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CBO’s Analysis of Fiscal Policy Options

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Key Criteria for Effective Fiscal Stimulus

- **Timing**: providing help when it is needed most.

- **Cost-effectiveness**: providing the most growth and employment per dollar cost to the federal budget.

- **Consistency with long-term fiscal objectives**: preventing the short-term deficit increase due to stimulative policy from adding excessively to federal debt in the long run.
Estimated Budgetary Effects of the American Recovery and Reinvestment Act (ARRA)

Billions of Dollars

- Total Effect on the Deficit
- Revenues
- Mandatory Outlays
- Discretionary Outlays

Years:
- 2009
- 2010
- 2011
- 2012
- 2013
- 2014
- 2015
Quantifying Short-Term Effects

- **Multipliers**: quantifies the estimated direct and indirect effects on the nation’s output of a dollar’s worth of a given policy.

- **Labor market effects**: estimates of ARRA’s effects on output were translated into estimates of the effects on the unemployment rate, total employment, and FTE employment.
Estimated Output Multipliers of Major Provisions of ARRA, Range of Low to High Estimates

- Corporate Tax Provisions Primarily Affecting Cash Flow
- Extension of First-Time Homebuyer Credit
- One-Year Tax Cut for Higher-Income People
- Two-Year Tax Cuts for Lower- and Middle-Income People
- One-Time Payments to Retirees
- Transfer Payments to State and Local Governments for Infrastructure
- Transfer Payments to State and Local Governments for Other Purposes
- Transfer Payments to Individuals
- Purchases of Goods and Services by the Federal Government

Change in GDP Attributable to ARRA

Change in Employment Attributable to ARRA

Cumulative Effects of Policy Options on Employment in 2010 and 2011, Range of Low to High Estimates


Note: Assumes enactment in early 2010.
Effects of Four Tax Policy Options on Real GNP in 2011 and 2012, Range of Low to High Estimates

Source: CBO’s September 2010 testimony, The Economic Outlook and Fiscal Policy Choices.
Quantifying Longer-Term Economic Effects

- **Textbook Growth Model**: Assumes that people do not consider expected future policies when they make economic decisions.

- **Life-Cycle Model**: Assumes that people adjust their decisions about work and saving in response to current changes in marginal tax rates, government transfer payments, and after-tax rates of return—and in anticipation of future changes in those factors.
Effects of Four Tax Policy Options on Real GNP in 2020

Source: CBO’s September 2010 testimony, The Economic Outlook and Fiscal Policy Choices.
CBO compared the effects of implementing policies that would halt the growth in federal debt as a percentage of GDP starting in 2015 with the effects of policies that would delay stabilizing the ratio of debt to output until 2025.

The analysis considers three illustrative policy changes: cutting federal benefit payments for all adults, cutting benefit payments for all adults except those who are age 60 or older at the time of the change, and raising tax rates on income from labor and capital.

The budgetary and economic consequences of delay would affect people’s well-being, and those effects would differ for different generations.
Effect on Output If the Ratio of Debt to Output is Stabilized in 2025 Instead of 2015, Under Three Illustrative Policies

Percentage Change

-6 -5 -4 -3 -2 -1 0 1 2 3

Source: CBO's December 2010 Issue Brief, Economic Impacts of Waiting to Resolve the Long-Term Budget Imbalance.