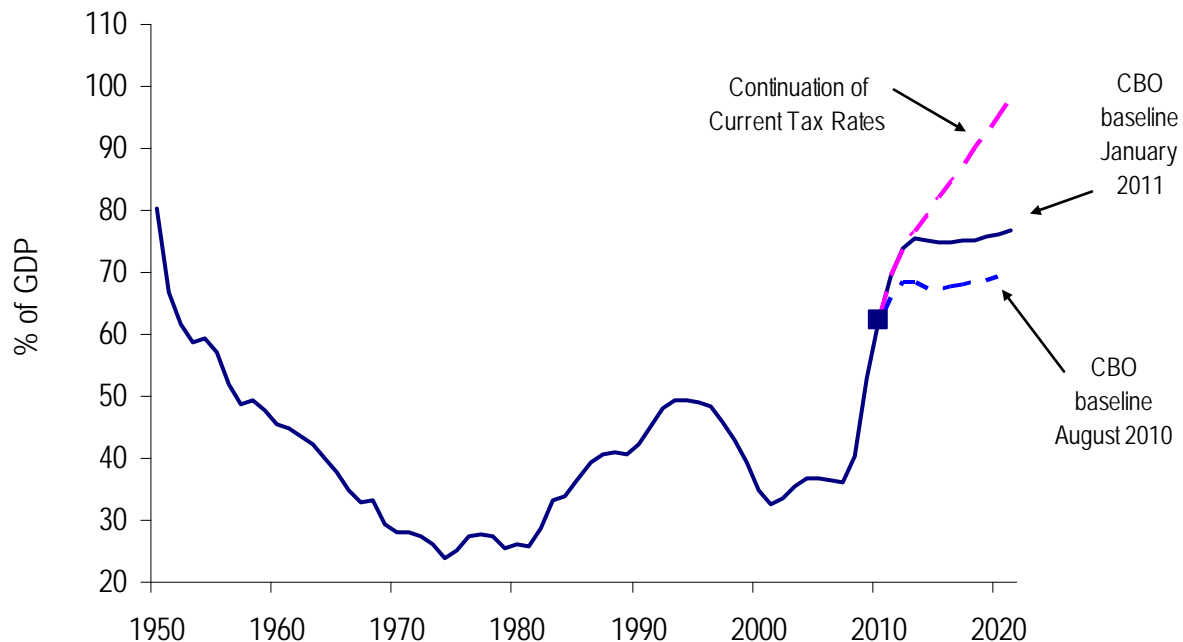


# Reaching the Limits of Washington's Debt Expansion

CBO just released its January 2011 economic and budget outlook. It's the first look at the deficit since the December lame-duck spending blow-out.

- Assuming continuation of current tax rates beyond 2012 (which CBO projects will add \$5.5 trillion in debt to the baseline), the **marketable national debt will rise to \$24 trillion in 2021, 100% of GDP**. At that point, the statutory debt limit, now \$14.3 trillion, would be \$31 trillion (page 125 in the CBO report plus the tax extenders on page 22). These debt figures are based on CBO's optimistic assumptions -- economic growth speeds up to an average 3.4% in 2013-2016, no deep recessions, discretionary spending grows slower than inflation and interest rates on the national debt stay relatively low.
- We think the U.S. fiscal situation is deteriorating rapidly enough that it is a key variable in the global economic outlook, with no sign in Washington of a legislative strategy to improve the fiscal course. In importance, we place the U.S. fiscal crisis on a par with growth, profits and innovation, and above the concerns about Europe's debt and banking problems and China's overheating.

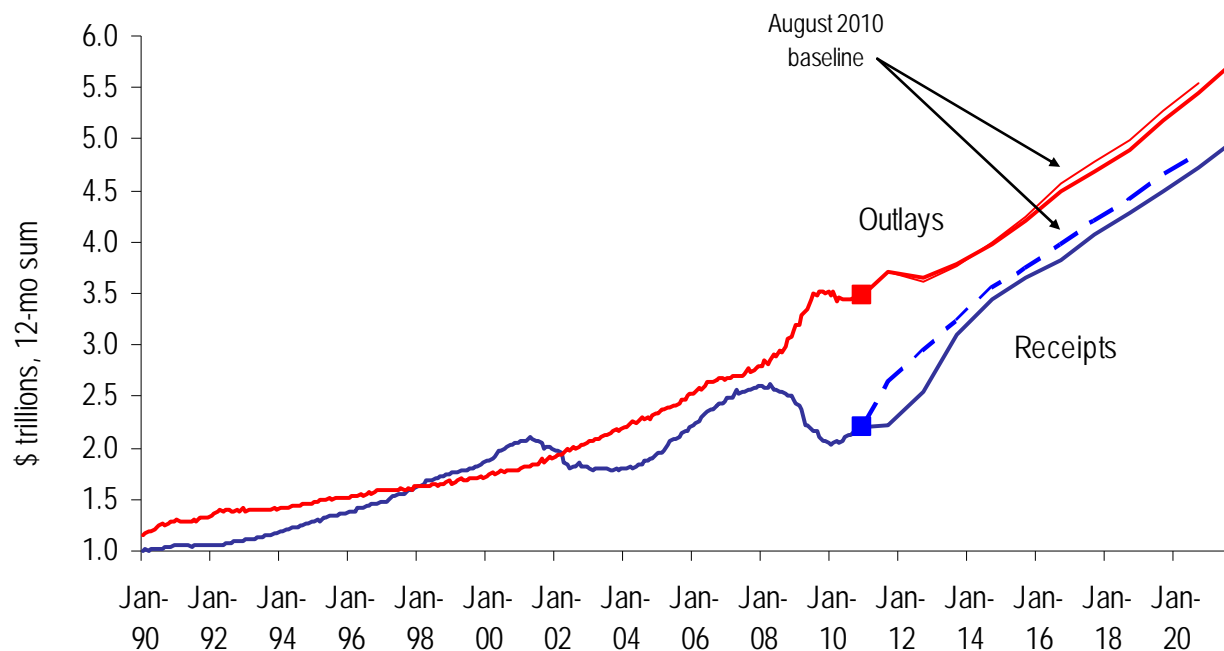
## Federal Debt / GDP (last obs. 2010, CBO projected to 2021)



Source: CBO; Encima Global

- The current marketable debt is \$9 trillion (62% of GDP). Under CBO's baseline, it would rise to \$18.3 trillion in 2021, 77% of GDP (page 20 of the CBO report). These baseline estimates assume that tax rates go up sharply in 2013 without any impact on growth. There would be an additional \$5.5 trillion increase in the national debt if current tax rates are extended again in December 2012 as they were in December 2010, pushing the debt-to-GDP ratio nearly 100% of the expected \$24 trillion GDP in 2021 (CBO page 128). Most tax rates, like the AMT patch, will have to be extended, so we think \$24 trillion and 100% of GDP are the more likely forecasts of current policy. Statutory debt would be 130% of GDP (\$31T/\$23.8T).
- In its new outlook, CBO increased its deficit projections for 2011 to \$1.5 trillion from \$1.1 trillion and for 2012 to \$1.1 trillion from \$700 billion. Under its baseline scenario (higher tax rates, no impact on economic growth), the 10-year deficit and increment in marketable national debt is \$7.7 trillion, up from \$6.2 trillion in CBO's August 2010 outlook.

### Federal Receipts and Outlays (last obs. December 2010, CBO projected to 2021)



Source: CBO; US Treasury; Encima Global

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