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Special Series: **Economic Recovery Watch**

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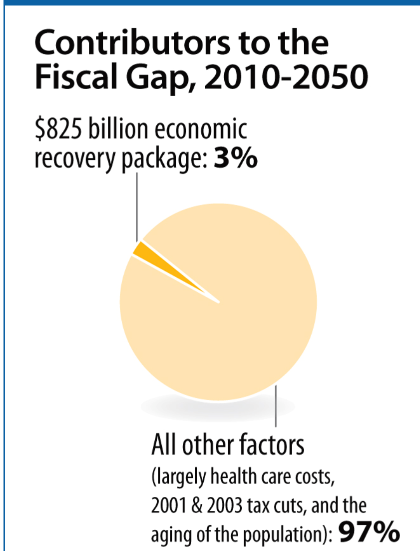
ECONOMIC RECOVERY BILL WOULD ADD LITTLE TO LONG-RUN FISCAL PROBLEM

By Paul Van de Water and Kris Cox

The $825 billion economic recovery package offered by congressional leaders will have only a very small impact on the nation's long-term fiscal problem, adding just 3 percent to the budget shortfall through 2050.

While the package aims to put millions of unemployed Americans back to work, some question whether the nation can afford to add such a large amount to government debt in the face of the bleak long-term fiscal outlook. Because the economic recovery measures would be temporary, however, they would have little effect on the long-run deficit problem. Even without the proposed recovery legislation, 97 percent of the projected long-term fiscal shortfall would still remain.

FIGURE 1:
Proposed Recovery Package is Small Share of Projected Long-Term Budget Shortfall



Source: CBPP calculations based on CBO data.

In December the Center on Budget and Policy Priorities released new projections of federal spending, revenues, deficits, and debt through 2050.[1] Those projections showed that without changes in policies, federal deficits and debt in coming decades will grow to unprecedented levels and threaten serious harm to the economy. Updating the projections to incorporate the proposed $825 billion recovery package yields two key findings.

First, the estimated long-term fiscal gap amounts to 4.3 percent of projected gross domestic product (GDP) through 2050. The fiscal gap offers a convenient way of summarizing the long-term budget outlook in a single number; it is the average amount of program reductions or revenue increases that

[1] Richard Kogan, Kris Cox, and James Horney, *The Long-Term Fiscal Outlook is Bleak: Restoring Fiscal Sustainability Will Require Major Changes to Programs, Revenues, and the Nation's Health Care System*, Center on Budget and Policy Priorities, December 16, 2008.

would be needed over the next four decades to ensure that the debt is no larger in 2050 than it will be at the end of 2009, measured as a share of the economy. This means that stabilizing the nation's finances through 2050 would require some combination of tax increases and spending cuts averaging 4.3 percent of GDP per year, a very large amount.

Second, the proposed $825 billion economic recovery package accounts for only 0.1 percentage point of the 4.3 percent long-term fiscal gap. Thus, even if the economic recovery legislation were not enacted, virtually all of the problem would still exist.

The fiscal gap is overwhelmingly the result of other factors — primarily the rapid growth in health care costs, the aging of the population, and the expensive tax cuts enacted in 2001 and 2003. Unlike the recovery proposals, whose costs largely disappear after a few years, these ongoing factors add to the deficit by continually increasing amounts each year. For example, making the 2001 and 2003 tax cuts permanent without offsetting their cost adds over 15 times as much to the long-term fiscal problem as the economic recovery package. Temporary costs — even if very large in the short run — contribute much less to the fiscal gap than permanent costs, because their costs are small relative to the size of the economy over several decades.

At this moment, the economy requires substantial fiscal stimulus to increase aggregate demand and avert a deep and prolonged recession — even if deficits exceed $1 trillion this year and next. As the economy recovers, however, policymakers should begin to implement a balanced approach to deficit reduction through reforming the health care system, slowing the growth of federal expenditures, and increasing federal tax revenues.