Budget deficit tops $1 trillion for first time

Federal budget deficit tops $1 trillion for first time, could reach $2 trillion by fall

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WASHINGTON -- The federal deficit has topped $1 trillion for the first time ever and could grow to nearly $2 trillion by this fall, intensifying fears about higher interest rates, inflation and the strength of the dollar.

The deficit has been widened by the huge sum the government has spent to ease the recession, combined with a sharp decline in tax revenues. The cost of wars in Iraq and Afghanistan also is a major factor.

The soaring deficit is making Chinese and other foreign buyers of U.S. debt nervous, which could make them reluctant lenders down the road. It could also force the Treasury Department to pay higher interest rates to make U.S. debt attractive longer-term.

"These are mind-boggling numbers," said Sung Won Sohn, an economist at the Smith School of Business at California State University. "Our foreign investors from China and elsewhere are starting to have concerns about not only the value of the dollar but how safe their investments will be in the long run."

The Treasury Department said Monday that the deficit in June totaled $94.3 billion, pushing the total since the budget year started in October to $1.09 trillion. The administration forecasts that the deficit for the entire year will hit $1.84 trillion in October.

Government spending is on the rise to address the worst financial crisis since the Great Depression and an unemployment rate that has climbed to 9.5 percent.

Congress already approved a $700 billion financial bailout for banks, automakers and other sectors, and a $787 billion economic stimulus package to try to jump-start a recovery. Outlays through the first nine months of this budget year total $2.67 trillion, up 20.5 percent from the same period a year ago.

There is growing talk among some Obama administration officials that a second round of stimulus may eventually be necessary.

That has many Republicans and deficit hawks worried that the U.S. could be setting itself up for more financial pain down the road if interest rates and inflation surge. They also are raising alarms about additional spending the administration is proposing, including its plan to reform health care.

President Barack Obama and Treasury Secretary Timothy Geithner have said the U.S. is committed to bringing down the deficits once the economy and financial sector recover. The Obama administration has set a goal of cutting the deficit in half by the end of his first term in office.

In the meantime, the U.S. debt now stands at $11.5 trillion. Interest payments on the debt cost $452 billion last year -- the largest federal spending category after Medicare-Medicaid, Social Security and defense.

The overall debt is now slightly more than 80 percent of the annual output of the entire U.S. economy, as measured by the gross domestic product. During World War II, it briefly rose to 120 percent of GDP.

The debt is largely financed by the sale of Treasury bonds and bills.

Many private economists say the administration had no choice but to take aggressive action during the financial crisis.

"We have a deep recession hammering tax revenues and forcing the government to provide a lot of help to the economy," said Mark Zandi, chief economist at Moody's Economy.com. "But without this help, the downturn would be even more severe."

History shows the dangers of assuming too soon that economic downturns have ended.

President Franklin D. Roosevelt made that mistake in 1936. Believing the Depression largely over, he sought to reduce public spending and to balance the federal budget, but that undermined a fragile recovery, pushing the economy back under water in 1937.

Japanese leaders made a similar mistake in the 1990s when they temporarily withdrew government stimulus spending, prolonging Japan's recession into one that lasted a full decade.

Republicans in Congress are seizing on the deficit -- and the persistence of the recession -- to attack Democrats.

"Washington Democrats keep borrowing and spending money we don't have," said House Republican Leader John Boehner of Ohio.

So far, interest rates have remained low.

This is partly because the Federal Reserve has kept a key short-term rate at a record near zero. Also, all the economic troubles in housing and the rest of the economy have depressed demand for credit by the private sector, meaning the government's borrowing costs are relatively low.

The benchmark 10-year Treasury security has risen by about a percentage point in recent weeks, but analysts note it is still trading at historically low levels of around 3.35 percent.

Geithner travels later this week to Saudi Arabia and the United Arab Emirates, where he is expected to face questions about the U.S. deficit. As he did during a visit to China last month, Geithner will try to reassure investors in the Middle East that their U.S. holdings are safe from a calamitous bout of inflation.

The deficit of $1.09 trillion so far this year compares to an imbalance of $285.85 billion through the same period a year ago. The deficit for the 2008 budget year, which ended Sept. 30, was $454.8 billion, the current record in dollar terms.

Revenues so far this year total $1.59 trillion, down 17.9 percent from a year ago, reflecting higher unemployment, which cuts into payroll taxes and corporate tax receipts.

Under the administration's budget estimates, the $1.84 trillion deficit for this year will be followed by a $1.26 trillion deficit in 2010, and will never dip below $500 billion over the next decade. The administration estimates the deficits will total $7.1 trillion from 2010 to 2019.

http://finance.yahoo.com/news/Budget-deficit-tops-1-apf-1385745052.html?x=0&sec=topStories&pos=1&asset=&ccode=