Insight

A Little Extra Growth Goes a Long Way

GORDON GRAY | FEBRUARY 3, 2015

The president's FY2016 Budget includes a host of proposals, some good, some bad, some ugly. Setting aside the individual policies, the budget, as estimated by the Office of Management and Budget (OMB), purports to put debt held by the public on a downward path as a share of the economy. This estimate is the set of economic assumptions that underpin the spending and revenue outlook in the president's budget. Compared to the Congressional Budget Office's (CBO) economic outlook, real economic growth averages 0.2 percentage points higher under OMB's assumptions. This is not a wildly rosy outlook – 2.5 percent real growth is nothing to cheer over. But for the budget numbers, a little growth goes a long way.

According to the CBO, if GDP is 0.1 percentage points lower per year, it has a $326 negative effect on the deficit. That is, because of lower incomes, employment, and other factors, tax revenue would be $288 less. Slower growth would have a small effect on mandatory spending, but the revenue shortfall would require more borrowing. These add up to $326 billion budget hole from just 0.1 percentage points of slower growth. Using this "rule of thumb," OMB's 0.2 percentage point growth advantage banks $652 billion in deficit savings. Adjusting OMB's debt numbers by this amount, and plotting them as a share of CBO's GDP numbers reveals a different tale than that being told by OMB.

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With just this adjustment, the president's budget essentially keeps the debt locked in at 75 percent of GDP for the next decade.