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PRESS BRIEFING
BY DIRECTOR OF THE OFFICE OF MANAGEMENT AND BUDGET JIM NUSSLE
AND
CHAIRMAN OF THE COUNCIL OF ECONOMIC ADVISERS DR. ED LAZEAR ON THE MID-SESSION REVIEW

Room 350
Eisenhower Executive Office Building

1:40 P.M. EDT

DIRECTOR NUSSLE: Good afternoon. Thank you for attending. The Mid-Session Review -- or popularly called the MSR -- updates the administration's estimates of receipts, outlays, and deficits or surpluses, to reflect economic, legislative and other changes since the President's FY'09 budget was released back in February.

I'm going to give you some of the highlights of the budgetary changes, and then turn it over to Dr. Lazear for an overview of the economic assumptions. And then we'll take your questions. And as Kristen said, because Dr. Lazear has to leave at 2:00 p.m., I think probably what we'll do is try and focus questions to you first, and then I'll stay behind for a little bit more.

Relative to 2007, the budget deficit for the next two years will be higher before it begins declining, and reaches surplus in 2012. Specifically, for this budget year 2008, the budget deficit is now estimated to be $389 billion, which is $21 billion lower than estimated in February, where it stood at $410 billion.

At 2.7 percent of GDP, gross domestic product, the 2008 deficit is projected to be just slightly above the average of the last 40 years, which is about 2.4 percent of GDP. The MSR provides a snapshot of the budget when Congress left for the July 4th recess, and reflects the enactment of the farm bill and the supplemental appropriations bill.

However, more recent developments such as the Medicare "doc fix," as it's called, or the housing bill, are not fully captured in this MSR. This suggests the final deficit for 2008 will be larger than our current projection of $389 billion.

So to be clear, that means that every dollar that is spent, whether it's spent by the administration or the Democrat Congress, spends beyond the budget and drives the deficit higher. For 2009, the deficit is projected to rise to $482 billion, or 3.3 percent of GDP. This is still below the recent peak of 3.6 percent of GDP in 2004, and it's well below the record deficit of all time, which was 6.0 percent of GDP back in 1983.

The primary reasons that there will be larger deficits in 2008 and 2009 are because of the bipartisan growth package, or stimulus checks, as well as slower economic growth. Earlier this year, the President and Congress, on a bipartisan basis, correctly agreed that action was needed for our economy, and made a deliberate and conscious decision to temporarily increase the deficit in order to get money into the people's hands and spur consumption. The determination was made that getting the economy back on track was a higher priority than immediate deficit reduction.

`To give you context for how the stimulus has impacted the deficit we talk about today, if you somehow could exclude the bipartisan growth package, the deficit would be 1.9 percent of the economy, or about $272 billion, instead of the $389 billion we speak of today. The deficit is projected to fall sharply then after 2009, with deficits in 2010 and '11, only slighter higher than we projected back in February. The President's budget blueprint remains on track to achieve balance with surpluses of $58 billion in 2012, and $29 billion in 2013.

The important point to remember is that near-term deficits are both temporary and manageable if, and only if, we keep spending in check, the tax burden low, and the economy growing. Excessive spending beyond the President's budget plan will make the problem worse. And it already appears that congressional Democrats are lining up to bust through the President's budget, and for that matter, bust through their own budget. They are seeking to add billions in extra spending to the regular appropriations bills, which will drive up the deficit even further. They've already racked up $209 billion in more spending requests than the President. That's why the President has been clear that discretionary spending beyond his reasonable and responsible levels will be met with a veto.

The President has also repeatedly proposed sensible reforms to the automatic entitlement spending that now accounts for almost two-thirds of the budget. Simply raising taxes is no solution and often makes the problems worse. And congressional Democrats plan to pay for all of their big-government spending with the largest tax increase in history. This is anti-growth policy. It will hurt our economy and jobs, and it will have a negative impact on the bottom line for taxpayers, as well as government.

We can drive down the deficit and get to balance if we maintain fiscal responsibility and continue pro-growth policies. The President and congressional Republicans have a plan to do just that, by restraining spending, the passage of the Colombia and Korean trade agreements to help increase job creation, sensible adjustments to achieve savings and important entitlement programs, and the extension of the President's tax relief which will prevent 116 million Americans from facing an average tax increase of $1,800.

And most importantly, the President and congressional Republicans have a plan to reduce our dependence on foreign sources of energy, including a budget amendment the administration is sending up today that would delete two provisions from the fiscal year 2009 budget request. This amendment would lift the restriction on spending for offshore pre-leasing, leasing, and related activities in federal waters in the Outer Continental Shelf. And we call on Congress to adopt these changes.

Unfortunately, congressional Democrats have a long record of standing in the way of steps when it comes to energy security. For example, back in 1995, President Clinton vetoed legislation that would have opened ANWR to oil production, arguing at the time that it would only supply a small portion of our needs. However, if he had signed that legislation, domestic oil production could be 800,000 barrels a day higher than current levels. In one year, that would be four times the amount of oil the Democrats are now proposing to be released from the Strategic Petroleum Reserve.

Americans and our economy need an energy plan now. And the Democratically controlled Congress is blocking all attempts to increase production. This summer, the House and Senate have refused to bring an Interior appropriations bill to the floor. For that matter, they've pretty much refused to bring any appropriations bill to the floor. This would provide an opportunity to lift the moratorium for drilling on the Outer Continental Shelf. And Democratic Leader Reid has even cancelled action on what he calls a stimulus bill just in order to block any debate on energy production amendments.

I'm quite sure that there will be people who criticize this report, they'll criticize the President, or they'll probably try and just focus attention on the big size of the numbers. And I hope that if they do that you will ask them to present a realistic and detailed budget plan, or at least inform the taxpayers of this country when such a plan will be enacted into law.

The President presented such a detailed budget plan six months ago, to meet the country's needs in a fiscally responsible manner and promoting growth for our economy. Unfortunately, Congress so far has failed to pass even one bill to begin the annual budget process. And I'm informed that there are now only 19 legislative days left in the fiscal year when they can even meet and pass such a plan.

I will now turn to the Chairman of the President's Council of Economic Advisers, Dr. Ed Lazear.

CHAIRMAN LAZEAR: Thank you, Jim. I'd like to talk to you today about our forecast. GDP is forecast to grow at 1.6 percent this year. We believe that this forecast is realistic and consistent with others from both private and

government forecasters. It is clear that 1.6 percent growth is below the average for the United States, but the positive growth that we are forecasting for 2008 reflects the resilience of the American economy in the face of significant shocks.

The economic stimulus that the President signed in February is a contributing factor to forecasts that sustain positive growth. Headline inflation is expected to moderate over the next few months, which should bring the rate for 2008 to around 3.8 percent. The 2009 inflation rate should be considerably lower, and we are forecasting 2.3 percent. Much of this reflects expectations that increases in energy and food prices that we saw this year will not be repeated. GDP price inflation will be significantly below headline levels at 2.2 percent.

The 1.6 percent GDP growth number is revised down from 2.7 percent that we forecast last autumn. There are three primary reasons. First, the rapid rise in oil and other commodity prices has put downward pressure on the economy. Second, tightness and reorganization of credit markets has affected business investment and other forms of borrowing. The extent of the credit market problems that materialized over the first half of 2008 were not built into the autumn forecast. Finally, housing has continued to be a drag on the economy and has subtracted more from GDP than was expected. Offsetting these drags on GDP growth is the expansion of exports, which has contributed significantly to the positive growth we have seen in recent quarters.

The unemployment rate is expected to remain close to its current levels into 2009. Although these levels are elevated relative to the last couple of years, they are not high by historic levels and are currently below the average for the 1990s. Unemployment rates should decline thereafter, eventually reaching what we believe to be long-run sustainable levels of 4.8 percent.

Interest rates, which are currently low, are forecast to revert to their long-term levels over time. This employs -- I'm sorry -- implies that the forecasted rate of 4 percent for 10-year Treasury notes will eventually rise to 5.3 percent, consistent with our inflation forecast and with historic relationships.

All forecasts are subject to uncertainty, and this one is no exception. We believe it reflects the best information and statistical methods available, and we have confidence that it provides accurate estimates of the key variables.

Thank you. We'd like to take your questions now.

Q Mr. Lazear, do you have an estimate of what the growth rate would have been without the stimulus package?

CHAIRMAN LAZEAR: We don't actually provide an estimate of what it would have been without the stimulus. And in fact, we don't break out the estimates quarter by quarter, as you know, we just give an annual estimate. We have seen indications that the stimulus is working. We're quite confidant that we made the right move back in January, when the President proposed the stimulus package. We did it for insurance reasons. We believe that it was a wise purchase. And we have seen some reflection of the stimulus in spending patterns of consumers over the past month or two. So there is indication that it is working, and we expect it to continue to work into the next couple of quarters.

Q Gentleman, the AP reports that you've left out war costs, and that violates new mandates in Congress. Is that correct?

DIRECTOR NUSSLE: We did not leave out war costs. In fact, we build in -- and we built into the budget for this year $70 billion for 2009. We certainly understand that may not be the full cost of the war. That number is still being developed by the Department of Defense, and when it is available and when it is developed, then it will be presented to the President for a decision about whether or not that is appropriate and needs to be sent up.

But we've made it very clear that we did not want to tie the hands of the next commander, that we wanted to provide flexibility to the next Commander-In-Chief. The $70 billion we estimate will provide funding for the global war on terror through -- we believe at this point in time, through late spring, possibly early summer, depending on how the Congress develops -- or if they pass an appropriations bill for the Department of Defense this year, or whether we have to live under a CR.

So there is some, I suppose, uncertainty based on how they decide to proceed. But the President has decided that the best way to not only ensure that we have funding through the next administration is to provide that $70 billion. And Congress put that into the supplemental that they passed back in late June.

Q   Just to follow up, are you violating congressional mandates by not including certain other war costs in this report?

DIRECTOR NUSSLE: No, we don't believe we are. In fact, Congress has chosen to take on the costs of the war in a piecemeal and a very delayed format. The President, in the most recent iteration of this, had a request for funding for the global war on terror that languished out there for more than a year before Congress even addressed it. Congress held hearings on it, but never even took it to the floor. So it's Congress that is choosing the path here of not addressing the cost of the war, not building it into their own budgets. In fact, they have built in the exact same amount into their budget that the President has built in. So Congress has chosen to take this on in a piecemeal approach, and as they do that, the President needs to respond in kind.

Q   Within the budget, it said that the economy can absorb high energy prices. Given where energy prices are right now, $130, roughly, for a barrel of oil, can that be indefinitely sustained as far as the economy being able to absorb that, or will prices have to go down in order for there to be economic growth in the future?

CHAIRMAN LAZEAR: We know that every time oil prices go up it takes off some growth from our economy. So we estimate that every $10 or so per barrel of oil costs us anywhere between a quarter of a point to .4 percentage points of GDP. So, obviously, what that means is that it does have an effect. It has an effect -- a continuing effect on the economy.

The reason that the economy has continued to grow throughout this period is because productivity has grown enough to offset those high energy costs. And what's happened over the past few years is that increasing productivity growth has meant that we've been able to lower

our costs of doing business, which in large part is responsible for the competitiveness of our export business, as well, and that has offset these energy costs.

That doesn't mean it doesn't cost us anything. Obviously when we see energy prices going up it does mean a drag on the economy. We've just been able to get through it because other things have been sufficiently positive to offset it.

Q Dr. Lazear, can you talk a little bit about what you're expecting for economic growth in 2009, and why you're seeing this big jump in the budget deficit over the February forecast in 2009 -- how much that has to do with the stimulus package, and how much it has to do with the much lower growth than you were expecting?

CHAIRMAN LAZEAR: I'll defer to Jim on the budgetary question, but I can certainly tell you about 2009. We're predicting 2.2 percent for 2009. We believe that that is a realistic forecast, that we should be back on track --

Q And what was it in February? I'm sorry. In February, what were you forecasting?

CHAIRMAN LAZEAR: In February -- oh, you mean our last forecast for that was 2.9 percent was our -- no, no, I'm sorry, that's not right. Fall was 3.0 -- 3.0. So we've revised it down, again for the same factors that I mentioned in my opening: energy prices, credit and housing.

Again, our hope is that we will be through most of the issues that are plaguing those markets right now and that we won't see continued increases in energy prices. We hope that those prices will stabilize or perhaps even fall. If they do, that will be a boost to the economy. The housing market bottoming out will also be a boost to the economy, as well, and we hope that that will happen sooner rather than later.

Again, we believe these forecasts are realistic. They are in line with the kinds of forecasts that you're seeing both among private forecasters and in other government agencies, as well, so we don't think this is a rosy scenario in any way, we think it's a realistic scenario.

Q The report says that the data was compiled from June statistics. You've had a number of bad economic indicators -- Fannie Mae and Freddie Mac have happened since then. Does that cause you to revise your thinking at all?

CHAIRMAN LAZEAR: Well, there’s always new information that come in weekly. We also had some good ones last week. We had a durables number that was pretty strong, and there have been a number of other indicators that seem strong. We'll get GDP numbers on Thursday. Obviously once we know the actual number for GDP in the second quarter that would be additional information that would affect our estimates, as well.

The problem is you always have to choose some point at which to draw the line and base your forecast at that point, and that's what we did. It was the best information we had at the time. Whether new information would have had any significant impact on that, I doubt that it would be significant. But obviously all new numbers do have an impact on the forecast.

Q In the Mid-Session Review, as in the February budget, corporate income tax corrections are lower each year from 2008 to 2011 than in 2007. Can you explain why that is?

CHAIRMAN LAZEAR: Than in 2007? Yes, I'd have to check on that. I can't give you an answer to that off the top of my head.

DIRECTOR NUSSLE: But a big part of it is as a result of the softening of the economy. I mean, that part of it is obvious. But exactly how that figures, we can check on it and get you more detailed answer.

CHAIRMAN LAZEAR: I'd want to make sure before I give you any specifics that you're going to quote. We can certainly get back to you on that.

Q How do you get back to balance and a surplus in 2012, as quickly as you did when you were estimating a $407 billion deficit for next year --

DIRECTOR NUSSLE: Well, I mean, I acknowledge --

Q -- robust recovery.

DIRECTOR NUSSLE: And I acknowledge in my statement that this is going to be a challenge, particularly given the atmosphere on Capitol Hill to spend more. Most of the bills, most of the proposals on the Hill have been to spend more, have been to obligate more. It's going to be a challenge, particularly given the fact that if you see more tax increases that could slow the growth and the economy. These are all challenges that need to be factored in.

So we acknowledge, both because of the small changes since the MSR was finished, as well as what we have not yet seen in the 19 days -- 19 legislative days that remain for Congress in this fiscal year, there are a number of pressures. Most of those pressures are upward pressures on the deficit, not downward pressures. And each one of those, every dollar that is added to that bottom line makes it more difficult and takes away the cushion that we have in 2012 and '13. We do have some cushion, but not enough to squander that with excessive spending programs.

Q In May, the Treasury survey of the primary dealers in public debt who keep very close track of the deficit, as well, estimated that it's going to be about $414 billion, and you guys are at $389 billion now. Historically, OMB has seemed to sort of over-project deficits in the MSR traditionally. I'm just curious as to where you think the likelihood and the probability is of seeing a record deficit for '08, as opposed to --

DIRECTOR NUSSLE: Well, we're giving you the projection as we know it today. I acknowledge, as I did in my statement, that there have been some changes, albeit not too significant, since the MSR has been put to bed. I think the biggest challenge will be as we see how Congress decides to end the year, so to speak, and begin the next fiscal year. There is enormous pressure for additional spending. There's talk of all sorts of legislation in addition to the regular appropriation process that has not even begun yet. All of those -- again, dollar for dollar -- add to the pressure, to the bottom line, whether it's projecting the deficit for the end of this year, or to the '09 deficit and beyond.

Q So you don't think that a record is possible this year?

DIRECTOR NUSSLE: Well, again, the record -- it's always interesting, you see these statements about this is a record deficit, or however it is. I mean, you can only compare these very large numbers against something. And I think it's acknowledged by most economists, as well as by most leaders both in the Congress and the administration, that the best way to compare a deficit is by your ability in the economy to manage that deficit. And so comparing it to GDP is the best way to be able to decide whether or not a number is big or not.

We are not happy about the deficit. It is slightly higher than the average of the last 40 years. We have a plan to address that deficit and bring it down, which I think is a responsible one. We call on Congress to both adopt one, as well as enact one, and to do so in a fiscally responsible way so that we can stay on track. But certainly there are a number of pressures out there that could, and will, add to the deficit bottom line if, in fact, we don't keep control over them.

Q   I was wondering if you could address how you are accounting for the AMT in the out-years, 2010 onward. Do you make an assumption that there will be an AMT fix, or no?

DIRECTOR NUSSLE: Well we patch the AMT, as you probably know, for the budget that we're currently trying to enact for 2009. The President believes that we should not patch the deficit -- or patch the AMT -- that rather we should enact AMT reform as part of a comprehensive tax reform. So while he has patched it in years past, made the determination that it should not be patched going forward, and that it should be part of a tax reform debate and, in fact, may be the, I guess you could say the energy that spurs the tax reform debate, and should, because it's a tax that needs to be reformed. And the President has a longstanding policy to do that. So that's how the President addresses it within this budget.

Q   So from 2010 onwards, there is no --

DIRECTOR NUSSLE: No.

Q   You're assuming that those revenues would flow in?

DIRECTOR NUSSLE: We're assuming that Congress would not be able to withstand the pressure much longer, and will finally address tax reform.

Anything else? Yes.

Q You mentioned how you're pretty happy with the results or you're seeing some benefits from the first stimulus, and you talked about spending -- potentially the second stimulus package. Maybe it's too early to say, but what are your feelings about a second stimulus getting through Congress at some point --

DIRECTOR NUSSLE: Well, I think what's peculiar about the talk of a second stimulus is that as -- Dr. Lazear spoke of and I think many have spoken of having a comprehensive energy package that deals with production. The President has laid out a four-step plan in order to accomplish a number of the challenges that -- to meet some of the challenges that we need in oil production and energy production. And rather than take that on, which would be quite stimulative to the economy, it appears that Congress is talking about -- we haven't seen anything yet that has been announced, but because we're getting closer and closer to election day, the proposals we hear about sound a lot more like election stimulus, or political stimulus, than it does economic stimulus, which is not all that surprising, as close as we are to election time.

What's also interesting is that there seems to be some rush to consider so-called stimulus, albeit possibly political stimulus, when the rest of the appropriations process has not yet been tackled, again, a peculiar situation and one that has not been seen for -- in modern time. It was before I was born the last time Congress has not adopted an appropriation bill, even taken it to the floor, by this time in the session. So it's a very strange, peculiar thing to watch why Congress is so interested in stimulating the economy so-called, and yet there is basically inaction on the floors.

Q According to a GAO report, the unfunded liability to Medicare Part D will be about $8 trillion over the next 75 years. Does that mean the prescription drug coverage was a bad idea or a feasible one from a budget perspective --

DIRECTOR NUSSLE: Well, actually, as we have projected, as we've seen the actual numbers come in with regard to the prescription drug benefit, the actual cost over the projected cost when it was first passed has come down significantly. I believe the projected cost was about $630 billion. It is now down to, I believe, based on the actual trend rate and how it's been used, we're in the $400 billion range. So it has not had the kind of projected cost that many had thought it would when it was first enacted. So actually that has been generally some very positive news and provided a good benefit for seniors who needed to have prescription drugs as part of a modern health benefit under Medicare.

So we believe that's generally been positive news within this not only MSR, but generally within the fiscal condition of the country. That is not to suggest the GAO is not sounding an appropriate alarm with regard to the unfunded liability for the entitlements. And this is true across the board when it comes to, now, two-thirds of the budget. This is probably one of the more disappointing parts of what Congress is basically not doing, and, in fact, just turned off, or is proposing to turn off the so-called trigger mechanism from Medicare.

This all I think bodes very poorly for our ability as a country to deal with some of these entitlements. The President, in his budget, begins to address this unfunded liability. He does it by thirds. He basically says, let's tackle this in bite-size chunks, if you will, taking on a third in this budget, and then proposing to do so again in the future before they become insolvent. And those are I think positive ways to address the unfunded liability that GAO speaks about. I wish Congress would listen to GAO.

So, we'll see. Yes.

Q You talked about Congress not finishing its appropriations bills. Congressional leaders are saying they'll pass a CR into the next presidency. Would President Bush sign that, or will he insist that Congress come back after the election to finish the appropriations work?

DIRECTOR NUSSLE: Well, it's disappointing I think to me and I believe it's going to be disappointing to the American people that they're going to continue to draw a

full year's salary and basically wait until next year to do any work. That to me seems like -- as though they're not doing the job that they signed up for. We understand that the Congress is basically gambling on the election, betting that they can get a better deal from the next President.

I hope the next President takes a look at this MSR, takes a look at the fiscal condition, and realizes that increasing taxes is not an answer, spending your way into prosperity -- government spending in particular -- is not an answer, and continuing to ignore the entitlement challenges is also not an answer. From what I read from what Congress is doing, they're going to basically ignore this until the next President comes here. That I believe is something they're going to have to be accountable for, not the President.

Q So he would sign a CR that bypassed --

DIRECTOR NUSSLE: Until we have a chance to see what a CR looks like, a continuing resolution looks like -- Congress still has 19 days in which to do some work and make some determination of how they're going to address this fiscal year. If it's true they're going all the way until next March or April, I have a feeling that the American taxpayers may have something to say about that.

Q Can you speak a little bit more about what you're sending to the Hill today -- the budget and the Outer Continental Shelf?

DIRECTOR NUSSLE: What we're doing, and we'll -- I think probably the best way to do that is to give you a copy of the amendment, let you have a chance to take a look at it -- but what we are doing is we are conforming the budget proposal itself to what the President has announced as part of his energy plan. And we're calling on Congress to adopt that. Congress, as you know, has a moratorium within their appropriation bill, and we're asking them to drop that moratorium. And that's the budget amendment that we're sending forward.

So, time for -- we'll come back to two more real quick and then we'll be done. Yes.

Q Just real quick, to get back to the CR. What would the absence or presence of congressional language

extending the offshore moratorium do to the changes of a CR being signed?

DIRECTOR NUSSLE: Again, at this point in time, it's speculating, and I think what we'd like to do is take a look at, work with the Congress to see if, in fact, they're only going to send a continuing resolution. It's been a tradition in those situations for it to be clean -- so-called clean CR, but there are many things they may want to add, may want to subtract. We would have to take a look at that before we could give any advice to the President.

Last one.

Q Do you care to respond to the Democrats generally -- they say the President came into office with a record surplus, and leaves office with a very big deficit, and as Senator Conrad says, he'll be remembered as the most fiscally irresponsible President?

DIRECTOR NUSSLE: It's always interesting to me how eight years can be boiled into one sentence like that, or as I suggested in my statement, that people will somehow compare one number to a next and assume it's the entire part of the story. I am somewhat amazed that there are those who continue to claim that the President inherited a surplus and assume that that in and of itself is the end of the story.

The President had, I think, a number of challenges when he came in, not the least of which was a recession. He had an underfunded military -- in fact, was running a deficit when it came to our ability to respond to homeland security and international intelligence and making sure that our country was protected. So while, mathematically, there may have been a surplus, there were many underlying deficits that the President had to deal with that became manifest on September 11th and beyond.

So the President, together with Congress -- which is also, I think, interesting that they forget their part of this last eight years -- decided to make some very important adjustments to spending -- not only in order to build a new Department of Homeland Security, but to deal with those deficits in national security, homeland security, and intelligence; also to make sure that we reduce taxes to keep the money in the pockets of small

businesses and individuals so that they could spend the money in order to help get us out of the recession that the President inherited.

There are a number of things -- that's just the first two years; I could go on. But there's much that happens between the first day the President took office and today when we talk about where we stand.

What we do know is, going forward, we have to keep the country strong. We cannot under-fund many of these important security programs in order to somehow get back to balance. The best way to get back to balance is to control spending in the domestic discretionary side of the ledger, to reform the entitlement spending, and to keep taxes low to make sure that economic growth continues to see the kind of receipts to the Treasury that we have seen, particularly during the time the President was in office.

So there's much more to the book, if you will, than the first page and the last page. There are many, many pages and chapters in between. And it's interesting that the Democrats seem to have not read all of them. They seem to want to skip to the last page and try and tell the story, and that's not going to work.

Thank you very much.

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2:13 P.M. EDT