WebMemo
Published by The Heritage Foundation

No. 1325
January 23, 2007

State of the Union 2007: Fiscal Policy Challenges for Today and Tomorrow

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President Bush's remarks in his State of the Union address on the economy and fiscal policy spoke of mixed past success. The Bush tax cuts are successful policy changes—especially the rate reductions on capital gains and dividends and the marginal income tax rate that have led to a strong economy and surging revenue growth. They have helped to meet the President's goal of cutting the deficit in half. However, as important as these surging revenues have been as a testament to pro-growth tax policy, they are only half of the deficit equation. If spending had grown only at the same rate as the economy, the nation would be near surplus today.

The President pledged to continue to work on the deficit, proposing eliminating the deficit by 2012 as his goal. To meet this goal, the President rightly called for spending discipline. He also clearly took tax increases off the table to meet this goal—also the right move. A focus directed solely on the deficit misses more important questions because it does not examine the level or trends of government spending or taxation. High levels of both are damaging to the economy, and a narrow focus on the deficit makes it only too tempting to raise taxes. America could have a balanced budget today, but if it took 100 percent of the economy, Americans would be much worse off than today.

Balancing the budget through spending discipline, not tax cuts, is a common-sense fiscal goal. After all, families and businesses balance their budgets every day. But balancing the budget by 2012 is pointless goal, like digging a moat around a sand castle when a tsunami is approaching. Much more is necessary. According to the Congressional Budget Office, spending on the big three entitlements—Medicare, Medicaid, and Social Security—is projected to rise from just over 8 percent of GDP today to almost 19 percent in 2050. This spending will crowd out every other program in the federal budget—including defense—and push taxes past the historical tax burden of 18.3 percent of GDP. This tsunami is not so far away either. It will start in 2008 when the first baby boomers retire and the huge tidal wave of spending that will swamp the federal budget starts to come our way.

That makes the President's call to fix Medicare, Medicaid, and Social Security all the more urgent. As the President noted, unless these programs are changed soon, Americans will ultimately face grim choices of huge tax increases, huge deficits, or huge and immediate benefit cuts that will hit today's younger generations squarely in the prime of their working years. Though no specifics were laid out in the State of the Union, tough choices will be necessary. Congress and the President should begin a seri-

This paper, in its entirety, can be found at:
www.heritage.org/research/budget/wm1325.cfm

Produced by the Thomas A. Roe Institute
for Economic Policy Studies

Published by The Heritage Foundation
214 Massachusetts Avenue, NE
Washington, DC 20002–4999
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The Heritage Foundation

ous bipartisan conversation about reforming these programs and reining in this huge spending wave before it overtakes our younger generations.

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