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PUTTING US FISCAL POLICY ON A SUSTAINABLE PATH

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ABSTRACT

Even allowing for substantial uncertainty regarding projections, current US fiscal policies are almost certainly unsustainable. Therefore, policymakers must decide when and in what ways to change policies. Changing policies sooner rather than later would put debt on a lower trajectory and thereby increase national savings and provide insurance against adverse developments by expanding fiscal space, protecting against a persistent shortfall in economic growth, and reducing the chance of a fiscal crisis. Yet, the probability of a near-term fiscal crisis is difficult to assess: Yields on Treasury debt are within their range of the past few decades, which suggests that investors are not that worried about the fiscal outlook—but debt and deficits are at nearly unprecedented levels, and experience shows that investors' confidence in a government's fiscal management can deteriorate quickly.

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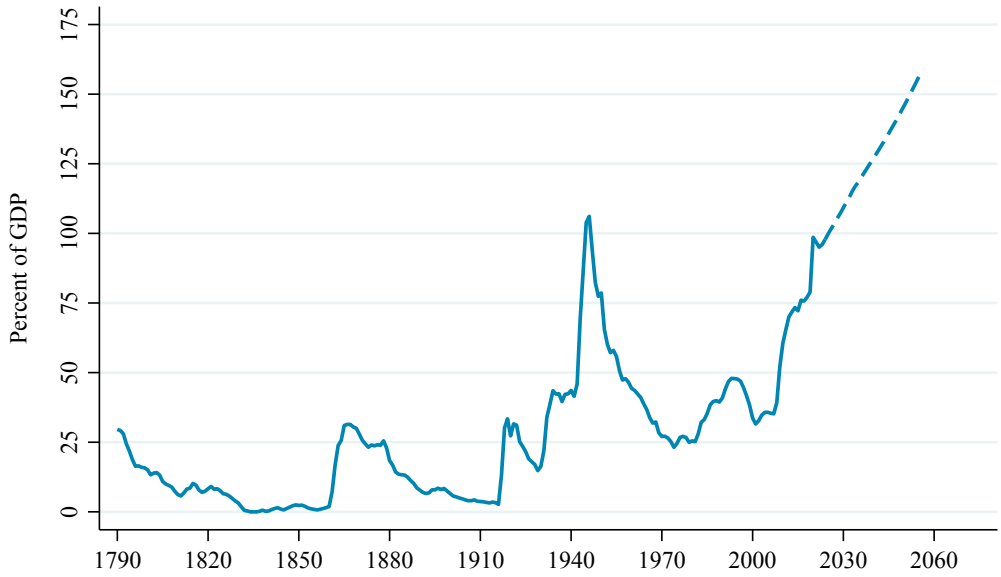
The US government's publicly held debt is now roughly equal to the country's annual output, a mark that has been exceeded only for a few years around the end of World War II and that is nearly three times the level in 2007 on the eve of the global financial crisis (as shown in figure 1). The Congressional Budget Office (CBO 2025c) projects that, under current law, debt will rise rapidly relative to output in the years ahead. Moreover, that projection understates the debt that would be incurred under a continuation of current *policies*, in particular because current law includes the upcoming expiration of tax cuts enacted in 2017. The United States has never experienced a significant rise in federal debt relative to output apart from major wars, recessions, and (on a much smaller scale) the 1980s, so the country is headed for new territory in both the level and trajectory of debt.[1]

Figure 1
Federal Debt



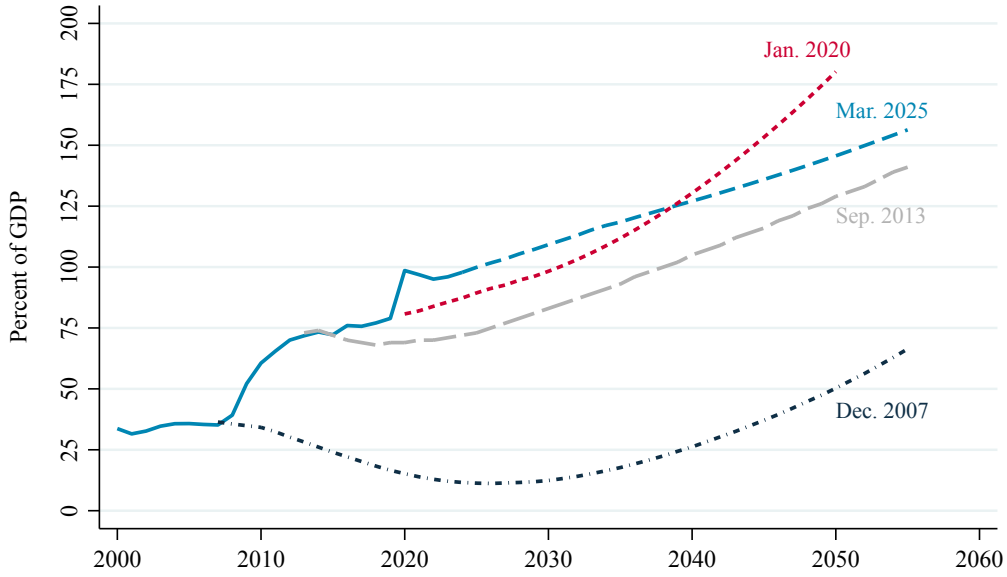
Source: Supplementary data files for Congressional Budget Office *Long-Term Budget Outlook* documents (Jan. 2020, Jan. 2025, and March 2025).
Note: Solid line is history; dashed line is projection under current law as of March 2025.

[1] Federal debt held by the public includes debt held by the Federal Reserve, and a more comprehensive measure of the federal government's financial position would consolidate the Federal Reserve's balance sheet and add other federal liabilities and assets. However, making those adjustments would not alter our main points. More generally, although debt is just one of many commitments made by the federal government, it has a special role legally, financially, and in people's perceptions; many federal commitments beyond the current debt (such as future Social Security payments) are reflected in the debt projections we discuss. We focus exclusively on the federal budget, although the budgets of many state and local governments also face large challenges.

Some parts of this story have been well-known for decades. The aging of the population and rapid growth in health care spending have made the largest federal programs increasingly expensive relative to output over time and will continue to do so. Meanwhile federal revenues have shown no trend relative to output over the past half-century, as legislated tax cuts have offset the tendency of a progressive tax code to raise more revenue when incomes rise.

But other parts of the story are newer. The projected path of debt is notably higher today than was projected under current law in 2007 (as shown in figure 2). That upward shift occurred not because aging and health care spending have had larger effects than expected; indeed, health care spending has risen less than projected in 2007 and accounts for some of the downward pivot in projected debt growth between 2020 and 2025. Instead, the jump owes to large tax cuts—in 2012 (making permanent most of the tax cuts enacted on a temporary basis in 2001 and 2003) and in 2017—and two major recessions and the policy responses to them.[2]

Figure 2
Vintages of Federal Debt Projections



Source: Supplementary data files for Congressional Budget Office *Long-Term Budget Outlook* documents (Dec. 2007, Sep. 2013, Jan. 2020, Jan. 2025, and March 2025).
Note: Solid line is history; dotted and dashed lines are projections under then-current law.

[2] For further discussion of revisions to the budget outlook over time, see Dynan (2023).

We explain in the next section that, even allowing for substantial uncertainty regarding projections, current US fiscal policies are almost certainly unsustainable. Therefore, the key questions for policymakers are *when* and *in what ways* policies might be changed. We address those questions in turn and then conclude with comments on the politics of fiscal policy. Throughout the paper, we emphasize the uncertainty of future developments.

Might Current Policies Be Sustainable Without Changes?

In CBO's (2025c) projections based on current law, ever-rising debt relative to gross domestic product (GDP) causes federal interest payments to increase continuously relative to GDP, and that dynamic is reinforced by the upward pressure on interest rates from growing debt. Projections based on current tax policies rather than current tax law would show notably faster rises in debt and interest payments. The increases in debt and interest payments shown in either set of projections cannot continue indefinitely.

Of course, budget projections are highly uncertain. To the extent that future economic conditions differ from what is expected today, future budget outcomes will differ as well. Might debt and interest payments stabilize relative to GDP without changing current laws or policies?

Assessing Sustainability

A useful starting point is a basic formula for the dynamics of debt:

Change in Debt/GDP ~= Primary Deficit/GDP + ((r-g)/(1+g))*Debt/GDP(-1),

where r is the interest rate on federal debt averaged across all outstanding securities, g is the growth rate of GDP, and the primary deficit equals spending apart from interest payments less revenue.[3] The elements of the formula are connected in multiple other ways too: The primary deficit depends on economic growth, and economic growth and interest rates both depend on the amount of debt. Not surprisingly, lower interest rates cause debt to compound more slowly, and higher GDP growth reduces debt relative to GDP. The formula highlights also that the difference between interest rates and growth rates is key to debt dynamics and that the difference is especially consequential when debt is large relative to GDP.

For many years, the federal government recorded mostly small primary deficits or surpluses, with an average primary deficit of 0.1 percent of GDP between 1962 and 2007. In addition, the average interest rate on federal debt was often lower than the growth rate

[3] The formula is only approximately correct because it omits some government financial transactions.

of GDP, with *r* averaging 0.4 percentage point less than *g* between 1962 and 2007. The result was a debt-to-GDP ratio that stayed below 50 percent of GDP between 1962 and 2007 and stood at 35 percent of GDP in 2007.

Then the situation shifted dramatically, in two countervailing ways: From 2008 through 2024, primary deficits averaged 4.6 percent of GDP, and the interest rate on federal debt averaged 1.8 percentage points less than the GDP growth rate. The former shift had a much larger effect on the debt-to-GDP ratio, which reached 98 percent in 2024.

Looking ahead, further notable shifts are expected. CBO (2025c) projected that, under current law, primary deficits will average 1.9 percent of GDP between 2030 and the mid-2050s with little trend (as shown in figure 3), and the economic growth rate will decline toward the interest rate on federal debt and ultimately fall below it (as shown in figure 4 with both rates depicted as five-year moving averages adjusted for inflation).[4] The result would be debt equal to 156 percent of GDP in 2055 and rising rapidly. Moreover, the path of debt under current *policies* would be even steeper. Estimates from CBO and the staff of the Joint Committee on Taxation (JCT) imply that extending the expiring provisions of the 2017 tax act would increase primary deficits to a little under 3 percent of GDP on average in the coming decades and would raise interest rates, putting debt in 2055 at something like 200 percent of GDP.[5]

Researchers have assessed the sustainability of fiscal policy (for the United States and other countries) in various ways. Some researchers have embedded debt dynamics in calibrated models of household, business, and government behavior and then estimated ranges of sustainable policy; for example, Mian et al. (2024) concluded that, prior to the pandemic, the United States could sustain a primary deficit just over 2 percent of GDP and debt equal to roughly 120 percent of GDP. Other researchers have focused on the uncertainty of future developments and estimated the amount of debt that would be manageable even with adverse shocks; for example, Debrun et al. (2020) estimated that,

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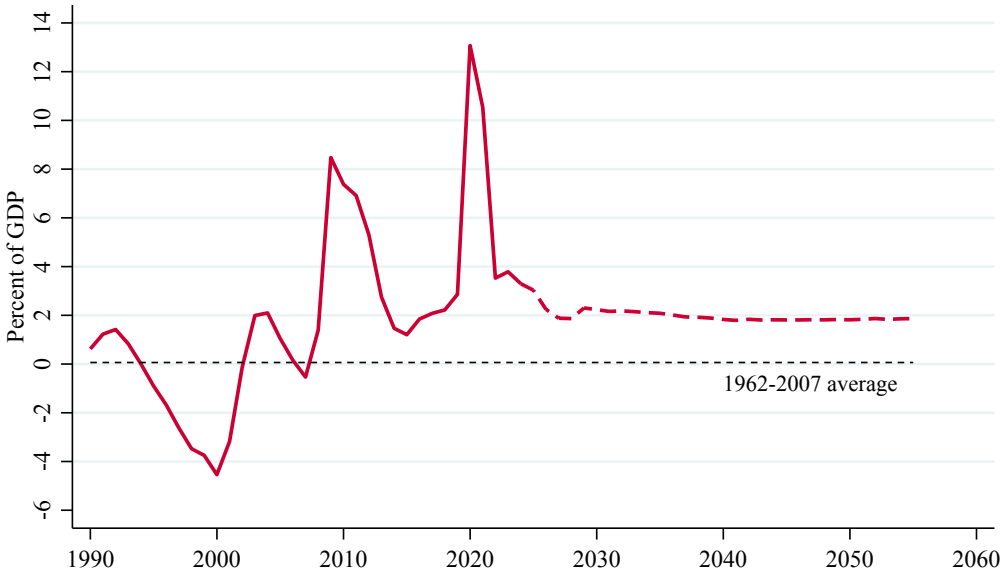
[4] The "2024" dot in figure 4 shows that the interest rate adjusted for inflation has become positive again. The five-year moving average plotted in the figure remains negative, as it is still picking up the inflation surge of the early 2020s.

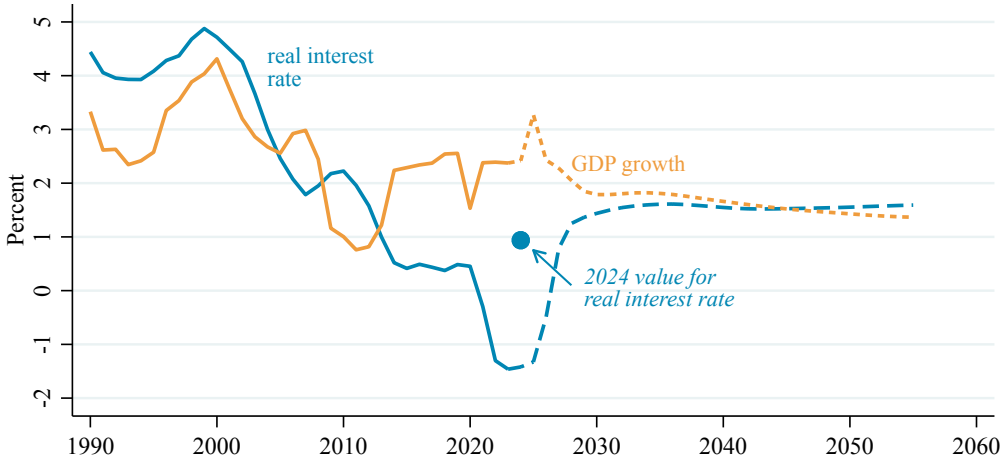
[5] According to JCT's (2025) estimates, extending the expiring individual tax provisions would reduce revenue by 1.0 percent of GDP in the coming decade, and extending the other expiring provisions would reduce revenue by another 0.2 percent of GDP. CBO (2025c) reported that extending the individual tax provisions alone would reduce revenue by 0.8 percent of GDP in 2055. Taken together, those figures suggest that extending all of the expiring provisions would reduce revenue by roughly 1 percent of GDP on average over the next three decades. Separately, CBO (2025d) reported that extending all of the expiring provisions *and* reducing revenue by a further specified amount would raise interest rates and put debt at 220 percent of GDP in 2055; subtracting a back-of-the-envelope assessment of the effect of the further specified revenue loss yields the approximate debt figure given in the text.

Figure 3
Primary Federal Deficit



Source: Supplementary data files for Congressional Budget Office *Long-Term Budget Outlook* documents (Jan. 2025 and March 2025).
Note: Solid lines are history; dotted and dashed lines are 2025 projections.

Figure 4
Real Interest Rate and Real GDP Growth
5-year lagged moving averages



Source: Authors' calculations based on data from Bureau of Economic Analysis and supplementary data files for Congressional Budget Office *Long-Term Budget Outlook* documents (Jan. 2025 and March 2025).
Note: Solid lines are history; dotted and dashed lines are 2025 projections. Beginning in 1995, the real interest is calculated as the nominal average interest rate published by CBO minus GDP price inflation. Prior to 1995, the real interest rate is calculated as 100*net interest/federal debt (CBO estimates) minus GDP price inflation.

under certain conditions, US debt less than about 160 percent of GDP would be "safe" in that sense. Still other researchers have estimated empirical reaction functions of policymakers and assessed whether policy is sustainable given those reaction functions; for example, Auerbach and Yagan (2024) found that fiscal feedback of the sort seen between 1984 and 2003 (but not more recently) would keep the US debt-to-GDP ratio below 250 percent for the coming century. Debrun et al. (2019) provided a useful review of a number of issues that arise in assessing fiscal sustainability.

Our goal in this section is to offer an intuitive understanding of the developments that would be needed to make current fiscal policies sustainable. We explore the possibilities that, relative to CBO's latest (2025c) projections, primary deficits would be smaller, economic growth faster, or interest rates lower. The opposite developments are clearly possible as well, and we draw out the implications of uncertainty later in the paper.

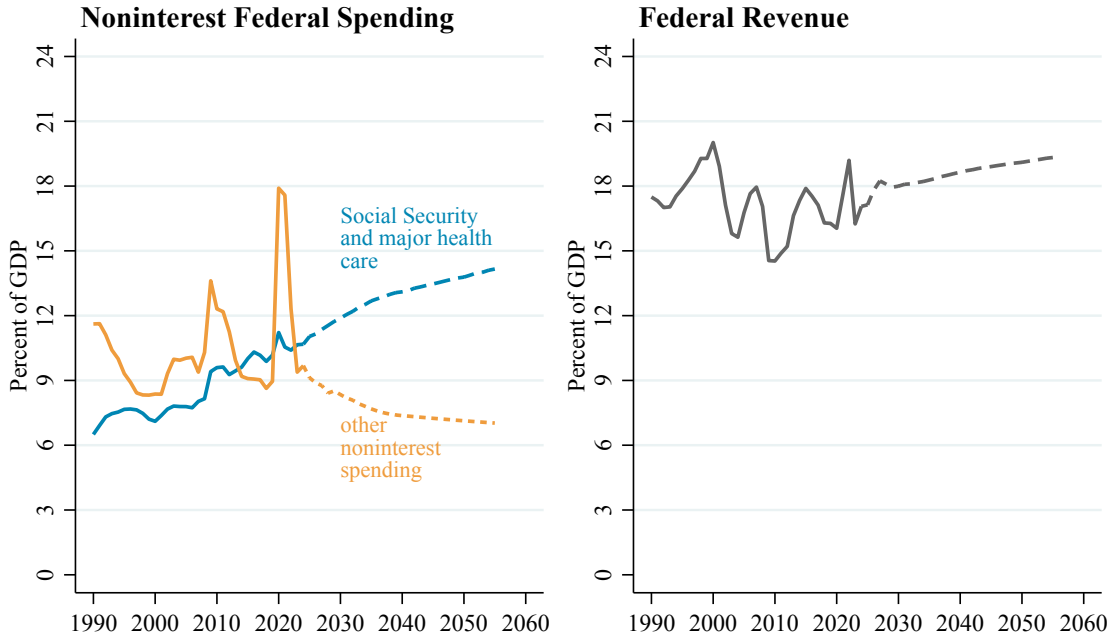
Primary Deficits

As noted above, over the next three decades, primary deficits are projected to be roughly 2 percent of GDP under current law and nearly 3 percent of GDP if the expiring 2017 tax cuts were extended permanently. Might primary deficits turn out to be considerably smaller than projected without any policy changes? We consider in turn the three broad components of the primary budget balance.

First, spending for Social Security and the major health care programs (Medicare [net of premiums paid], Medicaid, the Children's Health Insurance Program, and premium tax credits established by the Affordable Care Act) was just under 8 percent of GDP 30 years ago, is 11 percent of GDP in 2025, and is projected to be more than 14 percent of GDP 30 years ahead (as shown in the left panel of figure 5). That group of programs currently accounts for more than half of all federal noninterest spending. One key factor underlying the past and projected uptrends is the aging of the population; the other key factor is rising health care spending per person (adjusted for demographic change) relative to output per person, which CBO (2022b) terms "additional cost growth."

Population aging will certainly continue, but the future path of additional cost growth in federal health programs is especially difficult to predict: On one hand, such growth has trended down significantly over time, because of policy choices and other pressures to control costs; on the other hand, emerging new treatments may raise spending, because even when advances in medicine reduce health care costs at a point in time, any resulting increases in lifespans can raise total spending for health care (and Social Security). CBO's projections incorporate a slowing of additional cost growth, and that factor still accounts

Figure 5



Source: Supplementary data files for Congressional Budget Office *Long-Term Budget Outlook* documents (Jan. 2025 and March 2025).
Note: Solid lines are history; dotted and dashed lines are 2025 projections.

for growth in spending between 2025 and 2055 equal to 1.4 percent of GDP. But if additional cost growth falls even more than CBO projects, primary deficits would be smaller.

The second broad component of the primary budget balance is all other spending apart from interest payments. This component includes defense and nondefense activities determined by annual appropriations; the nondefense parts represent roughly half of this so-called "discretionary spending" and cover homeland security, highways, housing assistance, research and education, veterans' health care, and most of the government's operations. This component also includes include so-called "mandatory" benefit programs other than Social Security and the major health care programs, such as food stamps (known officially as "SNAP"), veterans' compensation, and federal retirement benefits.

CBO projects that spending in this broad category of federal spending will decline over time relative to GDP, from about 9 percent in 2025 to 7 percent in 2055 (as shown in the left panel of figure 5). For reference, the lowest share observed since 1962 (which is the earliest year for which comparable data are available) was 8.3 percent in the late 1990s. The projected decline stems directly from CBO's methodology. For the first decade of the projection period, appropriations are assumed to grow only with the prices of labor

(compensation) and purchased items for the coming decade and thus to decline relative to GDP. Thereafter, appropriations are assumed to grow in line with GDP following a short transition period. Meanwhile, the laws governing this set of mandatory benefit programs generally index benefits to inflation but not growth in inflation-adjusted incomes, so benefit payments tend to fall relative to GDP absent changes in law.

In the past, policymakers have made changes to appropriations and these benefit programs that have kept spending in this broad category from declining very far relative to GDP. One can surmise that this pattern has reflected growing demand for government services as the population has expanded and inflation-adjusted incomes have climbed (thereby boosting, for example, transportation needs and perhaps what society views as a minimum living standard). Because those trends probably will continue to some degree, "current policy" arguably would incorporate upward adjustments to spending relative to CBO's projections.

The current presidential administration wants to sharply reduce spending that is governed by nondefense appropriations, and if Congress concurs during the legislative process this year, that change in policy would reduce primary deficits. Whether such a reduction would be significant relative to the figures discussed here is not clear: Even if federal civilian employment fell by one-quarter, which would put such employment at its lowest level since 1950 (Office of Personnel Management 2025 and CBO 2024a), the savings in compensation would be less than 0.3 percent of GDP. And whether a sizable reduction in nondefense appropriations would persist is also not clear, as the historical record shows that previous efforts to reduce such appropriations have not been sustained.

The combination of a continuing uptrend relative to GDP for Social Security and the major health care programs and a projected downtrend relative to GDP for all other noninterest activities leaves total noninterest spending on a slight uptrend relative to GDP: CBO projects that, under current law, noninterest spending will rise from roughly 20 percent of GDP in 2025 to roughly 21 percent of GDP in 2055.

The third component of the primary budget balance is federal revenue. Revenue has shown no trend relative to the size of the economy for decades, equaling about 17 percent of GDP both 60 years ago and today. As noted earlier, legislated tax cuts have in the past offset the effect of the progressive tax code in increasing revenue relative to GDP as inflation-adjusted incomes rise—despite the well-known upward pressure on spending from

population aging.[6] Under current law, CBO projects that revenue will rise to a little over 19 percent of GDP in 2055 (as shown in the right panel of figure 5).

Revenue has varied considerably from year to year because of shifting economic and financial conditions, but *sustaining* higher revenue relative to GDP under current law would require more income in higher tax brackets, through either rapid growth of total income or a persistent increase in income inequality. The former outcome is covered implicitly in the discussion of higher productivity growth below. Regarding the latter outcome, CBO (2024c) estimated that, in 2019, households in the top one percent of the pre-tax, pre-transfer income distribution received 6 percent of total income and paid an average federal tax rate of 30 percent, while households in the middle three quintiles received 43 percent of total income and paid an average federal tax rate of 14 percent.[7] If 6 percent of total income shifted from the middle quintiles to the top percentile, federal tax revenue would rise by about 1 percent of GDP (.06*(.30-.14)) and the primary deficit would fall by that amount. However, such a rise in inequality also would increase eligibility for federal benefits, which would offset the higher tax collections to an important extent. Pierce (2021) estimated that a 14-percent increase in the standard deviation of the logarithm of earnings would reduce the budget deficit by less than 0.1 percent of GDP.

As discussed earlier, current law includes the expiration of significant tax cuts enacted in 2017. If the expiring tax cuts were made permanent so that current tax *policies* were maintained, revenue would be reduced and primary deficits increased by roughly 1 percent of GDP on average over the next three decades. In addition, the presidential administration is cutting the number of employees at the Internal Revenue Service very sharply, and that cut in staffing probably will reduce tax compliance and represent a separate drag on tax revenue in the future.

Economic Growth

In CBO's latest projection, total factor productivity growth in the nonfarm business sector averages 1.1 percent per year over the next 30 years. CBO (2024b) estimated that, if productivity growth was 0.5 percentage point per year higher, the debt-to-GDP ratio in

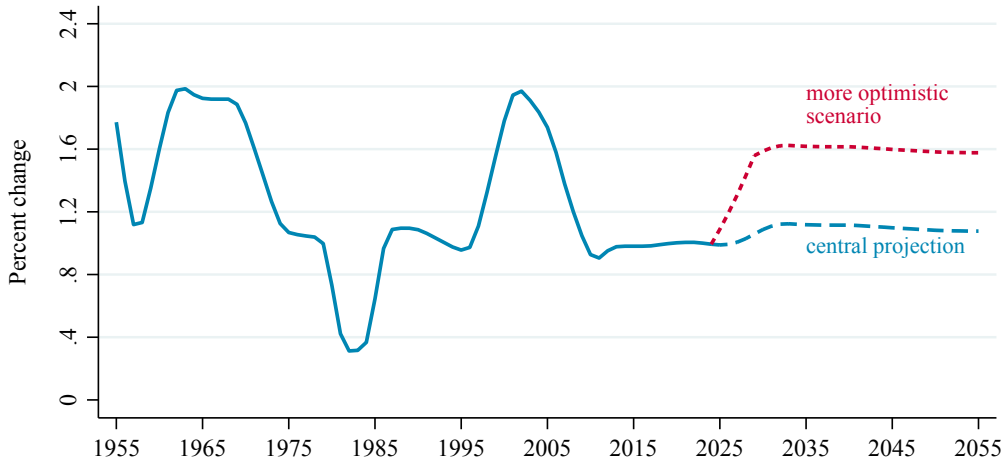
[6] The individual income tax code is generally indexed for inflation but not for growth in inflation-adjusted incomes.

[7] CBO presented estimates through 2021, but we use the figures for 2019 to avoid distortions related to the pandemic and associated policy responses. CBO used broad measures of income and taxes, and it defined pre-tax, pre-transfer income to include social insurance benefits such as Social Security and Medicare.

thirty years would be more than 40 percentage points below what it would be otherwise.[8] Is it plausible that this higher sustained pace of productivity growth could occur?[9]

Growth in potential total factor productivity has varied substantially over time (as shown by a five-year moving average in figure 6): Growth averaged 1.8 percent per year in the 1950s and in the 1960s, 1.1 percent in the 1970s, 0.7 percent in the 1980s, 1.3 percent in the 1990s, 1.4 percent in the 2000s, and 1.0 percent in the 2010s. Compared with average annual growth during the past thirty years, CBO's projection is about a tenth and a half lower—a difference that the agency attributes in part to smaller gains in educational attainment and a decline in federal appropriations for investment relative to GDP.

Figure 6
Total Factor Productivity Growth
5-year lagged moving average



Source: Authors' calculations and supplementary data files for Congressional Budget Office *Long-Term Budget Outlook* documents (Jan. 2025 and March 2025).
Note: Nonfarm business sector. Based on potential total factor productivity (history and projected) from 1950-2035 and actual projected total factor productivity growth thereafter. More optimistic scenario calls for 0.5pp higher total productivity growth starting in 2024. Solid line is history; dotted and dashed lines are projections.

[8] That estimate used CBO's baseline projections in early 2024; the agency has not released an updated estimate, but the number probably has not changed significantly.

[9] In CBO's analysis, faster productivity growth causes the average interest rate on federal debt to increase by a comparable amount, so (*r*-*g*) changes little, and the flattening of the debt path stems from the effect of faster growth on primary deficits. Economic growth could be boosted as well through faster growth of the capital stock or labor force, but sustaining such changes for decades would require ever-rising investment or higher fertility or immigration rates, and significant changes of those sorts do not seem plausible. Also, increases in fertility or immigration would have other effects on the budget that increases in productivity would not. For those who pine for the 3.3 percent annual average growth rate of GDP during the 1980s and 1990s, we note that annual labor force growth had fallen to a full percentage point below its pace in those decades prior to the immigration surge of the past few years.

Perhaps a much faster pace of productivity growth—closer to that of the 1950s and 1960s—will be achieved for a period through the further development and expanding use of artificial intelligence (or other technological advances). Indeed, it seems likely that, at some point, artificial intelligence will spur significantly faster productivity growth for an extended time. But sustaining notably faster productivity growth for decades is a tall order. The computer and online revolutions spurred fast growth at certain points during the past half-century, but those spurts did not last for decades. In addition, faster productivity growth through artificial intelligence might well displace workers so that output growth would not pick up in parallel with productivity growth, and the use of safety-net programs might increase.[10]

Interest Rates

In CBO's latest projection, the inflation-adjusted average interest rate on federal debt holds fairly steady around 1.5 percent over the coming decades (as shown in figure 4). CBO (2024b) estimated previously that, if the inflation-adjusted interest rate declined gradually and reached 0.2 percent in thirty years' time, the debt-to-GDP ratio in that year would be more than 30 percentage points below what it would be otherwise.[11] Is a persistent decline in the inflation-adjusted average interest rate to nearly zero plausible?

Treasury yields fell significantly during the 2000s and 2010s, with the nominal yield on 10-year Treasury notes dropping 3½ percentage points between 1999 and 2019 even as inflation changed little. The magnitude and persistence of the decline in inflation-adjusted Treasury yields—which was accompanied by declines in yields on both government and corporate debt in many other advanced economies—surprised many analysts and has generated a large amount of research regarding the global supply and demand for loanable funds. The drop in yields appears to have been caused by, among other factors, a reduced demand for investment stemming from slower trend growth of productivity and the labor force, along with an increased supply of saving as the effects of an older population and greater wealth inequality more than offset the impact of a surge in federal debt (for example, Gamber 2020).

[10] Elmendorf et al. (2025) explored a range of policy options that could boost productivity, including raising government support for research and development, relaxing restrictions on construction of housing and infrastructure, and changing tax policy related to business investment. But Elmendorf et al. explained that evidence is scarce regarding the magnitude of the productivity effects of many potential policy changes.

[11] As with the alternative path for productivity growth, an updated estimate using CBO's latest baseline projections probably would not be significantly different.

The inflation-adjusted average interest rate on federal debt dropped into negative territory during the pandemic and inflation surge and then rebounded as nominal yields increased and inflation retreated. Many of the factors that held down yields during the 2000s and 2010s are still present, such as slower growth of productivity and the labor force, but yields are being pushed up by other factors, including rising federal debt, greater investment in computing power and the energy transition, and a larger risk premium in light of the recent inflation experience and more-recent volatility of federal policy.

Analysts disagree about the net effect of these and other considerations (for example, Blanchard and Summers 2023, International Monetary Fund 2023, and Rogoff et al. 2024). CBO's (2025c) projection put inflation-adjusted interest rates above their level during the 2010s and below their level in earlier years.

One significant source of uncertainty is the sensitivity of rates to increases in federal debt—a sensitivity that is difficult to estimate because of endogeneity (weak economic activity causes debt to rise and interest rates to fall, but the rise in debt does not cause the fall in rates) and because the sensitivity might well change over time. Gust and Skaperdas (2024) documented estimates by previous researchers that an increase of 1 percentage point in the debt-to-GDP ratio increases long-term interest rates by 1 to 6 basis points, with more-recent estimates that use a greater span of data on the lower side.[12]

A further important issue is that government policies can effectively hold down interest rates on federal debt, by either increasing demand for debt or eroding the value of interest payments on existing debt. Some of these actions may be deliberate; others may occur as a collateral effect of decisions made for other reasons. Specifically, regulations to reduce the liquidity and solvency risk of financial institutions can push those institutions to hold more federal debt than they would otherwise—if implemented deliberately, a practice known as "financial repression"—and expansionary monetary policy can generate higher inflation that reduces the value of outstanding debt relative to nominal GDP—if implemented deliberately, a practice known as "fiscal dominance."

Both practices have been analyzed in substantial research literatures; for just a few examples, see Reinhart et al. (2011) on financial repression and Leeper (1991 and 2023) and Cochrane (2023) on fiscal dominance. Moreover, both financial regulation and

[12] CBO (2025c) projected that interest rates will stay fairly steady over the next 30 years, even though the large increase in debt would be expected to push up interest rates by more than a percentage point according to CBO's estimate (reported in Neveu and Schafer 2024) that each percentage-point rise in the debt-to-GDP ratio raises interest rates by 2 basis points. CBO did not directly explain which other factors are expected to push down interest rates by increasing amounts over time, but the key ones may be a projected slowing of labor force growth and rising private saving due to a projected increase in earnings inequality.

inflation have had quantitatively important effects on debt in the past: Acalin and Ball (2023) estimated that the drop in the debt-to-GDP ratio following World War II stemmed largely from unexpected inflation and the pegging of interest rates prior to the Treasury-Federal Reserve Accord of 1951, and high inflation in 2021 through 2023 (stemming from multiple sources) temporarily stabilized the debt-to-GDP ratio despite large primary deficits.

Looking ahead, though, these approaches seem unlikely to address a large share of the projected increase in government borrowing relative to the size of the economy.

Regarding financial repression, experience in this country and others suggests that some policymakers will try to deploy this strategy as debt rises. However, attempts by regulators to reduce risk by limiting financial institutions' investments are often rebuffed based on concerns about constricting the supply of credit and driving risk-taking into less-regulated entities. Therefore, significant, ongoing increases in pressure on financial institutions to hold federal debt rather than other assets would be surprising.

Regarding fiscal dominance, political leaders' short-term incentives to monetize debt increase as debt rises relative to GDP. Moreover, the current degree of independence for the Federal Reserve is not guaranteed to continue. For example, the president recently fired the leaders of two federal agencies for which the governing statutes appear to protect the leaders from being fired without cause, as is the case for the chair of the Federal Reserve Board; how the courts will rule in those cases and how those rulings might affect the Federal Reserve are not clear (Ip 2025b).

That said, policymakers have good reasons to keep resisting pressures to monetize debt even as debt rises. Higher inflation would be viewed very negatively by many people, as shown by research on preferences (for example, Stantcheva 2024) and by analysis of the 2024 presidential election (for example, Steinberg et al. 2024).[13] In addition, higher inflation would not necessarily improve the fiscal situation, because it would not only reduce the burden of outstanding debt but also increase interest rates on new debt (through higher expected inflation and a higher risk premium). That latter effect would be significant because the federal borrowing needed to both roll over outstanding debt and finance ongoing deficits is so large: For example, if inflation and interest rates were both 0.5 percentage point higher than projected, the estimates in CBO (2025b) imply that

[13] The Federal Reserve's reluctance to tighten monetary policy as inflation climbed in 2021 stemmed from a misinterpretation of incoming data rather than a deliberate accommodation of expansionary fiscal policy (Cieslak 2024; Dynan and Elmendorf 2024).

deficits over the coming decade would be roughly $1.6 trillion larger than projected. All told, ongoing monetization of substantial amounts of federal debt would be surprising.

In Sum

The authors of this paper have spent considerable time engaged in economic and budget forecasting, and we offer forecasts with humility and expect them to be received with skepticism. Nonetheless, we conclude that current fiscal policies are almost certainly unsustainable, because stabilizing the debt-to-GDP ratio under current policies would require large and favorable shifts in interest rates, productivity growth, primary deficits given existing policies, or all three. Moreover, unfavorable shifts in those factors are entirely possible as well, in which case larger changes in fiscal policies would be needed to stabilize the debt-to-GDP ratio.

If policies need to be changed at some point, the key questions for policymakers are *when* to change policies and *in what ways* to change policies. We take up these questions next. In answer to the "when" question, acting sooner rather than later would have a number of consequences, as we explain in the next two sections—the first addressing the effects of restraining debt growth, and the second addressing the implications of broadening the available policy options. In answer to the "in what ways" question, many considerations are relevant, and we choose just a few to highlight in the third section ahead.

One might expect a third question of *how much* policies might be changed. However, that question is really a variant of *when* policies might be changed, because the longer changes are delayed, the larger they need to be—either to hit the same debt-to-GDP ratio or to stabilize debt at a higher ratio to GDP (because that would require a larger primary surplus if the interest rate exceeds the economic growth rate, which is increasingly likely as debt rises).

With the economic growth rate and the average interest rate on federal debt projected by CBO to be roughly equal over the coming decades, the formula for debt dynamics presented above implies that stabilizing the debt-to-GDP ratio essentially requires primary budget balance. That balance was achieved, on average, during the roughly half-century preceding 2008—but it has not come close to being achieved in any year since then, and it will not be easy to achieve in the future.

More formally, the "fiscal gap" (Auerbach 1994) refers to the size of the policy adjustment that, if implemented immediately and maintained at the same share of GDP in each future year, would make the debt-to-GDP ratio equal to its current value at a chosen future date. The projected 30-year fiscal gap for the federal government is a little smaller than the

average projected primary deficit over the next 30 years because deficit reduction would strengthen economic growth, which would both reduce deficits further and allow for more debt in reaching a target debt-to-GDP ratio.[14] CBO has not released the data needed to estimate the fiscal gap corresponding to the agency's latest long-term projections.

Suppose, though, that the gap under current law was 1½ percent of GDP. Then, stabilizing the debt-to-GDP ratio near its current value of about 100 percent would require policymakers to allow the scheduled expiration of the 2017 tax cuts, enact no increases in benefit programs as inflation-adjusted incomes rise, decrease annual appropriations for defense and nondefense activities relative to GDP over time, *and* enact increases in revenue and reductions in spending that total roughly $450 billion per year now and stay at 1½ percent of GDP over time—or enact other combinations of policies with the same budgetary impact.[15]

When Might Policies Be Changed? The Effects of Restraining Debt Growth

Restraining the growth of federal debt has four principal effects: It raises national savings, provides insurance against emerging needs by increasing so-called "fiscal space," provides insurance against the risk of a persistent shortfall in economic growth, and provides insurance by reducing the chance of a fiscal crisis. We take up these effects in turn.

Raising National Savings

One effect of restraining debt growth is increasing national savings—thereby lessening the "crowding out" of capital—and in turn enhancing future living standards.

Because total factor productivity growth raises incomes over time, it is not apparent that current generations should give up consumption in order to increase the consumption of future generations. However, making sacrifices today to help people living in the future has long been part of our national ethos, and that ethos has been put into practice partly by restraining growth of government debt. Moreover, current generations will be leaving to future generations many substantial challenges, including threats to national security,

[14] Estimates of fiscal gaps presume that the policy changes made would have no effect on economic growth apart from the impact of reduced debt. If the policy changes boosted growth in other ways, smaller changes would be needed, and if the policy changes diminished growth in other ways, larger changes would be needed.

[15] Auerbach and Yagan (2024) estimated that, between 1986 and 1988, policymakers enacted deficit reduction equal to 2 percent of GDP, so there is precedent for fiscal adjustment of this magnitude.

climate change, and economic and social disruptions from artificial intelligence (which can co-exist with a positive effect of artificial intelligence on total output and income). In light of these burdens, some people may view greater restraint on government debt as especially important.

The quantitative impact of higher savings on future living standards is not as great as one might expect offhand. For example, Ball and Mankiw (1995) offered a very rough estimate that eliminating the national debt—then equal to about 50 percent of GDP—would raise national income by about 6 percent. That effect is large relative to the effects of many other potential policy changes but small relative to the growth of national income over time.

Moreover, the economic value of increasing national savings depends on the scarcity of capital. As the decline in interest rates during the 2000s and 2010s became more apparent, Summers (2014, 2015) argued that the economy was suffering from "secular stagnation" and that government borrowing was less costly or even beneficial under those conditions. Elmendorf and Sheiner (2017), Eggertsson et al. (2019), Blanchard (2019, 2023), Ball and Mankiw (2021), and many others have analyzed this issue. The body of research has shown that most, but not all, of the possible reasons why Treasury yields declined imply that capital is less scarce than it was before and therefore the value of increasing national savings is lower than it was before. Because Treasury yields have now reversed part of their earlier drop, one can infer that the value of increasing national savings probably has rebounded somewhat but remains lower than it was in the 1980s and 1990s.

Optimal national savings can be affected as well by the aging of the population. Aging stems from both greater longevity and lower fertility. Cutler et al. (1990) showed that both trends increase optimal savings since a larger retired population must be supported by a relatively smaller working population. However, lower fertility also has a countervailing effect, as slower labor force growth reduces the marginal product of capital and thereby decreases optimal saving. In a calibrated model, Elmendorf and Sheiner (2017) found that the net effect at that time was to raise optimal saving by roughly 1½ percent of GDP. In addition, population aging presents potential economic and budgetary challenges that are not included in the Elmendorf-Sheiner analysis (such as a possible damping effect on economic dynamism) or CBO's projections (such as the effect on state governments' Medicaid spending and possible demands for the federal government to support eldercare more broadly). Therefore, the aging of the population provides a further justification for increasing national savings.

Providing Insurance by Increasing Fiscal Space

Another effect of restraining debt growth is increasing the government's capacity to borrow more when budgetary needs arise without causing interest rates to spike upward. Such unused borrowing capacity is sometimes labeled "fiscal space," and it enables the government to respond more vigorously when some of today's uncertainties turn into tomorrow's problems.

One important use of fiscal space is countercyclical policy. The downtrend in interest rates over the past few decades has limited the Federal Reserve's room to cut the federal funds rate when economic activity is weak. That limitation increases the potential role of tax reductions and spending increases in spurring output and employment.

For example, during and after the global financial crisis, the federal government enacted fiscal stimulus equal to 10 percent of pre-crisis GDP, and after the COVID pandemic hit, the federal government enacted fiscal stimulus equal to 23 percent of pre-crisis GDP (Dynan and Elmendorf 2024). In addition, lower output and employment during those periods held down taxes and pushed up spending through the automatic stabilizers. All told, debt held by the public jumped from 35 percent of GDP in 2007 to 70 percent in 2012 and from 79 percent of GDP in 2019 to 97 percent in 2021, for a total increase of more than 50 percent of GDP during just 7 extraordinary years. To use fiscal space by deliberately increasing debt and allowing the automatic increase in debt during weak economic periods, fiscal space needs to be created by restraining debt during strong periods.[16]

Fiscal space also expands the government's capacity for responding to other problems that can arise. As noted above, significant risks to national security, the climate, public health, economic growth, and social stability abound. Maintaining fiscal space gives future policymakers more scope to take action and protect people when problems develop.[17]

Providing Insurance Against the Risk of a Persistent Shortfall in Economic Growth

A further effect of restraining debt growth is providing insurance against the risk that economic growth falls short of expectations for a prolonged period.

Recall that the average interest rate on federal debt has generally been lower than the growth rate of GDP. As Ball et al. (1995) explained, if the government ran a temporary primary deficit under those conditions, the increment to federal debt *probably* would

[16] Fiscal stimulus can reduce debt if the short-term multiplier is large enough or hysteresis is strong enough, but those conditions are not usually satisfied.

[17] Certain policy changes would help to insulate the government's finances from specific developments, such as indexing the eligibility age for Social Security to average life expectancy. However, that sort of change would not provide insurance against a broad array of possible developments, as lower debt would.

increase more slowly than GDP in the future, so the debt-to-GDP ratio would converge toward its original path with no further policy changes. However, Ball et al. pointed out that this favorable outcome is not guaranteed: If growth falters and interest rates do not decline commensurately, the debt-to-GDP ratio could increase, and subsequent policy changes would be needed.

Because that state of the world would already be unfavorable, the welfare consequences of the needed tax increases and spending cuts would be especially large. Indeed, people's recognition that adverse aggregate outcomes are possible *and* their desire to protect themselves from such outcomes can be seen in their acceptance of much lower average returns on safer federal debt than on riskier private capital.[18]

Providing Insurance by Reducing the Risk of a Fiscal Crisis

Yet another effect of restraining debt growth is reducing the risk of a fiscal crisis, which occurs when investors become unwilling to hold a government's debt at typical interest rates, and rates spike upward as a result. A fiscal crisis can occur because government borrowing surges or because investors lose confidence in policymakers' handling of government finances.

In a fiscal crisis, the spike in interest rates sharply increases the government's interest payments, and a given change in rates has a larger effect on payments for governments that have larger amounts of debt. The increase in interest payments worsens the outlook for debt, which can drive interest rates still higher, causing a path for debt that may have appeared sustainable to become quickly unsustainable. In addition, the runup in interest rates usually reverberates through the financial system, disrupting the flow of credit and impeding economic activity.

Without the ability to borrow as before, a government experiencing a fiscal crisis is forced to raise taxes and cut spending quickly, and often significantly, to lessen its borrowing. Such sudden and sizable changes in policies are generally painful for those who are affected directly, and they also can reduce overall output, income, and employment. Moreover, developing and implementing severe policy changes puts great strains on a country's political system.

[18] The return on private capital has generally been above the growth rate of GDP, which is consistent with the economy being dynamically efficient—so that increasing capital, as we discussed in an earlier sub-section, would raise rather than lower future consumption.

In countries whose governments borrow in currencies outside of their control, an inability to refinance existing debt at manageable interest rates can lead to default. For the US government, which borrows in dollars, default could be avoided by creating more dollars. However, creating more dollars would generate higher inflation, which would make many people unhappy and would cause investors to demand higher yields on new debt (as discussed above). In addition, given the central role of Treasury securities in global financial markets, a fiscal crisis in the United States would be especially damaging for the world's financial system and economy—and that widespread damage would increase the harm to Americans.

Assessing the probability of a US fiscal crisis at different levels of debt is difficult.

One approach is to examine periods of high government debt in other countries, as in Reinhart et al. (2012) among others. However, making strong inferences is difficult because sample sizes are small and countries differ in many respects. Reinhart et al. identified only 26 episodes where gross government debt exceeded 90 percent of GDP in advanced economies during the past two centuries.[19] Moreover, countries' situations differ not only in the amount of debt, but also in the size of deficits, the share of debt in externally controlled currencies, the structure of financial markets and institutions, the expected path of debt, and factors that affect the malleability of that path, including the capacity of the political system to address budget issues constructively. As a result, debt levels that may precipitate crises in some places and times can be readily accommodated in others.

Consider the example of Greece, which experienced a very serious fiscal crisis beginning in late 2009 and lasting for many years. At the start, gross government debt equaled about 140 percent of GDP—a high figure, but not as high as in Japan, for instance, where gross government debt now exceeds 200 percent of GDP and no fiscal crisis has emerged. Contributing factors to the crisis in Greece included a budget deficit close to 13 percent of GDP, a current account deficit that was almost as large, government debt denominated in Euros, widespread tax evasion, and significant revisions to budget statistics that reinforced concerns about the quality of publicly available data. The crisis and the sharp fiscal austerity adopted in response caused Greek GDP to fall dramatically and recover very slowly. The result was prolonged hardship. Moreover, there was little change in the debt-to-GDP ratio, as the fiscal consolidation was offset by the weakness of GDP.[20]

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[19] Gross government debt is a broader measure than debt held by the public, which is the usual focus of analysis for the United States and is our focus in this paper. At the end of fiscal year 2024, US gross debt was 122 percent of GDP, and US debt held by the public was 98 percent of GDP (CBO 2025a).

[20] For more on the Greek experience, see Lane (2012) and Thomsen (2019). Debt data in this paragraph and the following one are from the Organisation for Economic Co-operation and Development (OECD 2024).

Consider also the example of the United Kingdom, which experienced a far more limited fiscal crisis in 2022. Gross government debt equaled about 100 percent of GDP, and the government of prime minister Liz Truss announced new tax and spending proposals that investors feared would substantially increase debt—a perception reinforced by the government's decision to skip the usual review by the independent UK Office for Budget Responsibility. Yields on 30-year British bonds ("gilts") jumped 140 basis points over three days, with an initial increase in yields spurring bond sales by leveraged financial intermediaries that further pushed up yields, and the value of the British pound relative to other currencies fell sharply. To stabilize financial markets and limit spillovers to the nonfinancial economy, the Bank of England implemented an explicitly temporary purchase of gilts, but only after the government retracted most of the proposals and Truss resigned did yields normalize.[21]

Four lessons of the Greek and British experiences seem relevant for the United States. First, investors' perspectives can change very quickly, as UK financial conditions seemed calm prior to the budget announcement but then deteriorated abruptly. Second, higher debt and deficits increase vulnerability to potential shifts in investors' perspectives: If more fiscal space had been available, investors might not have lost confidence in those governments so rapidly, and the effect of higher interest rates on government budgets would have been smaller. Third, the ability to adjust policy swiftly is crucial in limiting damage from a crisis: The Greek government faced such a large budgetary imbalance that changing course took time (and assistance from the European Union and the International Monetary Fund), whereas the UK government could (and did) withdraw proposed new policies nearly overnight. Fourth, faltering confidence in the judgment and competence of government leaders, as occurred in both the Greek and British cases, can precipitate and worsen a fiscal crisis.

Even with those lessons in hand, the probability of a US fiscal crisis in the near term remains very unclear.

On the favorable side, interest rates on Treasury securities in April 2025 suggest that investors are not that worried about the fiscal outlook. As of this writing, the yield on 10-year Treasury notes and the yield on 10-year inflation-indexed Treasury securities are both close to their levels in 2007 when the debt-to-GDP ratio was about one-third what it is now.

However, there are also indications of significant vulnerability. One source of vulnerability is the nearly unprecedented size of federal debt and deficits. The United States has almost

[21] For more on the UK experience, see Chen and Kemp (2023) and Wilkins (2024).

no experience with federal debt that is larger than GDP, and it has no experience with sustained federal deficits that are close to 6 percent of GDP—but those outcomes are nearly upon the country absent changes in law that reduce deficits without delay.

Meanwhile, policymakers have taken no significant action to reduce deficits during the past twenty-five years and are currently planning to enact tax cuts that would substantially increase deficits going forward. Indeed, policymakers have struggled in recent years to accomplish more-basic fiscal actions such as raising the debt ceiling and funding government operations. Under these circumstances, maintaining investors' confidence in US governance cannot be taken for granted. We return to these political issues at the end of the paper.

Perhaps with those figures and events in mind, participants in US financial markets reacted in a surprising manner to the dramatic and shifting news about US trade policy in the first part of April 2025. During previous periods of global uncertainty, the demand for Treasury securities generally increased as investors sought safe assets, which pushed down yields on those securities and raised the exchange value of the dollar. During the global tumult in early April, by contrast, yields on Treasury securities increased, and the value of the dollar dropped. Some observers asserted that investors were losing trust in US governance and in the United States as a reliable partner to other countries (Goodman 2025 and Ip 2025a). While definitive conclusions cannot be drawn from such a short period, the episode raises questions about whether investors' perceptions have begun to shift.

A further worrying sign is estimates by Gómez-Cram et al. (2024) that increases in Treasury yields since the onset of the pandemic have been concentrated on days with unfavorable news about the fiscal outlook *and* that the effect of unfavorable news on yields has been greater during this period than it had been earlier. Given the size of debt and deficits, greater salience of fiscal news and greater sensitivity of interest rates to such news would not be surprising—and would increase the chance of a fiscal crisis.

Yet another source of concern is the maturity structure of Treasury debt. Debt equal to roughly one-third of GDP is maturing during 2025 and needing to be refinanced; the corresponding figures before the global financial crisis and before the pandemic were roughly one-tenth and one-fifth, respectively (Slok et al. 2024). With so much short-term debt, changes in market yields affect the government's interest payments fairly quickly. In

addition, liquidity in the Treasury market declined somewhat last year (Slok et al. 2024), which increases the chance that large auctions of debt will cause a sharp rise in yields.[22]

All told, the probability of a near-term fiscal crisis is not clear, but reducing debt would decrease risk in multiple ways: It would leave more fiscal space to respond to emerging needs, help to reassure investors that policymakers are managing the government's finances appropriately, and reduce the impact of an interest-rate increase on the deficit (which would lower the chance of a self-reinforcing cycle of rate increases).

Putting the Pieces Together

Consistent with the preceding discussion, Reinhart and Rogoff (2009) showed that countries with gross public debt exceeding 90 percent of output have experienced notably slower economic growth than countries with less debt, Reinhart et al. (2012) pointed to various researchers who have demonstrated a causal link from debt to growth, and Woo and Kumar (2015) showed that advanced economies with higher debt-to-GDP ratios experience slower subsequent growth. However, the evidence does not show that there is a specific debt-to-GDP ratio that represents an inflection point for economic growth or the probability of a fiscal crisis. Rather, the Greek and UK episodes we highlighted, as well as the movements in US financial markets in April 2025, suggest that fiscal danger stems not from high debt alone but from the interaction of high debt with other factors such as loss of confidence in governance.

We are left with a qualitative conclusion: Changing policies sooner rather than later would put debt on a lower trajectory and thereby increase national savings and provide insurance against adverse developments by expanding fiscal space, protecting against a persistent shortfall in economic growth, and reducing the chance of a fiscal crisis. These effects have become more notable during the past several years because debt has increased relative to GDP, inflation-adjusted interest rates have risen, the possibility of future economic downturns and health crises that would lead to fiscal responses is even clearer, and risks to national security, the climate, and social stability have increased.

Indeed, a key reason to prevent federal debt from rising into uncharted territory well above 100 percent of GDP is that no one knows what might happen if federal debt rose so far and no one knows what else the future holds. Yet, the probability of a near-term fiscal crisis is

[22] By contrast, the distribution of holders of Treasury securities is not especially concerning. One potential trigger for a fiscal crisis would be a decision by foreign holders to sell large amounts of debt in a short time, motivated perhaps by geopolitical considerations. However, holdings by foreigners have fallen to about 30 percent of the total today from nearly 50 percent a dozen years ago, and holdings by foreign official institutions have fallen to roughly 14 percent from roughly 35 percent over that same period.

difficult to assess: Interest rates are within their range of the past few decades, which suggests that investors are not that worried about the fiscal outlook, but experience shows that investors' confidence in a government's fiscal management can deteriorate quickly.

When Might Policies Be Changed? The Implications of Broadening Available Policy Options

Deciding sooner rather than later about policy changes to put federal debt on a sustainable path broadens the available options in multiple ways.

First, deciding sooner allows for changes to be implemented more gradually while still reaching a chosen amount of debt. Such gradual implementation can enhance economic efficiency. In particular, a smaller increase in tax rates applied sooner would distort work behavior less than a larger increase in tax rates applied later (Barro 1979).

Second, deciding on policy changes sooner enables policymakers to adjust the impact of tax and spending changes across more birth cohorts than if they decide later. For example, discussions of possible reductions in Social Security benefits usually involve broad agreement that people who are already collecting benefits or are close to doing so should not face reductions because they cannot adjust their work or saving behavior in response. A significant share of federal spending supports older people, so this consideration is potentially important.

For another example, CBO (2022a) estimated that delaying by 10 years increases in income tax rates sufficient to stabilize the debt-to-GDP ratio would raise the lifetime consumption of people in the lowest income tercile who were born in the 1940s and 1950s by 0.3 percent and have little effect on their hours worked, and it would lower the lifetime consumption of their counterparts born in the 2000s and 2010s by 1.1 percent while reducing their hours worked. As with the impact of increasing national savings that was discussed earlier, those differences are large relative to the effects of many other policy changes even though small relative to generational differences in lifetime incomes.

Third, deciding on policy changes sooner enables policymakers to implement the changes when economic activity is strong and fiscal stimulus is not needed to maintain full employment. Because tax increases and spending cuts that would put debt on a sustainable path would generally reduce aggregate demand in the short run, those changes would have larger economic costs when economic activity is weak, especially if the effective lower bound on interest rates would prevent the Federal Reserve from easing monetary policy in response to the tightening of fiscal policy. Under those conditions, the

short-term cost of fiscal restraint would be significant, and fiscal sustainability might not even be enhanced (Summers 2014; Auerbach and Gorodnichenko 2017). This concern is consequential because the federal funds rate was close to zero for 9 of the 13 years from 2009 through 2021, did not exceed 2½ percent for any month in that span, and may well return to zero at times in the future.

In What Ways Might Policies Be Changed?

The policy changes needed to stabilize the debt-to-GDP ratio are large, so choosing them wisely is important. Many considerations matter, including preferences about the role of government, evolving national and global conditions, possibilities for increasing economic growth, and the desired distribution of government benefits and burdens within and across generations.[23] Much has been written about those topics, and we limit ourselves to highlighting three issues.

First, because the core rationale for restraining debt is to help people in the future, debt-reducing policy changes that harm people's prospects in some other way could be at cross-purposes. The legacy of current generations to future ones will include more than just the federal debt—it will also include national security, public infrastructure, educational attainment, social cohesion, the climate and environment, and more. Spending cuts and tax increases that did not adversely affect those influences on well-being would be most consistent with the core rationale for restraining debt.

In particular, policy changes that directly reduce economic growth could be inconsistent with the core rationale for restraining debt—but avoiding such changes is challenging, because many sorts of reductions in government spending and increases in taxes could diminish growth apart from their effects via debt reduction. For example, research has shown that federal outlays for infrastructure and for research and development are investments with substantial returns; for example, see Ramey (2021) and Fieldhouse and Mertens (2023). In addition, a number researchers have demonstrated that government programs providing resources to lower-income families can improve the earnings potential and other aspects of life trajectories for children or adults in those families; examples include Aizer et al. (2022), Bailey et al. (2023), Brown et al. (2020), Hendren and Sprung-Keyser (2020), Hoynes et al. (2016), and Miller and Wherry (2019). Similarly, tax policy affects work, saving, and investment; for example, see Chodorow-Reich et al. (2024) and

[23] For examples of comprehensive proposals for changing tax and spending policies, see Gale (2019), Grand Bargain Committee (2024), and Peterson Foundation (2024).

Goodman et al. (2024). Elmendorf et al. (2025) reviewed evidence regarding these and other government policies that affect economic growth.

Second, because socioeconomic inequality has increased and income mobility has declined over the past several decades—see Case and Deaton 2023 and Chetty et al. 2017, among others—the distributional impact of potential tax and spending changes may be more important to policymakers now. For example, a report from the National Academies of Sciences, Engineering, and Medicine (2015) estimated that life expectancy was increasing across much of the income distribution but not in the lowest two quintiles, so some proposals to raise the eligibility age for full Social Security benefits include an offsetting adjustment to benefits for workers with lower lifetime incomes.

More generally, CBO (2024c, figure 5) showed that federal taxes and transfers have offset some, but not all, of the substantial increase in pre-tax, pre-transfer income inequality seen over the past several decades. Spending reductions or tax increases that diminished the progressivity of taxes and transfers would reinforce that rise in inequality rather than provide a counterweight to it. Yet, the upward trajectory of spending relative to GDP for the largest benefit programs will need to be altered at some point, or taxes would need to be increased again and again—and governments in other countries that collect more revenue relative to GDP than the US government often do so using broad-based consumption taxes that impose burdens across much of the population. Therefore, approaches to restraining benefits that protect lower- and middle-income recipients may receive particular attention as part of debt restraint. Note also that debt reduction itself has distributional effects, because increasing national savings tends to raise wages and reduce returns to capital.

Third, because the effective lower bound on interest rates can hinder the Federal Reserve in responding to economic downturns, and because fine-tuning fiscal stimulus through discretionary policy changes is difficult, the strength of automatic fiscal stabilizers has become more consequential. As discussed earlier, the decline in interest rates over the past few decades has limited the Federal Reserve's ability to lower the federal funds rate when the economy weakens, which has increased policymakers' interest in well-timed and appropriately sized fiscal stimulus. But economic forecasting is prone to error, and the fiscal policymaking process is not agile, so discretionary actions to provide fiscal stimulus can easily fall short of what would restore full employment, as in 2011 and 2012, or exceed what would have restored full employment, as in 2021 and 2022 (Dynan and Elmendorf 2024). Stronger automatic stabilizers not only would provide fiscal support more quickly when needed but also would withdraw fiscal support more quickly when the need recedes. For some potential approaches to strengthening automatic stabilizers, see Boushey et al. (2019) and Dynan and Elmendorf (2020).

How Will the Political Process Respond to Rising Debt?

For decades, analysts have warned that the aging of the population and rising health care spending, together with repeated tax cuts that restrained revenue growth, were putting US fiscal policy on an unsustainable path. Sharp runups in federal debt spurred by the global financial crisis and the COVID pandemic have significantly accentuated the unsustainability of current policies. Absent very favorable economic changes that are highly unlikely, the United States will ultimately need to scale back large and popular benefit programs, increase taxes relative to historical experience, or both.

Yet, over the past twenty-five years, policymakers have taken no significant action to put federal debt on a sustainable path. Instead, they have enacted legislation that, on balance, has increased debt substantially. Two bipartisan efforts to forge agreement on policy changes that would have lowered the debt trajectory—the 2010 National Commission on Fiscal Responsibility and Reform (commonly known as the "Bowles-Simpson commission" after its co-chairs) and the 2011 Joint Select Committee on Deficit Reduction (commonly known as the "Supercommittee")—failed to accomplish that goal. Moreover, Congress adopted a budget plan in early 2025 that would increase deficits by trillions of dollars over the coming decade relative to current law (Committee for a Responsible Federal Budget 2025).

This lack of deficit-reducing action represents a distinct change from policymakers' behavior in the 1980s and 1990s. During those decades, policymakers enacted some legislation that increased debt, but they also enacted legislation that reduced debt substantially. Recent estimates of the reaction function of fiscal policymakers confirmed the impression that policymakers have stopped responding to rising debt in substantive ways (Auerbach and Yagan 2024).

Moreover, several elements of the political environment suggest that a meaningful shift toward a sustainable debt path is unlikely to occur soon.

To start, the wide divide between the two major political parties has made even routine fiscal actions, like raising the debt ceiling or enacting appropriations to keep government operations running, difficult to achieve. In this atmosphere, reaching bipartisan agreement on the much more challenging actions needed to lower the debt trajectory does not seem feasible. Moreover, neither party has much incentive to restrain government borrowing on its own, because most significant tax increases and spending cuts would generate popular resistance, and because the fiscal space that would be created might be used by the other party to advance its own priorities when it next gains political control.

In addition, building public support for the scale of the policy changes needed to stabilize the debt-to-GDP ratio will be difficult. Although polls show that many people are concerned about rising debt, public knowledge about the federal budget is naturally limited and distorted in various ways. As a result, many people will be skeptical of specific potential tax increases and spending cuts unless public leaders make a persuasive case that those changes are worth making in order to lower the trajectory of debt—and the rise of populism shows widespread distrust of traditional leaders and institutions.

A further obstacle is that, despite years of predictions by public figures about the negative consequences of high and rising debt—and a near-tripling of debt relative to GDP since 2007—the predicted consequences generally have not materialized in visible ways. One partial exception is the inflation surge during 2021 and 2022 that has been linked to fiscal stimulus by some analysts (for example, Dynan and Elmendorf 2024) and that led the Federal Reserve to raise the federal funds rate significantly. But the most important sources of economic disruption in the United States in the 21st century have been financial meltdowns, disease vulnerability, technological change, and globalization, so people's attention might well be more focused on those challenges than on federal debt.

Then, what lies ahead?

Decisions about fiscal policy in 2025 will be important. With the scheduled expiration of tax cuts at the end of the year, promises made during the election campaign, and single-party control of the executive and legislative branches of the federal government, significant changes in tax and spending laws are coming. The extent to which those changes raise the trajectory of debt will matter directly and will also be a signal about likely fiscal policymaking during the following few years.

Looking further ahead, the spur for action is not clear. One possibility is that the depletion of the trust fund for old age and survivor benefits in Social Security—projected most recently for 2033—will induce changes in spending or dedicated revenue for that program. But that depletion date is still some distance in the future, and policymakers who want to avoid making substantive changes to the program could handle the trust-fund depletion simply by transferring money from the government's general funds into the trust fund.

Another possibility is that interest rates will increase significantly at some point because of high and rising federal debt. The escalation in borrowing costs for households and businesses—and the larger amount of federal interest payments—could make voters unhappy enough that they push their elected representatives to restrain debt growth. Or, if

the increase in rates is so sudden and sizable as to constitute a fiscal crisis, policymakers might have no choice but to raise taxes and cut spending sharply.

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