The Federal Government’s Long-Term Fiscal Outlook
Fall 2010 Update

GAO’s annual fall update of its long-term simulations underscores the need to address the long-term sustainability of the federal government’s fiscal policies. While the economy is still fragile and in need of careful attention, there is wide agreement on the need to look not only at the near-term but also at steps that begin to change the long-term fiscal path as soon as possible without slowing the recovery. With the passage of time the window to address the long-term challenge narrows and the magnitude of the required changes grows. The federal government faces long-term fiscal pressures that predate the economic downturn and are driven on the spending side largely by rising health care costs and an aging population. GAO’s simulations show continually increasing levels of debt that are unsustainable over the long-term (see fig. 1). Under the Alternative simulation, debt held by the public as a share of GDP would exceed the historical high reached in the aftermath of World War II by 2020.

Both of these simulations incorporate effects of health care legislation enacted in March 2010, which includes a number of provisions to control the growth of federal health care spending.1 There is a notable improvement in the long-term outlook under the Baseline Extended simulation, which assumes full implementation and effectiveness of cost control provisions, although

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In the “Alternative” simulation, all tax provisions are extended to 2020 and the alternative minimum tax (AMT) exemption amount is indexed to inflation through 2020; revenues are then brought back to the historical average as a share of GDP; discretionary spending grows with GDP during the entire period—keeping it just below the 40-year historical average as a share of GDP; Medicare physician payment rates are not reduced as in CBO’s baseline.

The two different sets of projections for Social Security and the major health entitlement programs are as follows: For Baseline Extended GAO uses (i) the Social Security and Medicare Trustees’ intermediate projections from their most recent report issued in August and (ii) the CBO projections that are closest to current law and CBO’s cost estimates for the recently enacted health care legislation. For the Alternative, projections for the major health entitlement programs are based on: (i) The CMS Actuary’s alternative projections, which assume that the full cost containment in the health care legislation is not sustained and (ii) the CBO alternative which assumed some of the policies intended to restrain growth in health care spending would not continue after 2020. At this point the spending effects of the cost containment mechanisms are unknown.

GAO also calculates the Fiscal Gap—the size of action that must be taken to stabilize debt at the current share of GDP.

These long-term simulations show that absent additional policy actions the federal government faces unsustainable growth in debt. Health care legislation enacted earlier this year has the potential to slow the growth of federal health care spending. However, even under the more optimistic Baseline Extended scenario, which assumes the full implementation and effectiveness of cost control provisions, debt grows continuously over the long term indicating that more needs to be done. As policymakers consider both the current economic weakness and any recommendations put forth by the National Commission on Fiscal Responsibility and Reform and other policy groups, it is clear that over the long term historical levels of spending and revenue cannot be maintained going forward.