The U.S. federal government budget balance has deteriorated for a third year in a row, according to the results for the 2018 fiscal year ended September 30. This brings the deficit to US$779 billion from US$666 billion in 2017 (graph 1). The 2018 deficit represents 3.9% of real GDP compared with 3.4% in 2017.

This further decline comes as no surprise. As expected, the tax cuts passed at the end of last year had a considerable effect on public finances. Revenues from corporate tax plunged 31.1% from the year before, deepening the deficit by US$92.3 billion. However, this was offset by the 6.1% rise in revenues from personal tax. Expenditures were up 3.2% from 2017, including an annual US$64.6 billion increase (+14.1%) for debt service.

The fiscal issues stem mainly from the past and recent budget choices made by the White House and Congress. Normally, at this stage in the economic cycle, with a very low jobless rate, the economy should allow the federal government to clean up its finances (graph 2). In 2000, when the economic situation was similar (jobless rate at 4.0%), revenues accounted for 20.0% of GDP. In 2018, that proportion is 16.5%. The ratio for expenditures in 2000 was 17.6%, but has since climbed to 20.3%.

**IMPLICATIONS**

If the federal government cannot improve its public finances in such a favourable climate, it is difficult to tell when it might be able to do so without painful policy decisions. It could be argued that the strong economic growth is a consequence of policies implemented over the past year. However, even with this in mind, the cost on public finances should be recognized. In a context of rising interest rates or a potential end to the cycle, the situation might prove even more problematic.