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President Obama's Budget: What to Watch For

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The President's post-debt-ceiling, election-year budget will provide a good test of whether he is serious about facing up to the country's looming fiscal crisis and driving spending down. At this critical moment for the nation's fiscal and economic health, he should seize the opportunity to change the course of fiscal policy.

No one expects President Obama to transform into a conservative. But he cannot ignore the fundamental problems of runaway spending and debt, and he can no longer turn these problems over to fiscal commissions or super committees. If his budget for fiscal year (FY) 2013 is to be a credible policy document—not just a public relations pitch—it should:

- Show specific proposals for reforming entitlements and reducing other spending not just for the next 10 years but over the long term as well;
- Prevent the devastating cuts in defense that are looming because of the debt-reduction Budget Control Act;
- Offer permanent solutions to the large spending and tax policies that keep vexing lawmakers and the public; and
- Reject phony budget savings and other gimmicks.

The Outlook. The Congressional Budget Office (CBO) analysis of the President's budget last year¹ showed the President's proposed spending rising inexorably to a post-World War II record of 24.2 percent of gross domestic product (GDP) in 2021,

more than twice the peak level as a share of the economy during the New Deal. His projected deficits would dip slightly in mid-decade but return to more than \$1 trillion in 2019 and beyond. His proposal would drive debt held by the public to 87.4 percent of GDP in 2021—nearly equal to the economy's total projected output for that year. These are unacceptable levels of spending and debt.²

The CBO's longer-term projections are even more daunting. They show spending rising to as much as 34 percent of GDP, with deficits at a post-war record of 15.5 percent of GDP and debt held by the public nearly twice the size of the entire economy.³

For the President's FY 2013 budget to be serious, it will need to reverse the rise of spending and debt with specific, credible policy proposals.

Reform Entitlements, Reduce Other Spending. The first place to start would be entitlement programs. In just a decade, total entitlement spending will reach \$3.5 trillion, almost as much as all federal outlays today. Roughly 40 percent of today's entitlement spending comes from health care programs, including Medicare, Medicaid, the Chil-

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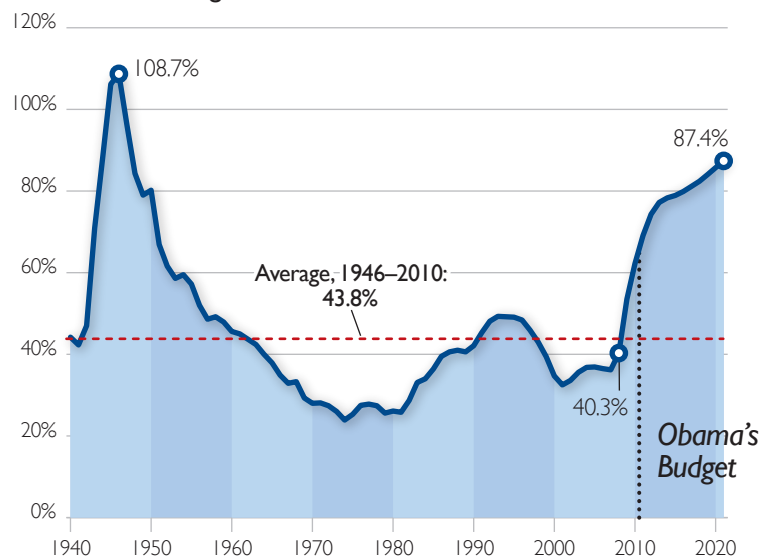
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Obama's Budget Would Send Federal Debt to Levels Not Seen Since World War II

In 2008, publicly held debt as a percentage of the economy (GDP) was 40.3 percent, nearly four points below the post-war average. Since then, the debt has increased more than 50 percent, and the President's FY 2012 budget would more than double it to 87.4 percent by 2021.

Debt as a Percentage of GDP



Source: Office of Management and Budget, *The President's Budget for Fiscal Year 2012*, table 7.1, February 2011, at <http://www.whitehouse.gov/omb/budget/Historicals> (February 9, 2012); Congressional Budget Office, *An Analysis of the President's Budgetary Proposals for Fiscal Year 2012*, Supplemental Materials on Federal Debt, April 2011, at <http://cbo.gov/ftpdocs/121xx/doc12130/04-15-AnalysisPresidentsBudget.pdf> (February 9, 2012).

Chart I • WM 3496 heritage.org

dren's Health Insurance Program, and Obamacare. This spending will more than double in the next 10 years and, by the middle of this century, along with Social Security, will consume about 18 percent of GDP, soaking up all the historical average of federal tax revenue.

In the past, the President has paid lip service to this immense problem and has offered proposals that only trim around the edges of these programs. This will no longer be enough. Fundamental restructuring of these programs is necessary.

For example, The Heritage Foundation budget plan, *Saving the American Dream*,⁴ and the bipartisan Ryan–Wyden legislation⁵ envision transforming Medicare from a government-run, price-controlled program into a patient-centered, “premium support” model that allows retirees to choose from a variety of health plans and promotes competition among insurers, which helps to restrain costs. *Saving the American Dream* also transitions Social Security “from an ‘income replacement’ system back to its original purpose of guaranteeing seniors freedom from fear of poverty and assuring a decent retirement income.” If the President

1. Congressional Budget Office, *An Analysis of the President's Budgetary Proposals for Fiscal Year 2012*, April 2011, table 1.2, p. 4, at <http://www.cbo.gov/doc.cfm?index=12130> (February 8, 2012).
2. CBO accepted most of the President's gimmicks and phony savings as occurring. See Brian M. Riedl, “Obama's 2012 Budget Offers More Gimmicks, Not Reform,” Heritage Foundation *Backgrounder* No. 2529, March 9, 2011, at <http://www.heritage.org/research/reports/2011/03/obama-s-2012-budget-offers-more-gimmicks-not-reform>.
3. Congressional Budget Office, *CBO's 2011 Long-Term Budget Outlook*, June 2011, table 1-2, at <http://www.cbo.gov/doc.cfm?index=12212> (February 8, 2012).
4. Stuart M. Butler, Alison Acosta Fraser, and William W. Beach, eds., *Saving the American Dream: The Heritage Plan to Fix the Debt, Cut Spending, and Restore Prosperity*, The Heritage Foundation, 2011, at <http://savingthedream.org/about-the-plan/plan-details/>.
5. Representative Paul D. Ryan (R–WI) and Senator Ron Wyden (D–OR), *Guaranteed Choices to Strengthen Medicare and Health Security for All*, December 15, 2011, at <http://budget.house.gov/UploadedFiles/WydenRyan.pdf> (February 9, 2012).

does not like these proposals, he should spell out his own plans to make entitlements sustainable now and for the long term.

But reforming entitlements is not enough. The President's budget should also propose reductions in other areas, whether through consolidation (the government's 47 different job-training programs would be a good start), eliminating programs that are obsolete or ineffective, or restoring to state and local governments or the private sector activities that the federal government should never have taken on in the first place.

Prevent Devastating Defense Cuts. National defense faces two streams of severe reductions. First, the cap in the Budget Control Act already imposes cuts in national defense that could range from \$445 billion to \$825 billion through 2021, according to the CBO.⁶ Second, the failure of the debt-reduction super committee triggered a crude, automatic spending reduction—known as a “sequester”—that will cut an additional \$492 billion from defense, further impairing military readiness.⁷

The President is commander in chief. He cannot allow these mindless cuts in defense spending to hollow out the armed forces and reduce America to a permanent lead-from-behind posture. His budget should present a specific proposal to rewrite the sequester and restore full funding for national defense.⁸

Offer Permanent Solutions for Unfinished Business. During the more than 1,000 days during which the Senate has failed to produce a budget resolution, a range of large, temporary spending and tax policies have accumulated that demand repeat-

ed, temporary fixes. One of the nagging spending provisions is the “doc fix,” a measure preventing steep reductions in payments to Medicare physicians. On the tax side are the scheduled expiration of the Bush-era tax cuts and inflation adjustments for the onerous alternative minimum tax (AMT) to prevent it from ensnaring millions more taxpayers. President Obama added to the list a year ago with his temporary payroll tax holiday.

The President's budget should take the first step toward stabilizing these policies. He should offer a plan for fixing Medicare reimbursement rates for providers, leading to a more fundamental reform of the Medicare program. He should also permanently extend the Bush tax rates and permanently fix the AMT. These steps would remove uncertainty for taxpayers and financial markets, which would help boost both economic growth and job creation.

Reject Phony Savings and Other Gimmicks. In his budget last year, the President claimed a range of illusory or misleading savings. Among the most prominent was an alleged \$1.09 trillion reduction through 2021 in spending for activities in Iraq and Afghanistan that was never going to be spent—a thoroughly discredited gimmick.⁹ He also claimed mandatory savings from policies that were actually tax or fee increases.

Such sleights of hand have become common with this Administration, but they are not acceptable. The President's budget should reject all such maneuvers and rely solely on real reductions that reduce spending and deficits.

A Need for Leadership. The President's budget is the first step of the congressional budget process.

6. Douglas W. Elmendorf, “Discretionary Spending,” testimony before the Joint Committee on Deficit Reduction, U.S. Congress, October 26, 2011, at http://www.cbo.gov/ftpdocs/124xx/doc12490/10-26-DiscretionarySpending_Testimony.pdf (February 8, 2012).

7. Congressional Budget Office, “Estimated Impact of Automatic Budget Enforcement Procedures Specified in the Budget Control Act,” September 2011, at <http://www.cbo.gov/doc.cfm?index=12414> (February 8, 2012).

8. See Baker Spring, “An Unacceptable Squeeze on Defense,” Heritage Foundation *WebMemo* No. 3417, December 21, 2011, at <http://www.heritage.org/research/reports/2011/12/an-unacceptable-squeeze-on-defense-modernization>.

9. See Patrick Louis Knudsen, “Note to Congress: Swear Off Phony War Savings, Now and Forever,” Heritage Foundation *Foundry*, February 2, 2012, at <http://blog.heritage.org/2012/02/02/note-to-congress-swear-off-phony-war-savings-now-and-forever/>.

His proposal for FY 2013 comes in a year that many predict will be unproductive, but it does not have to be that way.

Precisely because it is an election year, the President should offer a serious, detailed, and credible proposal for getting control of runaway spending and debt. This is a critical moment for the nation's

fiscal and economic health and a time when leadership is a priority.

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