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Three Ways to Rein in the Runaway Deficit

By Editor Test *Wed, Oct 27, 2010*

Without changes in tax and spending rules, the national debt will rise from 62% of GDP now to more than 100% of GDP by the end of the decade, says economist Martin Feldstein.

In a new analysis, "Preventing a National Debt Explosion," the economist Martin S. Feldstein discusses three strategies that, if combined, could reverse the rapid growth of the U.S. national debt and reduce the ratio of debt to Gross Domestic Product (GDP) to less than 50%.

Without changes in tax and spending rules, Feldstein finds, the national debt will rise from 62% of GDP now to more than 100% of GDP by the end of the decade and nearly twice that level within 25 years.

- The first strategy, which focuses on the current decade, would "reduce the Administration's proposed spending increases and tax reductions that would otherwise add $3.8 trillion to the national debt in 2020."
- The second strategy would "augment the tax-financed benefits for Social Security, Medicare and Medicaid with investment-based accounts would permit the higher future spending on health care and pensions with a relatively small increase in saving for such accounts."
- The third strategy focuses on tax exemptions and other subsidies that result in an annual revenue loss of about $1 trillion. "Reducing them could permanently reduce future deficits without increasing marginal tax rates or reducing the rewards for saving, investment, and risk taking," the paper said.

Feldstein's paper concludes with a discussion of how the high debt-to-GDP ratio after World War II was reversed and how the last four presidents ended their terms with small primary deficits or primary budget surpluses.