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The Upshot

EVERYDAY ECONOMICS

The Federal Budget Deficit Is Back to Normal

OCT. 10, 2014

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The federal budget deficit has narrowed sharply, and is back to relatively normal levels.

With the government's budget year having concluded at the end of September, the Congressional Budget Office now estimates that the deficit for 2014 was 2.8 percent of G.D.P., down from 4.1 percent last year. The deficit is now smaller than its average over the past 40 years of 3.1 percent.

The size and speed of the decline has come as a surprise to many forecasters. As recently as February 2013, this year's deficit was expected to be 3.7 percent of G.D.P. The deficit has declined in each of the past five years, and is now markedly smaller than the deficit (9.8 percent) registered in the 2008-09 fiscal year.

As the economic recovery continues, the deficit is expected to narrow even further next year. Based on current projections, the average deficit through President Obama's second term will be smaller than it was through President Reagan's second term.

These latest deficit numbers arrive while voters claim to be highly engaged by the federal budget. A recent Gallup poll shows that 73 percent of registered voters say that the federal budget deficit is either "very important" or "extremely important" to their vote for in next month's midterm elections, and the share is even higher among Republican voters.

How then should voters parse these latest numbers? The federal deficit reflects the confluence of two separate factors: the current tax-and-spending policies and the strength of the business cycle. A weak economy both reduces tax revenues and raises government spending. For this reason, economists who are trying to evaluate what the deficit would be if economic conditions were normal refer to the "cyclically adjusted budget balance," which strips out the effects of the economy's ups and downs.

It's a nice idea in theory, but in practice, a complete accounting of the factors that have narrowed the deficit is not possible. Even so, we can see something by juxtaposing two simple facts. It is surely the case that the economy is operating further below its capacity than it has, on average, over the past 40 years. And the budget deficit is also below its average over the same period. It follows then that any cyclically adjusted measure of the budget shows that fiscal policy is substantially tighter than its long-run average.

The harder question is not whether fiscal policy is relatively tight — it is — but rather whether tight fiscal policy is appropriate.

For those who are concerned about government debt, smaller deficits are surely a good thing. And indeed, because deficits are expected to remain relatively small, total public debt as a share of the economy's total output is projected to be roughly stable over the next decade. It is only over subsequent decades that the debt is projected to rise, although any economic forecast made decades in advance comes with a sufficiently wide margin of error that there's also a good chance that it also may fall.

But if your major concern is the state of the economy, you're probably disappointed by recent fiscal policy. After all, the usual textbook prescription is to spend more and tax less to try to support economic recovery. While the initial Obama stimulus probably boosted the economy, its subsequent withdrawal has held the recovery back over recent years. By this view, fiscal tightening before the economy has fully recovered is part of the reason the jobless rate has remained too high, for too long.

In terms of political implications, the Democrats may try to use the shrinking budget deficit as an argument to try to win support from fiscally conservative Republicans. But the reality of recent budget numbers is unlikely to win them much, because it stands so starkly at odds with the broader public perception that the deficit remains much larger than it really is.

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