases.

As an alternative to maintaining the current Federal share of potential GNP, however, the Federal income tax system might be indexed, so that effective rates of taxes would not rise because of inflation.

This would cut taxes below current policy from year to year, because the progressive income tax system implicit in current policy has a more than proportional response to inflation.

As a result, indexing would commit a portion of the fiscal drag offset for these automatic tax cuts. The remainder would be available either for further tax cuts or for spending increases.

The most important decisions in a multiyear targeting process involve program needs and costs. Current policy projections of outlays

and revenues again provide a neutral base that can be used to frame these decisions.

As indicated in table 3, the current policy base contains only slight changes from the current distribution among types of Federal programs. As a percent of the total, national defense outlays would rise slightly from 24 to 25 percent. Outlays for contributory payments to individuals would grow from 32 to 36 percent, largely because of changes in the number of social security and medicare beneficiaries. Outlays in the form of grants to State and local governments would fall from 12 to 10 percent because of the phaseout of certain counter-cyclical programs, as the economy improves.

[Table 3 follows:]

TABLE 3.—PERCENT OF TOTAL CURRENT POLICY OUTLAYS BY SOURCE

[By fiscal years]

	1977 estimate	1978 2d con- current resolution	Projections				
			1979	1980	1981	1982	1983
National defense.....	24	24	24	24	25	25	25
Contributory benefit payments to individuals.....	34	32	33	33	34	35	36
Other benefit payments for individuals.....	11	11	11	11	11	11	10
Grants to State and local governments.....	12	12	12	11	10	10	10
Net interest.....	7	7	7	7	7	7	6
Other Federal operations.....	12	13	14	14	13	13	13
Total.....	100	100	100	100	100	100	100

Mrs. RIVLIN. As indicated in table 4, greater changes would occur among types of Federal receipts. If tax policies were not to change over the next 5 years, the individual income tax, because of its progressive nature, would account for a greater percentage of total revenue, rising from its current 44 percent of total revenue to 52 percent by 1983.

[Table 4 follows:]

TABLE 4.—PERCENT OF TOTAL CURRENT POLICY RECEIPTS BY SOURCE

[By fiscal years]

	1977 estimate	1978 2d con- current resolution	Projections				
			1979	1980	1981	1982	1983
Individual income taxes.....	43.9	44.1	46.6	48.2	49.2	50.6	51.8
Corporate income taxes.....	15.4	14.9	14.7	14.6	14.6	14.2	14.1
Social insurance taxes and contributions.....	30.4	31.3	30.0	28.9	28.1	27.8	27.0
Excise taxes.....	4.9	5.1	4.4	4.0	3.7	3.6	3.3
Estate and gift taxes.....	2.0	1.4	1.3	1.3	1.4	1.2	1.1
Customs duties.....	1.5	1.4	1.3	1.3	1.4	1.3	1.3
Miscellaneous receipts.....	1.8	1.8	1.8	1.5	1.4	1.2	1.1
Total.....	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Mrs. RIVLIN. Over the same period, corporate income taxes would account for approximately the same proportion of the total, while social insurance taxes and contributions would fall from their current 31 percent of total receipts to 27 percent in 1983.

If pending social security legislation were enacted, however, the share of total receipts that are for social insurance taxes and contributions would decline very little.

The Congress, of course, has the option of modifying the current policy base. Program changes that range from welfare reform to national health insurance to energy legislation could, if enacted, significantly change the balance among types of programs.

In addition, each of the three major tax categories is a likely object of significant revision over the next 5 years. Changes in social security taxes are currently before the Congress and modifications of the income tax structure that could involve such issues as the integration of corporate and individual income taxes and incentives for capital formation will probably come before the Congress within the next few years.

These individual program changes will be debated within the context of, and will affect, other congressional goals—such as achieving full employment, reducing or controlling inflation, achieving a given magnitude of Federal effort, and producing a balanced budget.

A hard fact is that in only the most optimistic scenario of non-Federal demand will the Congress be able to achieve all its desired economic and budgetary goals. Consequently, the Congress will have to face hard tradeoffs among program goals, full employment, and a balanced budget.

Although such choices probably cannot be avoided, the Congressional Budget Office believes that they can best be addressed in an advanced targeting framework.

Thank you, Senator Proxmire.

Senator PROXMIRE. Thank you, Mrs. Rivlin.

I think this is a very, very helpful statement for giving us a realistic framework within which to act on economic policies.

You said when I interrupted you that you thought this might be regarded as a target as well as a projection. I presume the 4.5-percent unemployment rate, as I said in my opening statement, is a fairly optimistic target.

I think on the basis of our most recent experience we would be happy with that. But I cannot understand how we can possibly justify a 6-percent inflation as any kind of a target.

It seems to me that that would be a real failure if we have that 5 or 6 years from now. How do you explain that 6-percent level?

Mrs. RIVLIN. No one thinks that 6-percent inflation is desirable. The reason we have assumed 6 percent in this projection is that we believe that, unfortunately, the level of 6 percent is probably consistent with achieving a 4.5-percent unemployment rate by 1983.

Inflation, as you know Senator Proxmire, has proved extremely intractable. Once we have it, it is very hard to get rid of it. An optimist about inflation is one who thinks it won't get much worse. That is about what we are saying here—that the 5 to 6 percent that we have been experiencing over the last couple of years will not, in our view, necessarily accelerate as we move to 4.5 percent unemployment.

Senator PROXMIRE. Then you are saying that there is in fact a tradeoff, whether we like it or not; if we are going to try to reduce inflation, we are going to have to settle for a higher level of unemployment; if we are going to try to reduce unemployment more sharply, we will have to settle for a higher rate of inflation.

The Phillips curve is still true in spite of our recent experience of the last couple years which seem to give us both high rates of inflation and high levels of unemployment?

Mrs. RIVLIN. Yes; we are saying that, Senator Proxmire. There is a great deal of uncertainty about this relationship, but we do believe that certainly in extreme cases, if we were to move faster on the growth rate, say, to get a 4-percent unemployment rate in 5 years or go below that, that there would be costs in terms of inflation. Such growth would accelerate, to some extent, the inflation rate.

Senator PROXMIRE. Well, now, the Humphrey-Hawkins bill says two things. I want to ask you, incidently, what that would do to these projections if we enact the Humphrey-Hawkins bill.

No. 1, it sets a target of 4 percent unemployment. I am not sure of that; maybe you can tell me about the timetable—is that 4 percent unemployment within 5 years? Is that the projection?

Mrs. RIVLIN. By 1983, yes. It is the same time frame that we are talking about.

Senator PROXMIRE. That is a half percent below what you have.

Mrs. RIVLIN. That is right.

Senator PROXMIRE. Are you saying, then, if we should pass the Humphrey-Hawkins bill, that on the basis of realistic assumptions, we should expect to have an inflation rate of higher than 6 percent, maybe 7 percent, something like that?

Mrs. RIVLIN. It would certainly add somewhat to inflationary pressure.

Senator PROXMIRE. Supposing we should adopt—I am thinking very seriously of putting in an amendment to the Humphrey-Hawkins bill that would set a specific numerical target for inflation as well as for employment.

I want to be realistic about it; at the same time, I think you could argue very strongly and you could probably get support in the Congress, including the Senate Banking Committee, for a 2- or 3-percent target for unemployment in 5 years.

But, you are saying if you do that, you are going to have to either not achieve it, or if you do achieve it, probably have a very high level of unemployment.

Mrs. RIVLIN. Of inflation; yes. It depends, of course, on how you do it. And there would be some measures, such as increased public employment, that would have less inflationary effect than achieving the higher growth rate for economic policy.

Senator PROXMIRE. The Humphrey-Hawkins bill in all fairness, while it sets a level of unemployment, it also intends to do everything it could to achieve price stability. So assume you follow policies that are just as noninflationary as you can consistent with the reduction of unemployment.

Mrs. RIVLIN. Then, what would happen to inflation?

Senator PROXMIRE. Right.

Mrs. RIVLIN. I think, consistent with our projections, one would certainly worry that the inflation rate would escalate above 6 percent as you moved below the 4.5-percent unemployment.

Senator PROXMIRE. Now, you also have in your statement the argument that on the basis of the assumptions, which you say are relatively optimistic, we will have a \$19 billion deficit in 1983.

Mrs. RIVLIN. Approximately.

Senator PROXMIRE. But with somewhat more optimistic assumptions you could have a balanced budget in 1983 or 1982; is that right?

Mrs. RIVLIN. Yes.

Senator PROXMIRE. Now the President has indicated that his goal is to achieve a balanced budget in 1981. He now seems to indicate that that is not a commitment but a goal, if not a dream.

Mrs. RIVLIN. I don't think he has said 1981 very recently, Senator.

Senator PROXMIRE. I guess he keeps moving that year up. It is like Arthur Burns' attempt to justify achievement of a specific target for increasing the money supply. He forgets about what has been done in the preceding few months and keeps pushing it up.

But 1981 was certainly the asserted goal a few months ago. It would be interesting to hear whether you would say 1981 is at all practical or possible to achieve with a level of unemployment of, say, 5.5 or 6 percent?

Mrs. RIVLIN. We think it would be very difficult to achieve a balanced budget by 1981 on the growth path that we have projected.

Senator PROXMIRE. What kind of growth path would you need? You said "very difficult."

How could you achieve a balanced budget by 1981?

Mrs. RIVLIN. By 1981. One would have to have sustained growth of over 5 percent to achieve that by 1981. That would imply that the non-Federal sectors, the private sector, State and local governments, would have to be extraordinarily strong, way above historical averages and even somewhat above our report's optimistic scenario for non-Federal demand.

Senator PROXMIRE. Has there ever been a time in our economic history that you can recall when after having had a period of a couple years of recovery, I guess it is a couple years now, a little more than that now, I guess, it started in the spring of 1975, this is the fall of 1977, about 2½ years of recovery; has there ever been a period when we have had that sustained growth at the level you are talking about that would give us a balanced budget by 1981?

Mrs. RIVLIN. We came quite close in the early 1960's; 1961 to 1966 was a sustained period of high growth. If we could match that again, we would come close to balancing the budget by 1981. But we would have to do even a little better than was done in the 1960's.

Senator PROXMIRE. We would have to do even better than we have done with the best record we have ever had to balance the budget by 1981?

Mrs. RIVLIN. Yes; we would.

Senator PROXMIRE. Are there any anti-inflation policies that would not increase unemployment that you think ought to be considered?

Mrs. RIVLIN. No one has easy answers to inflation. There are a variety of possibilities. Some form of incomes policy or wage-price control would be the first thing one would think about.

Senator PROXMIRE. Well, the administration apparently is firmly committed against wage-price controls or income policies, I understand. Let's rule that out.

What is next?

Mrs. RIVLIN. What is next, I think, would be a variety of attempts on the part of the Federal Government to mitigate inflation. Certainly lowering payroll taxes would have that effect. Not increasing the minimum wage would have an anti-inflationary effect.

Senator PROXMIRE. Well, that is in place, that has been signed into law.

Mrs. RIVLIN. That is right.

Senator PROXMIRE. So we know that will be in the law for 3 or 4 years.

Mrs. RIVLIN. I don't have a ready-made kit of tools for doing this once one rules out some of the more obvious things.

Senator PROXMIRE. You have the Wallich proposal and the Okun proposal, both of which would rely on the tax system to encourage employers to hold down wages and to hold down prices.

Mrs. RIVLIN. Yes, those are interesting proposals, I think.

Senator PROXMIRE. Put into the framework projected here, would they in your view give us a better tradeoff of unemployment to inflation?

Mrs. RIVLIN. Yes; they are in a sense a form of incomes policy in which one would use the Federal tax system to give incentives to keep wages and prices from increasing as rapidly as they have been. If they were to work; yes, they would mitigate inflation.

Senator PROXMIRE. All right.

Mrs. RIVLIN. Another possibility along the same lines has been the suggestion of using Federal incentives to encourage State and local governments to cut their sales taxes which would also have an anti-inflationary effect.

Senator PROXMIRE. Can you give some numerical notion of how important these would be? To what extent in your view would that kind of policy providing a corporation income tax incentive, for instance, of a reduction or increase, an increase if they increased price and a reduction if they decreased them—what are the limits of policies of that kind or of the kind that Arthur Okun is suggesting; or the sales tax proposals?

Are they pretty marginal? Do they give us less than one-half of 1 percent less inflation, something of that kind; or are they something that would be rather sharp and clear?

Mrs. RIVLIN. No one knows, Senator. These are new proposals with which there is no experience. It is difficult to estimate how effective they would be and we have not focused on these proposals in any detail.

Clearly, if one could hold the increase in wages—

Senator PROXMIRE. There is no experience in any other country with that kind of policy? It is completely untried; is that right?

Mrs. RIVLIN. There is experience with incomes policy—

Senator PROXMIRE. Oh, no, no, I know there is with incomes policy including experience here. I am talking about experience with a tax action that would provide a tax incentive for holding down prices and holding down wages.

Mrs. RIVLIN. I don't know of any direct experience, but there may be some.

Senator PROXMIRE. Do your colleagues know of any?

[Negative response.]

Senator PROXMIRE. If unemployment were achieved such as is called for in the Humphrey-Hawkins bill, if 4 percent were to be reached; what would be the difference in gross national product and gross receipts given your present projections?

Mrs. RIVLIN. If unemployment were to come down to 4 percent by 1983, which is consistent with the Humphrey-Hawkins target, we would then estimate that current policy receipts would be \$760 billion, and current policy outlays would be \$654 billion. That would give us—without anything else happening—a surplus of \$106 billion. But one would not expect to achieve that, since the drag on the economy would be considerable, and we estimate that in order to get to those targets, one would need a deficit by that year of about \$40 billion.

Senator PROXMIRE. So, you would have to either spend more, tax less, or both, in order to achieve that?

Mrs. RIVLIN. That is right.

Senator PROXMIRE. So you would have a deficit even with unemployment of 4 percent?

Mrs. RIVLIN. To get to the 4 percent unemployment, you would have to use the Federal budget in a stimulatory manner. We are also assuming a moderate performance on the part of the non-Federal sector.

Senator PROXMIRE. Right.

Let me ask you, how good are these 5-year projections really?

Mrs. RIVLIN. What an unfair question!

Senator PROXMIRE. Are they a mechanical arithmetical projection? Maybe you can tell me. I have my own feelings about their being useful but I would like to hear your feeling about it.

Are there advantages in them to businessmen, the public, are they likely to be misleading, possibly more misleading than they are worth? Or how do you justify them?

Mrs. RIVLIN. I think there is a basic dilemma for decisionmaking. It is very difficult to look ahead and predict accurately the performance of anything as complicated as the U.S. economy. Any set of projections, even a year ahead, is quite likely to be wrong and we have had experience over the last several years that would certainly bear that out.

On the other hand, it is important to look ahead and to see what the various possibilities are and these sets of projections, I think, give a framework for decisionmaking in the sense that they try to outline the conditions under which various things would happen.

They tell you roughly what would happen to the Federal budget if the economy performs in a certain way; and how much stimulus would be necessary through the Federal budget to bring about the growth path that is desired. We cannot claim that they are absolutely accurate or even approximately accurate but they do give the dimensions of the problem with which you are dealing.

Senator PROXMIRE. Let me ask you this: I understand we are in about the third generation of econometric models in making projections and they have been going on for 15 years or something like that.

Can you give me an idea of how accurate they have been and are they getting more accurate; what is the range of error?

Mrs. RIVLIN. In general terms, I think certainly, they are getting more accurate. On the other hand, the world economy has made it extremely difficult to test that proposition in the last several years. One cannot expect econometric models of the U.S. economy to forecast such events as the Arabs raising oil prices, the weather, and other outside activities. All they can do is to tell you, when you get those

outside shocks to the economy, approximately what can you expect from them.

Senator PROXMIRE. I understand, I wouldn't expect them to be accurate and I think there are all kinds of reasons why they shouldn't be.

Nevertheless, as a matter of fact, I would like to know how accurate they have been.

Mrs. RIVLIN. What I am saying is that, when you are dealing in a world where there are these outside kinds of shocks, it is difficult to say what would have happened if you had not had them.

Senator PROXMIRE. Can you tell me, for instance, how badly distorted they were by the tremendous, completely unforeseen development in oil prices in 1973, 1974, 1975, and 1976?

What happened to the projections then? Were they off by an enormous factor? Was inflation much higher than expected?

Mrs. RIVLIN. There was no way that the models could have predicted that. That is not a test of the models. Certainly, inflation was much higher in 1973 and 1974 than would have been predicted by any model.

Senator PROXMIRE. Can you find a period when they were accurate?

Mrs. RIVLIN. Oh, sure. The 1960's models did pretty well, and through certainly part of the 1970's, looking at the short run, the projections have been fairly accurate, once one is given the outside shocks that occurred.

Senator PROXMIRE. I can recall in the last 15 or 20 years that there was a long period when Congress reduced the President's proposals for budget authority. I remember Lyndon Johnson, when he was the majority leader, used to get up on the floor almost every day and chided Senator Dirksen saying the Democrats were much better economizers, much more careful about spending money, held down spending much more than the President and he used to raise the dickens about President Eisenhower being so extravagant and wasteful in spending.

But, as a matter of fact, Congress, for one reason or another did hold down or reduce Presidential proposals for new budget authority.

Now, under the Budget Act, Congress is going the other direction. They have exceeded the President's requests for spending.

Do you have any reason to determine whether in the first place my observation is accurate; in the second place, if it is accurate, is it a good thing or a bad thing?

Mrs. RIVLIN. It is substantially accurate over a period of the Budget Act or over the last 3 years. The congressionally enacted budgets have been slightly higher than the Presidential proposals. I would not venture a comment on whether it was a good thing or a bad thing. The Congressional Budget Office, as you know, does not make recommendations or take policy positions.

Senator PROXMIRE. Do you think that the Federal Reserve Board should be included in the budget process, in the receipts and expenditures examined by Congress through the budget and appropriations process?

Mrs. RIVLIN. I don't really have a view on that, Senator. I think it is part of the whole discussion about the independence of the Federal Reserve and would change the nature of the relationship between Congress and the Federal Reserve.

Senator PROXMIRE. They spend about \$700 million a year, they handle as you know over \$6 billion, and what they don't spend reverts to the Treasury. I should say \$7 billion is what they earn, comes in. And it is beyond me why that shouldn't be included.

But you say you have no opinion?

Mrs. RIVLIN. It seems to me to be part of the discussion of the independence of the Fed but not necessarily the most important part. The important part is how the Congress would exert control over monetary policy itself.

Senator PROXMIRE. I cannot understand how understanding where the money goes would put Congress in a position to affect monetary policy one way or the other.

Now, you say that the income system might be indexed. You take all the fun out of being a Senator. [Laughter.] And out of being a Member of Congress. Concerning inflation, the one thing we can do that we are sure is pretty popular is cut taxes. If you index that you take that away from us.

Mrs. RIVLIN. Right.

Senator PROXMIRE. We have an automatic reason every election year to reduce taxes and I doubt if Congress is going to go along with that kind of recommendation.

Mrs. RIVLIN. You took away some of the fun from yourselves when you indexed the social security benefits. [Laughter.]

Senator PROXMIRE. Well, nobody is perfect. [Laughter.] I want to be sure I fully understand the sensitivity of these long-range projections. As I read your report, you said, first, it assumes the spending levels contained in the second concurrent resolution as a base; and secondly, these spending levels are probably too high.

Using a current outlay estimate of \$450 billion and deducting the \$6 billion to \$8 billion spending shortfall which many indicate is likely, fiscal year 1978 expenditures could be about \$443 billion, \$15 billion below the target levels set in the second concurrent resolution.

Using this lower estimate as a base for 5-year projections and assuming your estimate annual increase of 7.3 percent, expenditures would be roughly \$23 billion below your estimate by 1983.

Do you follow my arithmetic?

Mrs. RIVLIN. Those numbers seem to be too low. The spending level in the second concurrent resolution is \$458 billion. We believe it could come under that by \$3 billion to \$5 billion so that it might be that the total would be \$450 billion. But the numbers you were giving seem unrealistic to me.

Senator PROXMIRE. Well, as I figured it, the reasoning is as I did it. You can modify my assumptions by that comment, if you wish; it could mean that an additional budget stimulus—you discuss \$120 billion by 1983—would be too low by roughly \$25 billion.

This is using your optimistic assumptions about the strength of private demand. You say that is not correct, it would be somewhat less than \$25 billion; is that correct?

Mrs. RIVLIN. Yes. Let me ask if Mr. Capra would like to answer that question.

Senator PROXMIRE. Go ahead, Mr. Capra.

Mr. CAPRA. The report discusses a possible shortfall of \$6 billion to \$8 billion. If you took the rates of increase we are talking about, that \$6 billion to \$8 billion inflates to about \$12 billion by 1983 so I

think that the number, at least by my computations here, would be around \$12 billion or \$13 billion.

So, that would be \$12 billion or \$13 billion, as you pointed out, Senator, of additional stimulus that would be needed under the assumptions we are using.

Senator PROXMIRE. Not \$25 billion but \$8 to \$12 billion.

Mr. CAPRA. Right.

Senator PROXMIRE. A second assumption is that the current social security law remains in effect. Yet you say that the legislation now under consideration would increase taxes by \$23 billion to \$26 billion by 1983.

Now, combining the \$8 billion to \$12 billion spending reduction to a lower 1978 base with a \$23 billion to \$26 billion social security tax increase means that the fiscal stimulus needed by 1983 could easily be some \$40 billion more than you estimated; is that correct?

What is your comment on that?

Mrs. RIVLIN. Again, from what Mr. Capra just said, that is substantially correct. We do believe that an additional \$23 billion to \$26 billion would be needed to offset the fiscal drag, the restrictive effect of social security tax increases.

Senator PROXMIRE. Now, all of this is, of course, assuming strong growth in non-Federal demand. If the scenario of weaker non-Federal demand occurs, weaker demand, I figured \$186 billion, maybe that should be \$175 billion, would be necessary by 1983, yet the unemployment rate would remain at about 5.5 percent.

Do you follow that?

Mrs. RIVLIN. That is right. Under the weaker assumptions about non-Federal demand the picture looks bleak.

Senator PROXMIRE. I am surprised to find no discussion of monetary policy in your description of the economic path which underlies your projections. Surely that will play a role in any projection of the strength of non-Federal demand.

Could you describe in general terms how money is handled in these projections? Specifically, what growth rate in M-1 is necessary to achieve your target of 4.5 percent unemployment?

Mrs. RIVLIN. You are correct, Senator, we did not make explicit assumptions about monetary policy. We have made assumptions about the strength of non-Federal demand. The moderate assumption assumes a rather sustained investment growth at a real rate of about 7 percent, and the optimistic scenario assumes an 8-percent sustained investment growth. Now, both of those imply, especially the most optimistic, an accommodative policy in the amount of—

Senator PROXMIRE. A what monetary policy?

Mrs. RIVLIN. An accommodative monetary policy. It assumes that the Federal Reserve would act to keep interest rates from rising, otherwise I think one would not expect—

Senator PROXMIRE. Do you have any idea what that would mean? Would that mean an increase in the money supply of 5 percent, 6 percent, or 7 percent?

Mrs. RIVLIN. We did not attempt to specify that.

Senator PROXMIRE. What level of long-term interest rates do you assume for that?

Mrs. RIVLIN. Let me see if we have those.

We can supply those for the record, Senator.

Senator PROXMIRE. We would like to get that.

[The following information was subsequently supplied for the record:]

Long-term assumed interest rates, by calendar year

Calendar year:	Moody's rate
1977.....	8.01
1978.....	8.08
1979-83.....	8.13

Senator PROXMIRE. It is interesting to hear and good to hear your recognition that monetary policy would play a significant role in these areas.

Mrs. RIVLIN. Oh, it would. Monetary policy would be one of the most important determinants of the strength of non-Federal demand. And, clearly, it would take an expansionary monetary policy to achieve the optimistic non-Federal demand scenario or even a moderate one.

Senator PROXMIRE. Incidentally, are you familiar with a study, and I just read about it the other day. This is a study of some 200 years of experience in England which indicated—I just made a note of it—the study by Robert Schiller and Jeremy Seagull, published, of all places, by the University of Chicago, which has been monetarist, but this is criticizing the monetarist view.

They say that using some 250 years of interest rate and price data from Britain torpedoed the idea that interest rates fluctuate only because of the expected rate of inflation.

The Schiller-Seagull analysis indicates easier money will not simply push up prices but will spur economic growth.

That is the thesis that the nonmonetarists, I take it, have assumed. They recognize that, of course, there is some inflationary effect, but there is also a considerable effect on economic growth.

I take it you espouse that view?

Mrs. RIVLIN. Yes; I have not only seen that study but I think monetarists and fiscalists are coming together these days and there is a widespread view that monetary policy does affect the economy, not just through prices alone.

Senator PROXMIRE. Now, if growth in 1978 is weaker than you forecast, necessitating a more expansive policy than that contained in the second concurrent resolution, what would you regard as appropriate behavior by the Federal Reserve Board?

Mrs. RIVLIN. I hesitate to prescribe to the Federal Reserve Board but, presumably, if the economy comes in weaker than we have all assumed, then both a more expansionary fiscal policy and a more expansionary monetary policy would be in order to reach the targets that are desired.

Senator PROXMIRE. A footnote in this paper says that it is assumed that the spending ceiling and revenue floor in the second concurrent resolution are consistent with the fiscal stimulus needed for the economy to grow at a rate of 4.8 percent in fiscal 1978.

I would like to discuss the validity of that assumption. I know in our midyear report, the Joint Economic Committee forecasts a rate of 4 to 4.5 percent assuming spending levels in the second concurrent resolution.

It now appears that actual spending will be below the level of the second resolution. This causes me to question the validity of your basic assumption.

First, you regard your basic assumption as a reasonable one; would you forecast real growth at 4.8 percent next year?

Mrs. RIVLIN. For 1978?

Senator PROXMIRE. That is right.

Mrs. RIVLIN. Yes. We still think it is within a realistic range, the "not improbable" range.

Senator PROXMIRE. It is pretty high compared to the other forecasts. Mr. Burns told us 4.5 percent; the consensus of forecasts seems to be around 4.5 percent, in the higher range at least.

Mrs. RIVLIN. That is correct. And the signals that the economy are giving right now can only be described as mixed. The last few weeks have been a little bit stronger on some fronts than was thought, and I think until we see the end of the year's statistics and what is happening early in 1978, it would be very difficult to say whether this is realistic or not.

Senator PROXMIRE. If the economy moves to be much weaker next year, what impact will this have on your budget projections, and economic stimulus needed to reach the 4.5-percent unemployment target by 1983?

Mrs. RIVLIN. If the economy proves weaker, more stimulus will be needed over the whole period to reach those goals.

Senator PROXMIRE. Now, President Carter has indicated he will ask for a substantial tax reduction early next year. This might become effective on July 1, and it would, therefore, have some impact in 1978 and 1979.

Do you consider a tax reduction desirable?

Mrs. RIVLIN. A tax reduction is clearly one way to provide more stimulus if you think more stimulus is needed.

Senator PROXMIRE. It's one way; it is also a quicker way, many people feel, than the spending route. My question again is, would you view that as a desirable thing?

You simply tell me you cannot say if you feel that that is desirable.

Mrs. RIVLIN. No; I really cannot make a policy recommendation, Senator. We don't do that.

Senator PROXMIRE. Well, can you give me any notion of the effects of dividing that between consumers and businesses, supposing it all goes to consumers on the other hand, or supposing a quarter of it or a substantial portion of it, a third of it, might go to business.

What that have any effect in your view on the stimulative effect of the tax cut?

I am not asking you to recommend one or the other; I am just saying, what would the effect be?

Mrs. RIVLIN. I think we probably would have to think about that a little bit.

The most problematical part is what would be the effect on businesses, and that, of course, depends on what kind of a business tax cut it is.

The objective presumably would be to stimulate investment, and not a lot is known about how to do that through the tax system.

Increases in the investment tax credit have had some effect in the past, particularly temporary increases.

I think a corporate profits tax cut is likely to be less effective in stimulating investment than some other things that I can think of, especially an investment tax credit.

Senator PROXMIRE. How should the monetary authorities respond to a tax reduction on the assumption they wanted to make that fully effective?

Mrs. RIVLIN. Assuming that the monetary authorities and the fiscal authorities have the same goal, which is a higher growth rate for the economy, and if the economy is weakening, then one would think the same reasoning that would lead the fiscal authorities to more stimulus would lead the monetary authorities to an easier monetary policy.

Senator PROXMIRE. Would you agree that if the Chairman of the Federal Reserve Board should take the notion that inflation is more important to fight, and, therefore, have a restrictive policy, while the President of the United States and the Congress feel it is important to stimulate the economy and provide more jobs, that the two policies may well clash and result in neutralizing each other?

Mrs. RIVLIN. That is certainly possible.

Senator PROXMIRE. Now, your discussion stresses the need for additional fiscal stimulus to achieve the target of 4.5 percent unemployment by 1983.

The discussion implies that either spending increases above current policy levels or tax reductions can provide the necessary stimulus.

Do you mean to imply that it does not matter whether spending increases or taxes cut, would the impact on the deficit be the same? What about the types of spending increases or tax cut?

For example, some argue that over the long run we need more investment and tax cuts should, therefore, be directed to encourage this. If this is true surely it will affect the non-Federal demand which places such an important role in your projections.

Mrs. RIVLIN. That is certainly correct. We are deriving very general estimates here of stimulus, and we are assuming that, in the large, the effects would be the same. But it certainly makes a difference in how one carries out the stimulus.

If one is thinking, for instance, on how to achieve an optimistic level of non-Federal demand, then besides monetary policies, one might consider what tax measures would stimulate investment. A tax policy more stimulative to investment for the same amount of tax cut might be able more likely to give you an optimistic scenario.

Senator PROXMIRE. In your projections, the baseline case shows the amount of fiscal stimulus needed to reach the growth target grows from \$29 billion in 1979 to \$115 in 1983.

Mrs. RIVLIN. Right.

Senator PROXMIRE. Can you tell us the impact of this policy on full employment budget? Can you provide full employment budget sometimes on a current policy basis?

Mrs. RIVLIN. Yes; I guess we can. We can do that for the record.

[The following information was subsequently supplied for the record:]

ESTIMATES OF A CURRENT POLICY FULL EMPLOYMENT BUDGET

[By fiscal years; in billions]

	1977	1978	1979	1980	1981	1982	1983
Receipts.....	396.1	439.1	496.4	551.0	612.9	681.2	760.9
Outlays.....	403.1	456.4	494.7	531.7	570.3	614.4	663.8
Surplus.....	-7.0	-17.3	1.6	19.2	42.6	66.8	97.1

Senator PROXMIRE. Your report characterizes the growth in non-Federal demand as moderate. I note that you have a very brief discussion of a stronger non-Federal sector in an appendix.

Given the current situation with very low investment for the past several years, it seems to me you would have been justified in making a more optimistic assumption in this area.

Certainly it is not unreasonable to explore the implications of a stronger private sector over the next several years.

Why and how did you select this scenario particularly?

Mrs. RIVLIN. The moderate scenario was our major point.

Senator PROXMIRE. But why did you think that to be more realistic under all the circumstances?

Mrs. RIVLIN. It just seemed less extreme. One might reason that because investment has been lagging in this recovery, there is hope that it will pick up and be extraordinarily strong in the next several years.

On the other hand, one might reason that the factors that have been causing investment to lag, perhaps lack of confidence in the economy or other factors, would be likely to continue.

I don't know which is the more likely scenario, but we chose this moderate scenario, which is moderately optimistic, after all, and is roughly consistent with historical averages and is, therefore, a useful baseline. We then offered calculations based on a more optimistic or less optimistic scenario.

Senator PROXMIRE. On Friday, the head of the Bureau of Labor Statistics testified before this committee and he pointed out several really startling developments to me.

One was that we have had a 3.9-million increase in jobs in the last year; second that that was the biggest increase in our history by far in any year; third, that we have had the highest proportion of the American people at work than we have ever had, higher than in 1929—higher than in World War II, higher than any time—a higher proportion of the population is at work.

Now, the element that we have left out of this discussion so far is that when you talk about unemployment at 4.5 percent, you have to make an assumption of the size of the work force, and people coming into the work force, and so forth.

There have been great, great changes in the last 20 years, particularly in the last year or two in the work force.

Now, with the kind of expansion which we have had, which Mr. Shiskin called the best we have ever had, that kind of expansion, normally you would have had a sharp reduction in unemployment.

As you know, between April and November, there was no reduction at all. It has been 7 percent—6.9 to 7.1 percent.

What assumptions do you make about the work force? Do you expect it to continue to grow at the vast rate it has grown in the last year or two?

How did you determine that?

Mrs. RIVLIN. We assumed continuation of the trend toward higher participation of women over the next several years. That and a high number of teenagers—young people coming into the labor force—have certainly been some of the things that have made it difficult to lower the unemployment rate.

When the labor force is increasing, you have to create a lot more jobs just to stay even. We have projected some continuation in the increased labor force participation. By 1982 or 1983, the demographic changes caused by more young people will be running out. The baby boom will have passed.

Senator PROXMIRE. Well, that baby boom—I thought that it reached—of course, it is the World War II baby boom—I thought that passed about 10 years ago or so.

Mrs. RIVLIN. Yes, but the birth rate continued very high. The year in which it began to come down, I believe, was 1957, which was about 20 years ago. So we are about to get into a period where there are actually decreasing numbers of young people coming into the labor force.

Senator PROXMIRE. Nevertheless, you would agree that there is likely to be an increase of women coming into the work force and you assumed that in making your projections.

Mrs. RIVLIN. That is right.

Senator PROXMIRE. Can you tell me how much you assumed the labor force would grow? I understand, incidentally, that—unfortunately, they don't have a clock at the Bureau of Labor Statistics, but we may be reaching 100 million people in the work force now.

Maybe it was today, yesterday, maybe it will be next week. But they made such a fuss when we had 200 million persons, it seems to me that 100 million Americans in the work force might be a cause for throwing our hats in the air.

Mrs. RIVLIN. We can supply our assumptions on the labor force for the record.

[The following information was subsequently supplied for the record:]

Assumed civilian labor force by calendar year

	<i>Thousands</i>
1977.....	96, 571
1978.....	99, 391
1979.....	101, 705
1980.....	103, 452
1981.....	105, 046
1982.....	106, 474
1983.....	107, 849

Senator PROXMIRE. In revenue production, you note taxes have been a stable share of the gross national product.

Mrs. RIVLIN. That is right.

Senator PROXMIRE. 17.7 percent in 1957, and 18.8 percent in 1977.

Without tax reduction, it would be 21.7 percent in 1983. Suppose we hold this ratio constant at roughly 18.5 percent?

Would this alone provide the amount of stimulus which you estimate is necessary to reach your underlying growth targets or would we need to do more?

Mrs. RIVLIN. Yes; I think that provides more than enough stimulant.

Senator PROXMIRE. More than enough stimulus?

Mrs. RIVLIN. Yes.

Senator PROXMIRE. At what rate would you feel we have a stimulus that would give us no shortfall? You had \$115 billion needed for that much additional stimulus by 1983, but those were with the assumptions I take it that we have a higher percentage of income going in taxes.

Can you tell me at what level you would need any further stimulus as a level of taxes? What percentage?

Mrs. RIVLIN. We can do that calculation for the record.

Senator PROXMIRE. All right.

[The following information was subsequently supplied for the record:]

REVENUES AS A PERCENT OF GNP, ASSUMING REQUIRED STIMULUS COMES FROM TAX CUTS

[By fiscal years; in billions]

	1978	1979	1980	1981	1982	1983
Current policy revenues.....	397.0	457	519	590	668	751
Tax cuts (cumulative).....		29	51	74	101	115
Net revenues.....	397.0	428	468	516	567	636
GNP.....	2,056.6	2,273.8	2,518.6	2,782.8	3,079.2	3,386.5
Net revenues as a percent of GNP.....	19.3	18.8	18.6	18.5	18.4	18.8

Senator PROXMIRE. I see they broke your deadline in the Washington Star today, "Hill Gets Bleak Jobs, Budget Picture." You will have to change your name to "Cassandra."

No, I think you have done an excellent job, very helpful and realistic and most timely for our committee and for the Congress and for the public policy.

I think it is going to be extremely helpful having this picture.

Thank you, very much. The committee will stand adjourned.

Mrs. RIVLIN. Thank you very much.

[Whereupon, at 11:08 a.m., the committee adjourned, subject to the call of the Chair.]

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