

# Business insights

## *Federal spending lags expectations*

Federal government spending has been running substantially below forecasts since the beginning of January. Although the most recent Congressional target for spending during fiscal 1977 (ending September 30) was set at \$417 billion, actual spending during the January-March quarter was at an estimated annual rate of \$398 billion.<sup>1</sup>

This shortfall in spending since January 1 is in marked contrast to what occurred during the first quarter of fiscal 1977 (October-December 1976) when spending was at an estimated annual rate of \$413 billion.<sup>2</sup> This rate was in line with the level set in the Second Congressional Budget Resolution, \$413.1 billion, passed September 16, 1976. That resolution established the spending target in effect prior to President Carter's request for changes in the budget dated February 1. The Third Budget Resolution was passed by Congress on March 3, 1977 to accommodate the new Administration's request for additional stimulus to the economy.

### **Rerun of 1976**

The current shortfall in federal government spending repeats the experience of the second and third quarters of 1976. Then, too, federal spending dropped substantially below expected rates. As a result total spending during fiscal 1976 was \$366 billion instead of the expected \$374 billion. During the second quarter of 1976 (the final quarter of fiscal 1976) the Office of Management and Budget (OMB) suggested that the lower than expected spending had occurred because of the change in timing of the fiscal year. Historical-

ly, federal agencies have accelerated spending toward the end of each fiscal year to prevent the lapse of spending authority. However, under the new budget procedure the timing of the fiscal year was changed. Fiscal 1976 was the last fiscal year ending June 30. The July-September quarter was scheduled as a transition quarter between fiscal 1976 and fiscal 1977, but spending plans had been made for the entire 15-month period from July 1, 1975, through September 30, 1976, rather than for the usual 12 months. OMB expected the shortfall in spending to be made up during the transition quarter, but this did not occur. Actual spending during the transition quarter was \$95 billion instead of the \$102 billion OMB predicted when the quarter began.

In October of last year the Congressional Budget Office (CBO) released an analysis of spending during fiscal 1976 and the transition quarter, and concluded that the shortfall in spending had occurred over a broad spectrum of agencies and departments. CBO suggested a number of reasons for the shortfall:

- Inflation was lower than had been anticipated when spending was planned.
- Interest rates and federal borrowing were both lower than forecast, lowering total interest costs.
- Sales of government assets (negative expenditures) exceeded plans.
- Several programs, particularly procurement for defense, proceeded slower than planned.
- Department budgets included larger-than-normal contingencies which had gone unused.

On April 22 OMB notified Congress that spending was lagging targets and stated that it now expects spending for fiscal 1977 to total

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<sup>1</sup>U.S. Treasury data, adjusted for seasonal variation and trend.

<sup>2</sup>See note 1.

## The Federal Budget—An Ongoing Process

The Congressional Budget Act of 1974 provides a formal calendar of steps in the development and control of the federal budget. This schedule extends from November 10, nearly a year before a particular fiscal year begins, until July 15 of that fiscal year, a span of 20 months. Some aspects of budget planning and control by both Congress and the executive branch, therefore, occur simultaneously for the current fiscal year and two succeeding years. The major deadlines in the calendar are listed below. Changes may be made at other times if necessary.

- November 10 - President submits the "current services estimates" for the next fiscal year to Congress. This document provides estimates of budget authority and outlays needed assuming no change in programs or levels of activity.
- January<sup>1</sup> - President submits "The Budget of the U.S. Government" to Congress. This document gives the Administration's detailed plan for the next fiscal year, including new and changed programs, tax changes, and the economic assumptions on which the plan is based. Proposed wording of each appropriations bill is included in an Appendix.
- March 15 - Committees in each house of Congress submit reports to their respective budget committees giving suggested budget action in their areas of jurisdiction.
- April 1 - Congressional Budget Office submits report to budget committees analyzing the impact of the budget on the economy and recommending an appropriate fiscal policy.
- April 15 - Budget Committees in both houses report their proposed versions of "The First Concurrent Resolution on the Budget" recommending ceilings on authorizations and outlays, a floor for revenues, detailed allocations of spending by major functions, and, if needed, a change in the federal debt limit.
- May 15 - Congress adopts "The First Concurrent Resolution on the Budget."
- September<sup>2</sup> - Congress completes action on all bills providing budget authority.
- September 15 - Congress adopts "Second Concurrent Resolution on the Budget."
- September 25 - Congress adopts "Reconciliation Bill" to adjust previous legislation for conformity with second budget resolution.
- October 1 - Fiscal year begins.
- April 10 - President submits budget update requesting changes as needed for accommodating newly enacted programs, new proposals by the Administration, and changed economic assumptions, if any.
- July 15 - President submits second budget update, if needed.

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<sup>1</sup>Fifteen days after Congress begins.

<sup>2</sup>One week after Labor Day.

\$408 billion. This amount is in line with the average rate of spending during the first six months of the fiscal year, but even to reach this level will require a large increase in spending over the rate of the January-March period. OMB explained their lowered estimates for fiscal 1977 spending with several of the same reasons set forth in the CBO analysis of the overestimates of 1976. They added the same cautionary note they had underlined during 1976. Most of the unspent funds remain authorized, so that estimates of spending could swing from being too high to being too low in 1978 and later years. This is particularly true for fiscal 1978 since some of the stimulus provided by the President's plan for 1977 may not appear as actual spending until after 1978 begins.

Some observers have suggested that the change in the Administration may account for part of the lag in spending. Delays in filling second-level policy and administrative positions and in implementing programs of the new administration have resulted in spending based on the original fiscal 1977 budget submitted by President Ford in January 1976. That budget had called for spending of \$395 billion for the fiscal year, over \$20 billion less than the new Administration's proposal. Although President Ford raised his estimate of fiscal 1977 spending to \$411 billion in the January 1977 budget message, this increase in planned spending did not show up in the actual spending in January, his last month in office. Since then departmental spending has remained at a restrained level while President Carter and his subordinates translated their plans into detailed action.

Difficulty in estimating what government spending will be has not been confined to the most recent two years. Furthermore, the tendency has been to regularly overestimate spending six months before the end of the fiscal year. Since fiscal 1970 the estimates made six months ahead have underestimated spending only twice, in 1970 and 1974. Forecasting the deficit accurately has proven to be even more difficult. OMB currently is engaged in a major effort to improve the quality of budget estimates. Unfortunately

their task is made very difficult by the size of the numbers involved. An error of 1 percent in forecasting corresponds to an absolute error of over \$4 billion.

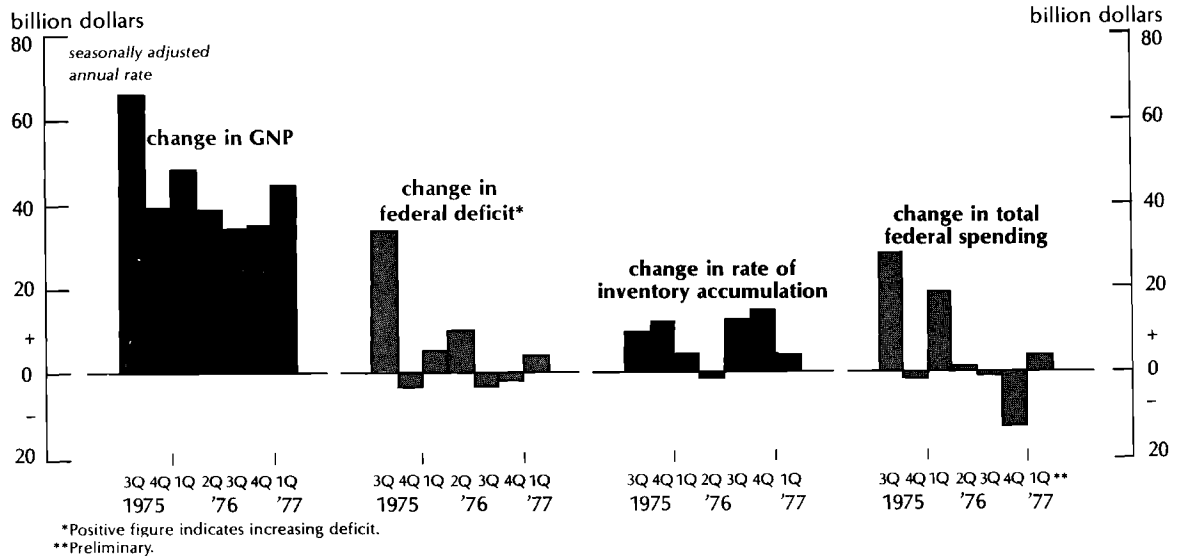
### Shortfall and the economy

During the current and the 1976 periods of government spending lags, government receipts remained roughly in line with expectations, so the shortfall in spending was accompanied by a corresponding decrease in the federal deficit. During fiscal 1976 and the transition quarter taken together, spending totaled \$461 billion, \$12 billion below the estimate of March 1976. The deficit for the two periods combined was \$79 billion, about \$14

| Budget estimates and results |                             |                              |               |
|------------------------------|-----------------------------|------------------------------|---------------|
| Fiscal year                  | First estimate <sup>1</sup> | Second estimate <sup>2</sup> | Final result  |
| (billion dollars)            |                             |                              |               |
| a. Spending                  |                             |                              |               |
| 1970                         | 194.3                       | 195.0                        | 196.6         |
| 1971                         | 200.1                       | 212.8                        | 211.4         |
| 1972                         | 229.2                       | 236.6                        | 231.9         |
| 1973                         | 246.3                       | 249.8                        | 246.5         |
| 1974                         | 268.7                       | 274.7                        | 268.4         |
| 1975                         | 304.4                       | 313.4                        | 324.6         |
| 1976                         | 349.4                       | 373.5                        | 366.5         |
| Transition Q <sup>3</sup>    | 98.0                        | 102.1                        | 94.7          |
| 1977 <sup>4</sup>            | 394.2                       | 417.4                        | 408.2 (est.)  |
| b. Surplus or deficit ( )    |                             |                              |               |
| 1970                         | 4.3                         | 8.7                          | (2.8)         |
| 1971                         | 2.0                         | (18.6)                       | (23.0)        |
| 1972                         | (11.6)                      | (38.8)                       | (23.2)        |
| 1973                         | (25.5)                      | (24.7)                       | (14.3)        |
| 1974                         | (12.7)                      | (4.7)                        | (3.5)         |
| 1975                         | (9.4)                       | (34.6)                       | (43.6)        |
| 1976                         | (51.8)                      | (76.0)                       | (66.5)        |
| Transition Q <sup>3</sup>    | (16.1)                      | (20.0)                       | (12.9)        |
| 1977 <sup>4</sup>            | (42.9)                      | (68.0)                       | (48.7) (est.) |

<sup>1</sup>Six months prior to the start of fiscal year.  
<sup>2</sup>Six months after the start of fiscal year.  
<sup>3</sup>For the transition quarter the first estimate was included in the 1977 Budget message. The second estimate was issued in the 1977 budget update on July 16, 1976 and was not changed during the quarter.  
<sup>4</sup>The first estimate is the budget submitted by the Ford Administration. Because of the shift in the fiscal year this estimate was about nine months prior to the starting date rather than the six months for earlier years. The second estimate was submitted by the Carter Administration in the 1978 Budget revisions, issued February 22, 1977. The final result is the OMB estimate of mid-April.

## The 1976 GNP slowdown



billion below the expected level. It is now estimated that the fiscal 1977 deficit will be about \$20 billion less than the \$68 billion forecast by OMB in the February budget revision message. Dropping of the rebate accounts for part of the reduced estimate of the deficit but about half the reduction results from lower-than-expected spending. Many economists believe that the lower-than-expected levels of government spending, and perhaps more important, the smaller-than-expected deficit contributed significantly to the slowdown in GNP growth which occurred during 1976. Other economists, however, suggest that the lag in government spending merely happened to coincide with an inventory adjustment following the big swing toward inventory accumulation which occurred in the first quarter of 1976. When the quarterly changes in GNP growth, government spending, and the changes in the rate of inventory investment are examined there are enough similarities to suggest impact from both government action and inventory adjustment were factors.

The two quarters with the lowest growth in GNP followed the two quarters of slow-

down in federal spending with a one-quarter lag, and the more rapid growth during 1977-I followed two quarters of more rapid increase in federal spending. The size in the change of GNP changed from the previous quarter in the same direction as the change in rate of inventory accumulation in every quarter since 1975-III except the last quarter of 1976. The change in the size of the deficit from quarter to quarter does not show any clear relationship with the changes in GNP.

Regardless of the attitude toward the importance of the shortfall in government spending during 1976, most observers look upon the current shortfall as a favorable factor for the economy for the rest of 1977. The lower deficit accompanying the slower growth of spending suggests that interest rates will be lower than they otherwise might be, encouraging capital expansion by the private sector. Furthermore, the lower federal spending now means that the increases in spending over the next few years are added to a lower base. The chances for progressive reductions in the deficit are thus enhanced.

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