When something is balanced, it is evenly distributed on all sides. When you’re talking about a budget, it means income equals expenses. In other words, you don’t spend more than you make.

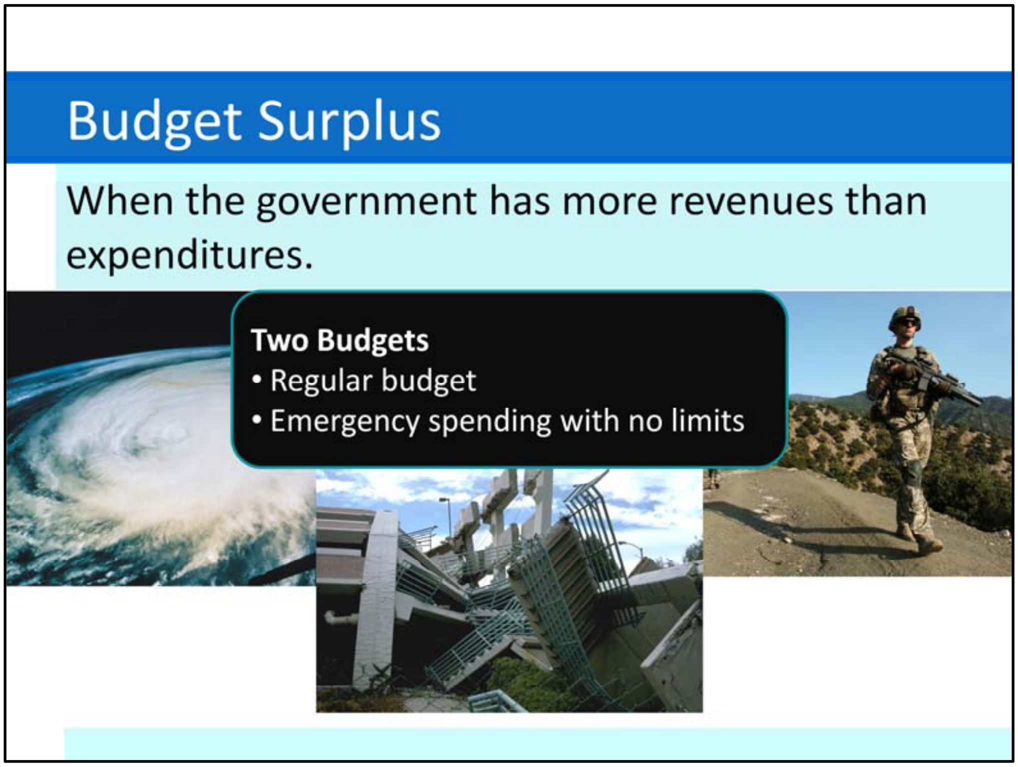
When you create budget, you have to balance what you’d like with what you can afford. Let’s see how well you can do this.

Just like consumers, the government has to balance its income with its expenditures.

How does the government get revenues to pay for the things it does? It collects taxes.

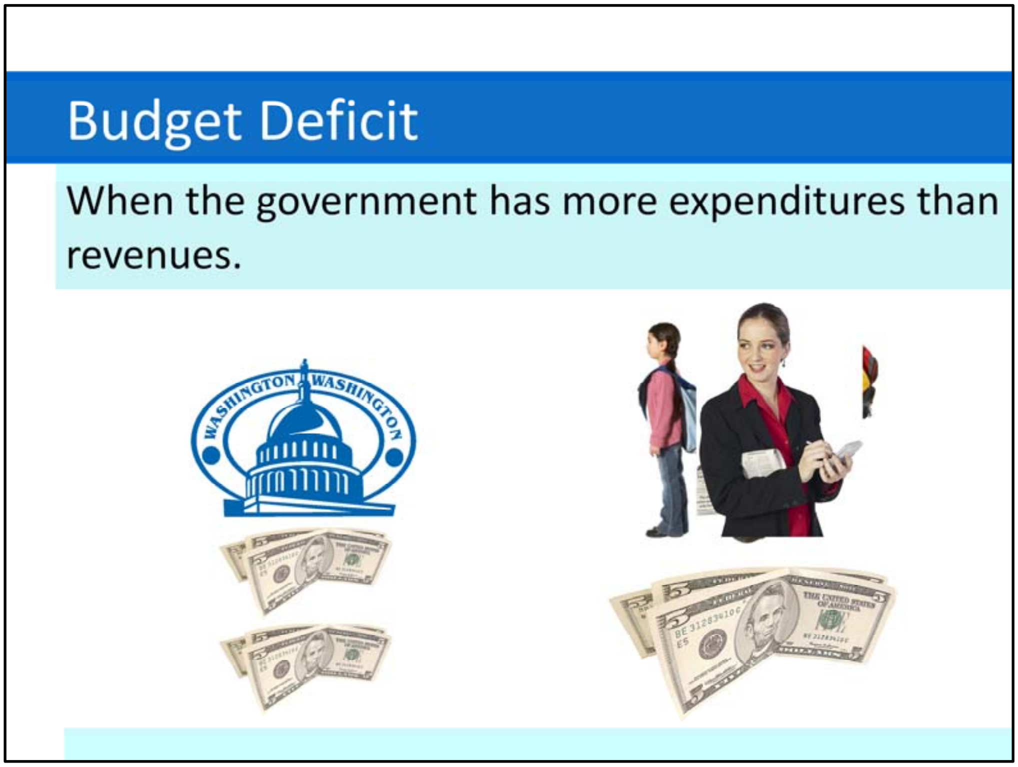
How does the government plan its expenditures? Every year, it creates the federal budget, which is its plan for spending federal revenues. The budget is prepared by the Office of Management and Budget after estimating how much income the government will receive for the year and evaluating the spending requests it receives from all federal departments and agencies.

This office sets aside money for specific purposes, like fixing highways or building a new battleship. This money is called appropriations. When every dollar coming in equals every dollar being spent, the budget is balanced.



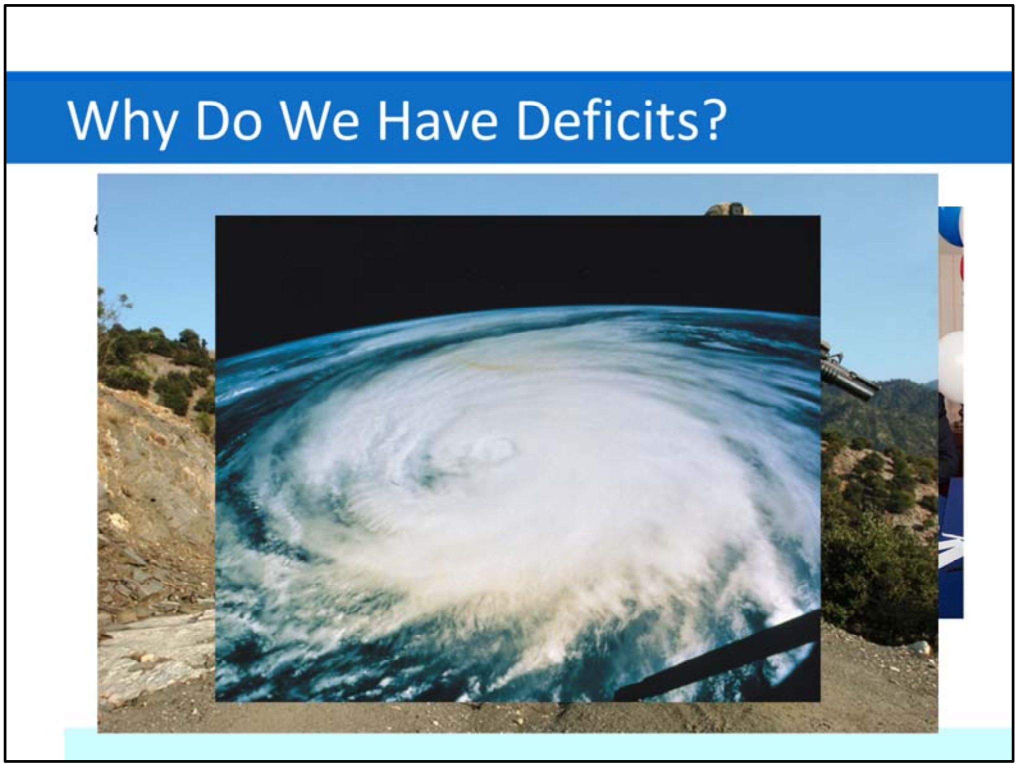
What happens if the government brings in more revenues than it spends during a year? This is called a budget surplus. It doesn't happen very often. Since the Great Depression, our government has had only a few years of budget surpluses.

Some states have laws that require the state government to balance the budget every year. They are not allowed to spend more than they make. Our federal government does not have this restriction. In 1990 the Budget Enforcement Act was passed which attempts to limit the government's ability to spend more than it collects in taxes. This act did not, however, take into account unforeseen disasters, like war, hurricanes, and earthquakes. As a result, today our government has two budgets – the regular budget and another one for emergency spending, which has no limits.



When the government spends more than it collects in revenue during the year, this is called a deficit.

How does the government do this? Basically, the government borrows and expects future taxpayers to repay the loans. This is called deficit spending. Does the government borrow money from banks like you and I do? No, the government sells U.S. government securities such as bonds. When businesses, individuals, and foreigners buy these bonds, they are lending the government money for a certain period of time, after which, they'll be paid back with interest.



Since the Great Depression, the federal government has been in deficit eighty four percent of the time. Why? Well, one reason is that voters want government programs like Social Security and Medicare. All of these programs cost money. Voters also like tax cuts. They want to pay less money in taxes every year.

Politicians want people to vote for them, so they often promise to give voters lower taxes and keep the spending programs that voters like.

Wars can also cause deficits. The government has to spend more money on military salaries and equipment during wartime. National emergencies, like when Hurricane Katrina hit New Orleans, can also cause deficit spending. The need for public goods and services—such as highways, dams, and airports—also increases spending. You learned earlier that sometimes the government also spends money to stimulate the economy. All of this spending has its benefits, but it is very costly to the federal budget.

Are Deficits Always a Bad Thing?

Borrow money to stimulate the economy and make it grow.
Leads to higher tax revenues in the future.

Is deficit spending always a bad thing? Some economists argue that it's necessary sometimes to borrow money to stimulate the economy so that it will grow, and the government will have higher tax revenues in the future as these businesses grow.

Obviously, you can't run large deficits forever and hope that people will keep lending you money, since you may not be able to pay these debts some day. Whether governments should have debts or not, and how big those debts can be before they are a problem is a hotly debated topic among economists, politicians, and voters. When you begin to vote, you'll find you'll have to make some of the same difficult decisions about cutting taxes or services.

So we know that most of the time, the government borrows money to finance all of its spending. When does it pay back the loans?

Believe it or not, the federal government rarely pays off its debt. When the bonds mature and are due to be repaid, often times the government sells more bonds pay off the investors who are cashing in their bonds. Nearly half of the national debt is refinanced every year.

When interest rates rise, the cost of the federal debt rises also because the government has to pay more interest on its loans. Our federal government owes trillions of dollars. This is what is known as the national debt. To calculate the actual amount of the national debt, economists first add up all of the yearly deficits. Then they add up all of the yearly surpluses. The total deficits minus total surpluses equals the amount of the national debt. Every year the government has a deficit, our national debt grows.

Americans aren't unique. Most of the countries in the world also have a national debt for many of the reasons that we do: people want services, but they don't always want to pay for them.