United States Senate
WASHINGTON, DC 20510–6200

February 15, 2022

Dr. Phillip Swagel
Director
Congressional Budget Office
United States Congress
Washington, DC 20515

Dear Director Swagel,

Inflation substantially increased and accelerated throughout 2021, and has been harmful to American households and businesses.

Year-over-year growth in consumer prices, as measured by the consumer price index (CPI-U), rose to a staggering 7.5 percent in January, from 1.4 percent in January of last year, and from an average of 1.9 percent between the beginning of 2017 and the beginning of 2021. Consumer price inflation, measured either by the CPI or the Personal Consumption Expenditures price index, has accelerated to highs not seen in 40 years.

Signaling that more price inflation will face households and businesses moving forward, producer price inflation has also accelerated to record highs. Year-over-year growth in producer prices, as measured by the Producer Price Index, rose to a record-high 9.8 percent late last year, from 1.6 percent in January of last year, and from an average of 1.8 percent between the beginning of 2017 and the beginning of 2021.

Without doubt, in 2021, we went from a long period of low and stable inflation to persistent and accelerating inflation that is harming workers, households, and the economy. Inflation is also acting like a stealth tax, eating away at the purchasing power of Americans' paychecks.

While many did not foresee runaway, persistent, and accelerating inflation over the course of 2021, others did, especially in light of the American Rescue Plan Act which, according to CBO, will increase estimated outlays by $1.8 trillion over the 2021-2030 period and increase the estimated deficit by $1.9 trillion, measured against a budget baseline which assumed far lower inflation than was realized last year.[1]

Increased inflation leads to more federal spending and more federal revenue. The added revenue stems partly, and unfortunately for taxpayers, from nominal inflationary gains that do not show up as purchasing-power-adjusted gains for federal taxpayers. The stealth-like nature of inflation taxes, and revenues that flow from them, should not be viewed as an economic plus.

Efforts by the Federal Reserve to slow the rate of inflation by raising interest rates can have painful economic consequences, driving up the cost of both public and private sector borrowing.

[1] "Estimated Budgetary Effects of H.R. 1319, American Rescue Plan Act of 2021," March 10, 2021 cost estimate at https://www.cbo.gov/publication/57056 .

As history has shown with the Federal Reserve under Chairman Volker, once inflation is out of hand, taming inflation can be temporarily devastating to the economy.

A budget workbook on CBO's website suggests that a persistent one percent inflation increase above CBO's baseline projection made early last year could increase deficits by nearly $2.3 trillion over a 10-year period.[2] And, according to the workbook, a one percent increase in interest rates above CBO's baseline projection, beginning in 2022, could increase deficits by more than $2.1 trillion over a 10-year period.[3] While those results are only approximations of what CBO would project using its broad set of economic and budget models, they are indicative of significant adverse budgetary effects amounting to trillions of taxpayer dollars arising from higher sustained inflation and interest rates moving forward.

Adverse effects of inflation on the federal budget, including likely increased payments to service outstanding debt, absorb fiscal space and crowd out a host of national priorities, ranging from low-income support programs to national defense to disaster relief.

Given the potential for significant adverse budget effects from inflation, we ask that CBO provide a discussion of those effects. Please provide a description of budgetary effects of: high inflation; inflation that persists; and, higher interest rates that can result from high inflation and possible Federal Reserve responses to inflation.

We look forward to your responses, and appreciate the hard work performed by analysts at the CBO.

Sincerely,

Mike Crapo
United States Senator

Charles E. Grassley
United States Senator

John Cornyn
United States Senator

John Thune
United States Senator

[2] $2.267 trillion obtains as the deficit increase over the 2022-2031 period relative to CBO's baseline upon increasing inflation relative to CBO's February 2021 baseline in each year 2021-2031 in Tab 4 of the workbook at [Workbook for How Changes in Economic Conditions Might Affect the Federal Budget, June 2021 | Congressional Budget Office (cbo.gov)]

[3] $2.125 trillion obtains as the deficit increase over the 2022-2031 period relative to CBO's baseline upon increasing the assumed interest rate on 10-year Treasury notes relative to CBO's February 2021 baseline in each year 2022-2031 in Tab 3 of the workbook cited above.

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