Congressional Budget Office

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Fiscal Policy and Automatic Stabilizers

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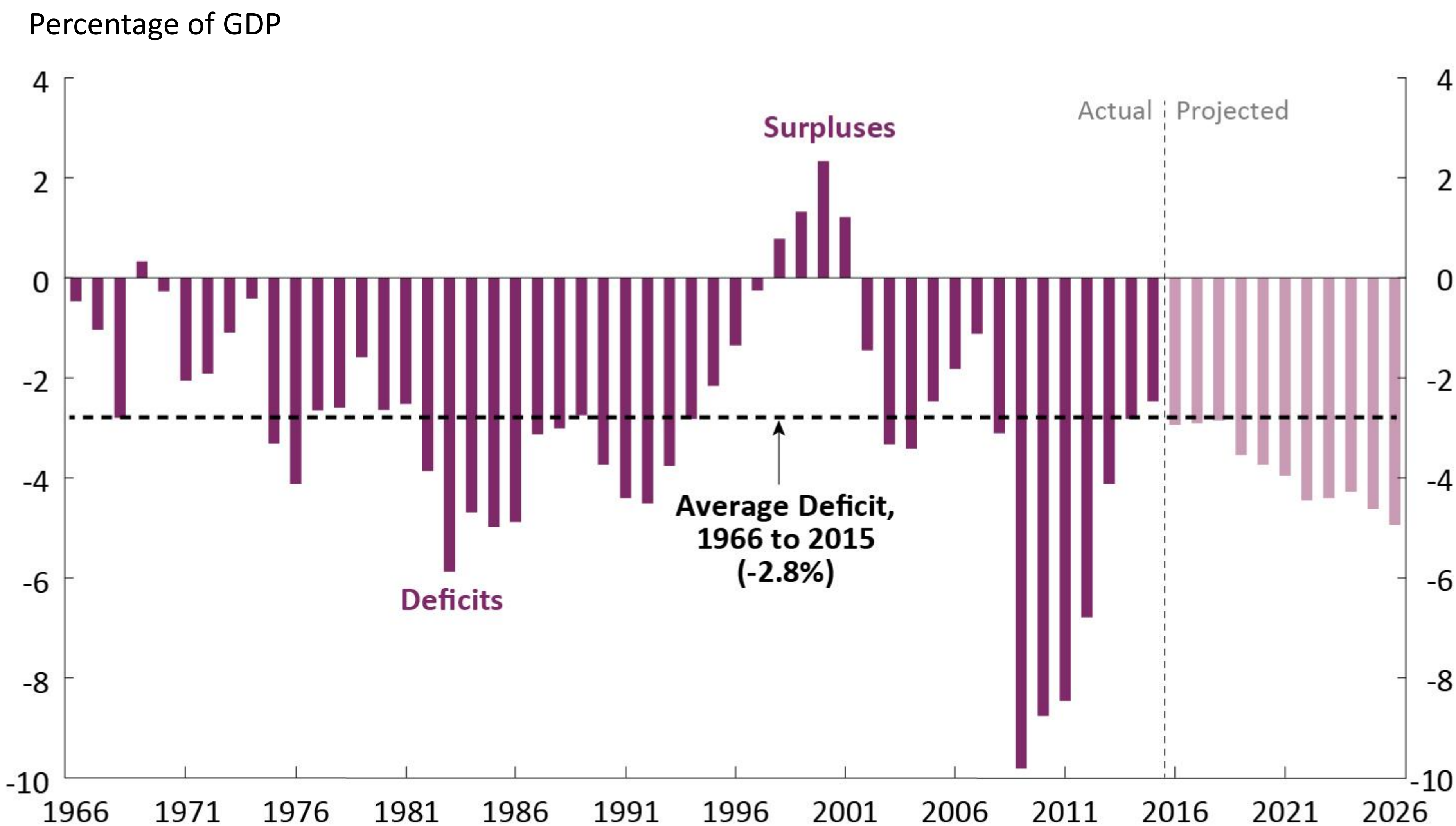
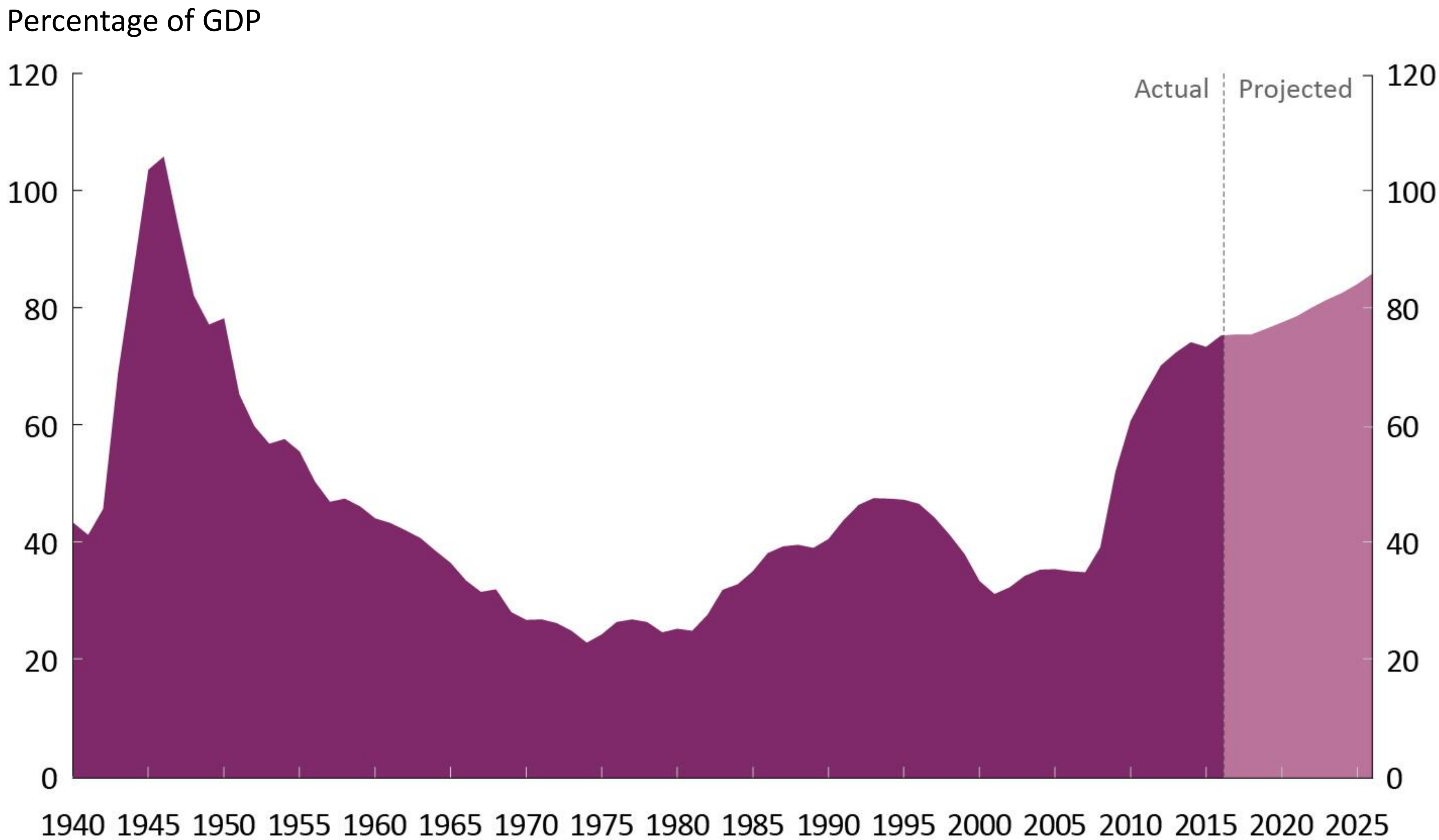
If current laws remain generally the same, growing deficits are projected to raise federal debt held by the public to 86 percent of gross domestic product (GDP) by 2026—up from 74 percent at the end of 2015 and a little more than twice the average of the past five decades.

Total Deficits or Surpluses



Federal Debt Held by the Public



High and rising debt has a number of consequences:

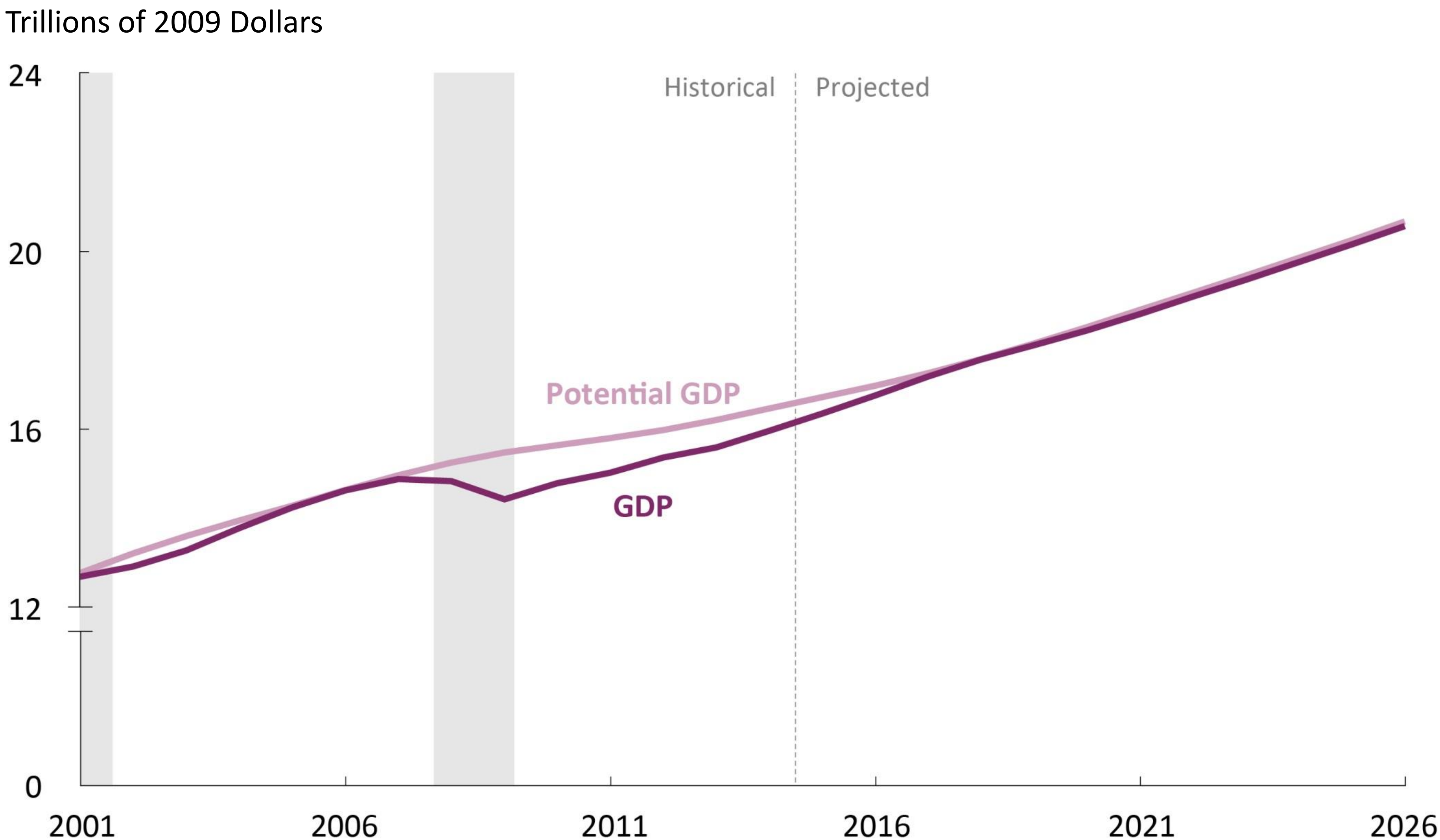
- Lawmakers would have less flexibility to use tax and spending policies to respond to unexpected challenges.
- Federal spending on interest payments would rise substantially when interest rates increased from their current levels to more typical ones.
- The likelihood of a fiscal crisis in the United States would increase.

- Because federal borrowing reduces total saving in the economy over time, the nation’s capital stock would ultimately be smaller than it would be if debt was smaller, and productivity and total wages would be lower.

- There would be a greater risk that investors would become unwilling to finance the government’s borrowing needs unless they were compensated with very high interest rates; if that happened, interest rates on federal debt would rise suddenly and sharply.

Over the next few years, CBO anticipates a near elimination of slack in the economy, as evidenced by the closing gap between GDP and potential GDP.

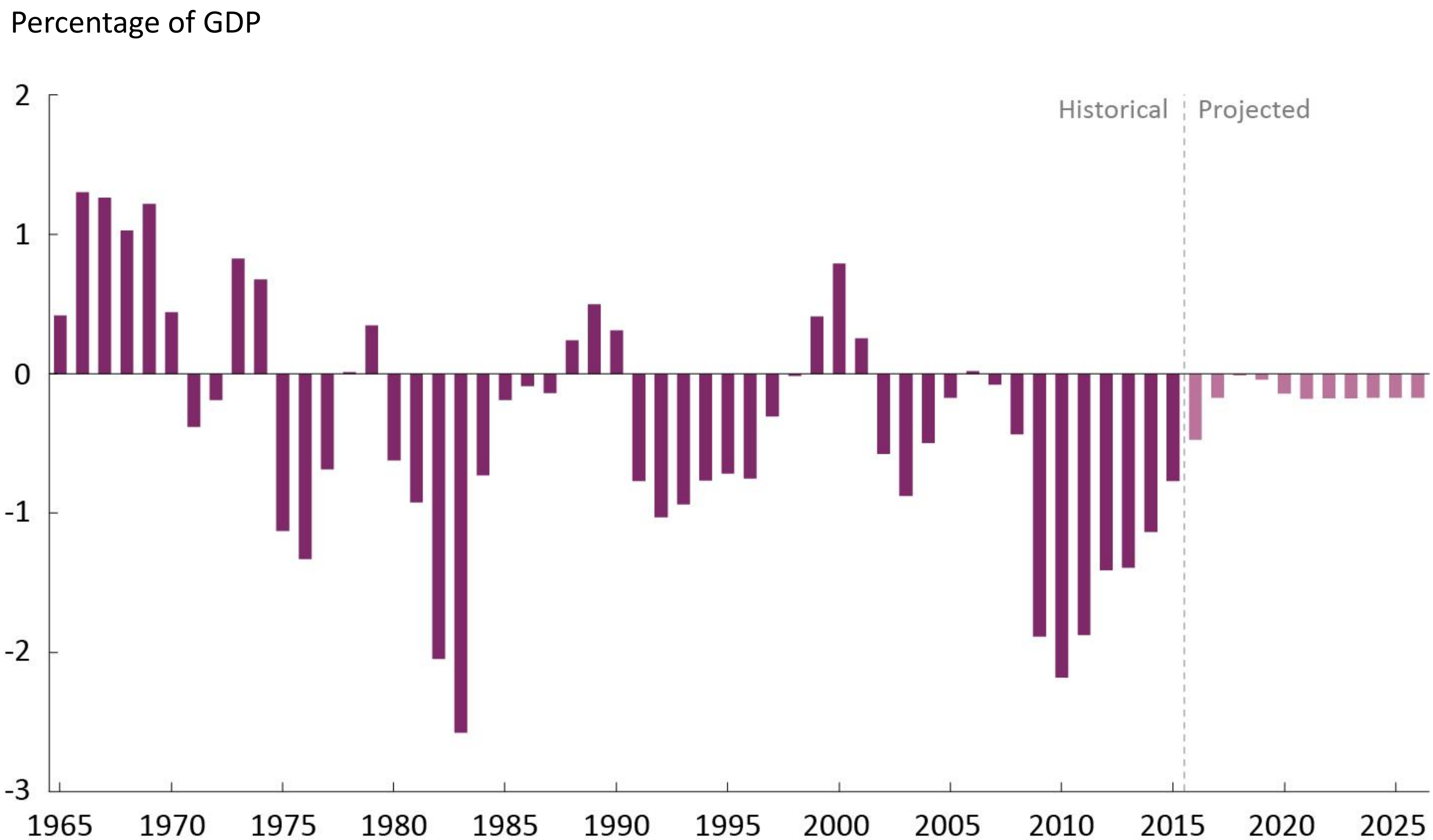
GDP and Potential GDP



CBO expects that automatic stabilizers will provide less economic stimulus over the next few years.

Automatic stabilizers are the automatic increases in revenues and decreases in outlays in the federal budget that occur when the economy strengthens, and the opposite changes that occur when the economy weakens.

Contribution of Automatic Stabilizers to Budget Deficits and Surpluses

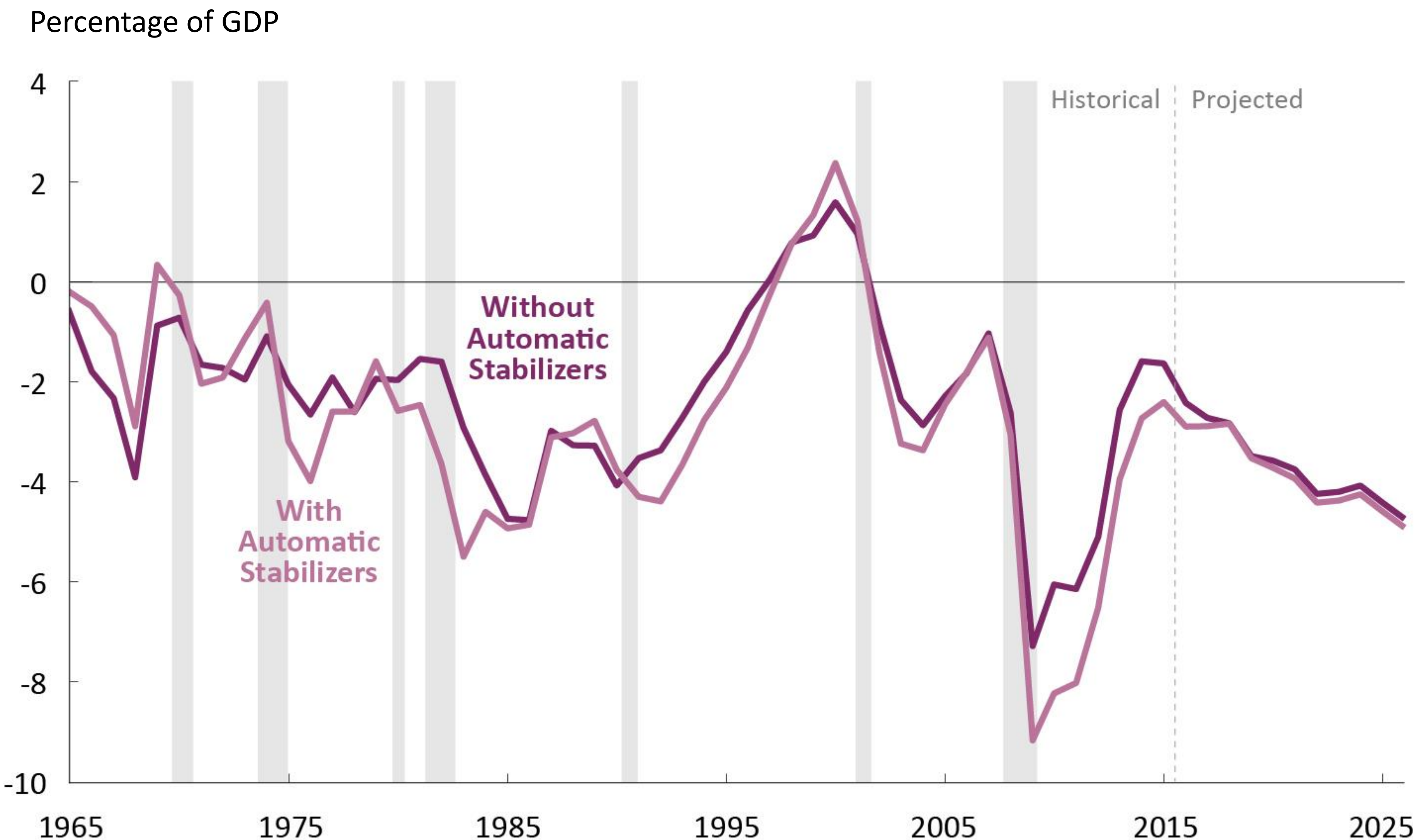


Contribution of Automatic Stabilizers to the Deficit as a Share of Potential GDP

Percent

Beginning of Recession	After Four Quarters	After Eight Quarters
1969, Fourth Quarter	1.4	1.1
1973, Fourth Quarter	1.9	2.6
1980, First Quarter	0.5	1.8
1981, Third Quarter	1.6	1.1
1990, Third Quarter	1.1	1.0
2001, First Quarter	0.9	1.3
2007, Fourth Quarter	1.2	2.1

Budget Deficits and Surpluses With and Without Automatic Stabilizers



For more information, see:

Congressional Budget Office, *The Budget and Economic Outlook: 2016 to 2026* (January 2016), www.cbo.gov/publication/49892.

Frank Russek and Kim Kowalewski, *How CBO Estimates Automatic Stabilizers*, Working Paper 2015-07 (Congressional Budget Office, November 2015), www.cbo.gov/publication/51005.