

“Forecasters Predict Drop in Deficit”

Associated Press, August 15, 2005

Last month, we reported that surging federal tax receipts were beginning to close the budget deficit. Stronger corporate profits and an economy that continues to grow in spite of every conceivable worry by hand-wringing economists have saved the government from its own fiscal looseness. Now, a new report from the Congressional Budget Office confirms earlier reports by the Treasury. The deficit is shrinking, and at a faster rate than originally thought:

“The federal budget-deficit picture turned brighter Monday as congressional scorekeepers released new estimates showing the level of red ink for the current fiscal year would drop to \$331 billion.[Even lower than the \$333 B estimated by the Treasury - Charles]

“The new report by the nonpartisan Congressional Budget Office, which does budget analysis for lawmakers in Washington, gave the latest proof that surging revenues and a steadily growing economy are combining to bring the deficit down from a record \$412 billion posted last year. CBO predicts a \$314 billion deficit for the budget year starting Oct. 1.”

The improved budget picture does not excuse wasteful spending, of course, but it is important to keep things in perspective. While the deficit still remains enormous, it is near its historical range as a percentage of GDP:

“Last year's deficit was a record in dollar terms, though many previous deficits in the mid-1980s and early 1990s were larger when measured against the size of the economy. The White House and most economists say that the more relevant measure of the deficit is to weigh it against the size of the economy. Measured that way, the latest estimates for this year are slightly worse than recent historic averages.”

Complete article: http://biz.yahoo.com/ap/050815/budget_deficit.html?.v=4

Even if the deficit were to remain at its current level, we could anticipate its decline as a percentage of GDP as our economic boom continues to gain speed. Still, to reverse the cliché, every silver lining has its cloud. The longer term budget picture does not look good. Democrats raised the relevant point that the Boomers would be retiring soon in large numbers, removing a large chunk of those taxpayers in the highest brackets.

As always, Japan has proven to be a good test case. Due primarily to aging demographics, Japan languished throughout the 1990s, and consumer demand was nowhere to be found. The economy stagnated, failing to grow GDP by any meaningful amount, while government spending rose aggressively. By 2002, Japan's sovereign credit rating had fallen below that of Botswana.

Bottom line? Enjoy the coming years of healthy government finances, but don't get too attached. If Japan is any indicator, then the good times won't last much beyond 2010.

