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Macro Roundup Article

Headline: The Long-Term Budget Outlook Under Alternative Scenarios for the Economy and the Budget

Article Link: https://www.cbo.gov/system/files/2024-05/60169-scenarios.pdf

Author(s)	Daniel Crown and Aaron Betz
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Tweet: A new @USCBO analysis argues rising government debt may drive significant crowding out going forward: "In CBO's assessment, every additional dollar of deficit-financed spending reduces private investment by 33 cents."

Summary: Under the [“If sensitivity of private investment to deficits differed: Greater sensitivity”] scenario, in which debt held by the public exceeds 250% of GDP beginning in 2051, private investment would be smaller than projected in CBO’s extended baseline. The reduction in private investment would, over time, lower the stock of private capital and reduce output. Lower economic output would reduce federal revenues and lead to even larger deficits as the effect on private investment compounded. Reductions in private investment would also decrease the amount of capital used by each worker, thereby increasing the return on capital and the return on investments (including government bonds). In CBO’s assessment, that greater sensitivity of private investment to deficits would increase the average interest rate on federal debt in 2051 by 2pp in relation to the agency’s extended baseline. Real GNP per person would be 18% (or $21,300) lower in that year than it is in CBO’s extended baseline. Under the second scenario, private investment would be larger than projected in CBO’s extended baseline. The increase in private investment would, over time, boost the stock of private capital and output. It would also increase the amount of capital used by each worker, thereby reducing the return on capital and the return on investments (including government bonds). In CBO’s assessment, the reduced sensitivity of private investment to deficits would lower the average interest rate on federal debt by 0.7pp in 2054 in relation to the agency’s extended baseline. Real GNP per person under that scenario would be 7% (or $8,700) higher in that year than it is in CBO’s extended baseline.

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