



PROJECT ON DEFENSE ALTERNATIVES
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The Pentagon and Deficit Reduction

FY-2012 Budget Retains Exceptional Level of Defense Spending

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Executive Summary

President Obama's 2012 budget plan maps out a future of steady increases for the National Defense account (apart from war costs, which the budget presumes will decline). The budget sets the base or peacetime portion of national defense to rise from \$551.9 billion in 2010 to \$637.6 billion in 2016 - a boost of about 15.5%. This increase exceeds the expected rate of inflation by about seven-tenths of a percent per year.

The new budget fixes in place and extends the unprecedented rise in defense spending since 1998. Even apart from war costs, the Pentagon budget has risen by nearly 50% in real terms over the past 12 years. With war costs added, it has risen by more than 91% in real terms. For now and the foreseeable future, the 2012 plan sets base defense spending at levels that in real terms exceed the average during the Reagan years, when Cold War spending peaked.

The new budget request largely disregards the proposals on defense savings put forward last year by the President's bipartisan Fiscal Commission and other policy groups. These sought to rollback previous plans for base defense spending over the 2012-2016 period by \$300 billion to \$450 billion total. Instead, the FY-2012 budget rolls back previous plans by only \$75 billion. (By contrast, it rolls back the previous plan for non-defense discretionary spending by \$125 billion.)

As suggested above, the rollback in planned future defense spending does not entail an actual reduction from current (2010) levels. Instead, it is merely a downward revision in planned increases. In accord with the FY 2012 plan, the base portion of national defense spending will average \$58 billion more per year during the 2012-2016 period than it did in 2010. (Last year's plan would have tacked an additional \$15 billion per year, on average, to that increase.)

The new budget plan also re-balances the allocation of federal dollars among discretionary accounts. Looking forward from 2010 to 2016, the National Defense slice (including war costs) gradually declines on the assumption that war costs drop dramatically from about \$160 billion today to \$50 billion in 2016. However, looking at just the non-war portion of defense spending, a different picture emerges: The proportion of discretionary funds allocated to the base national defense budget actually rises from about 50% today to 53% in 2016. In effect, the plan takes most of the savings that it supposes will come from winding down the wars and transfers them to the peacetime portion of the defense budget.

Since the late 1990s, defense's share of discretionary spending has been growing. So the current plan continues this trend. And, in fact, it goes further in this direction than the budget plan presented last year (before the deficit-reduction campaign took hold). This, because the new plan extracts deficit savings disproportionately from non-defense discretionary accounts. By contrast, the President's Fiscal Commission had implied more equal treatment for defense and non-defense accounts.

Certainly, the contribution of defense to the nation's current debt problem is significant. The most recent year in which the federal budget ended with an on-budget surplus was 2000. During the 10 years that followed, \$7.9 trillion was added to America's gross federal debt. Taking the budget in 2000 as a spending baseline, the federal government spent \$9.9 trillion dollars above the year 2000 level during 2001-2010. Of this, discretionary spending above the 2000 baseline was \$4.25 trillion. Defense was responsible for more than 56% of this additional discretionary spending and 24.3% of the additional federal spending overall. Only about half of this additional spending is attributable to war.

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1. Past and Future Change in US National Defense Spending & Budget Share

President Obama's 2012 budget plan maps out a future of steady increases for the National Defense account apart from war costs (which are presumed to decline). As shown in Figure 1-1, National defense *sans* war is set to rise from \$551.9 billion in 2010 to \$627.6 billion in 2016 – a boost of about 15.5%. This increase exceeds the expected rate of inflation for the period by about seven-tenths of one percent annually. Although small by recent standards, the increase is not insignificant in the context of deficit-reduction efforts.

The 2012-2016 plan indicates a reduction in war expenditures that seems quite dramatic, but this is an accounting artifact. The plan treats war costs as unsettled and uncertain for the years after 2012. Thus, it uses a “place-keeper” sum of \$50 billion per year for the period 2013-2016. This is neither a goal nor a forecast, but instead an effort to lessen the planning distortion caused by uncertainty. Actual war expenditures are likely to exceed \$50 billion per year – perhaps by a very substantial margin for 2013 and 2014. The low “place keeper” figure for Overseas Contingency Operations after 2012 also lends to the impression that overall defense spending will decline by 3.7% over the course of the plan.

Figure 1-1. Planned National Defense Spending and Budget Share, 2010-2016

(dollars current billions)

	2010	2012	2013	2014	2015	2016	% Change 2010 > 2016
National Defense Discretionary w/o OCO	551.9	578.4	595.9	612.1	624.5	637.6	15.5%
Overseas Contingency Ops (OCO)	162.3	117.6	50	50	50	50	-69.2%
National Defense (050) Discretionary	714.2	696	645.9	662.1	674.5	687.6	-3.7%
Non-defense Discretionary Spending	543.4	546.7	542.2	546	553.1	566.4	4%
Total Discretionary Spending	1257.6	1242.7	1188.1	1208.1	1227.6	1254	-0.3%
Total Discretionary Spending w/o OCO	1095.3	1125.1	1138.1	1158.1	1177.6	1204	9.9%
National Defense w/o OCO as % of Discretionary Spending w/o OCO	50.4%	51.4	52.4	52.9	53	53	

Sources: *Budget of the US Government, FY2012*; Undersecretary of Defense (Comptroller), *FY 2012 Budget Request*.

Turning to non-defense discretionary spending: It is set to grow by 4% in “then year” dollars over the period 2010-2016, which equates to a real *reduction* of about one percent per year. Comparing this to base defense spending – that is, defense spending minus war costs – shows the two categories of expenditure to be moving in opposite direction in real terms. This means that most of the putative savings from the presumed reduction in war costs are reinvested in the non-war portion of defense. As a result, National Defense spending *sans* war grows as a proportion of discretionary spending, while the share allotted to non-defense spending declines. Put simply, apart from war costs, the plan re-balances spending in favor of defense.

Figures 1-2 and 1-3 review budget shares in historical perspective, looking at the period 1998-2016 in four clusters. Those years with similar allotments of funds among the various accounts have been grouped together. Each cluster is represented by an average annual expenditure for the years that the cluster encompasses.

In Figure 1-2, the defense share of discretionary spending is shown to grow successively across the first three clusters before being scheduled to decline slightly during 2012-2016. However, the apparent decline is an artifact of assuming low war costs during most of this period. This assumption does not affect the calculation of defense spending minus war costs, however, and these are shown to grow steadily in absolute terms.

Figure 1-2. National Defense as a Share of Discretionary Spending, 1998-2016
(dollars current billions)

	1998-2002	2003-2006	2007-2011	2012-2016
Total Discretionary Spending	617.7	934.7	1249.6	1224.1
Non-defense Discretionary	309.1	435.4	559.5	550.9
National Defense Discretionary	308.6	499.2	690.1	673.2
– Overseas Contingency Ops (OCO)	10.3	88.9	163.2	63.6
– National Defense w/o OCO	298.3	410.3	526.9	609.6
Non-defense	50.0%	46.6%	44.4%	45.0%
National Defense	50.0%	53.4%	55.6%	55.0%
National Defense w/o OCO	48.5%	43.9%	42.3%	49.8%
OCO	1.5%	9.5%	13.3%	5.2%

Sources: *Budget of the US Government, Fiscal Years 2002-2012*

Base defense spending as a percentage of overall discretionary spending slips slightly in the third period due to increased non-defense expenditures for economic recovery. It is then set to rebound and, indeed, rise to new heights in the final period, 2012-2016. As a consequence of deficit-reduction efforts, total discretionary spending is set to decline during the final period. However, the share allotted to the base defense account increases to compensate. As noted above, base defense spending actually continues to grow at a rate greater than inflation.

Figure 1-3. National Defense as a Share of Total Federal Spending, 1998-2016
(dollars current billions)

	1998-2002	2003-2006	2007-2011	2012-2016
Total Federal Spending	1868.7	2524.5	3480.6	4036.5
National Defense	312.8	502.2	696.1	679.9
Interest on Debt	214.7	181	215.9	407.3
National Defense as % of Total Spending minus Interest Payments	18.9%	21.4%	21.3%	18.7%

Sources: *Budget of the US Government, Fiscal Years 2002-2012*

The next table, Figure 1-3, looks at National Defense spending as part of total federal spending, discretionary and mandatory. Commensurate with this, the figures for National Defense include both the discretionary and mandatory portions of that account. The denominator used for calculating defense share in the table is total federal spending minus interest payments on the national debt.

The table indicates that, during the 2012-2016 period, defense's share of total federal spending will return to the balance prevailing during the years 1998-2002. Again, this is partly an artifact of assuming low future costs for war. However, most important in reducing the defense share of total spending is the growth in mandatory accounts, especially health care. Again, base defense spending does not actually decline in absolute terms. As pointed out above, it grows at a rate greater than inflation. The overall budgetary dynamic is one in which health care consumes more of the total federal dollar, while base defense spending is maintained and given room to grow by allocating to it a greater share of discretionary spending.

2. New Budget Plan Gives Pentagon Bigger Budget Slice

Each year's budget lays out a plan for future spending. The most relevant future years are the next five – for this year: 2012-2016. The following two tables compares planning for this period as presented in three successive budgets: the President's FY 2010, 2011, and 2012 budget submissions. Comparing planned funding for 2012-2016 in these three budgets shows how the administration has adapted to changing circumstances and political demands.

Especially relevant is the change in planning between last year's submission and this year's (released 14 February 2011). Comparing these two budget plans shows the Administration response to deficit reduction demands. Deficit reduction proposals by the President's Fiscal Commission and others calculated future deficits and remedial measures based on the FY 2011 plan. The FY 2012 plan shows the President's response.

The first table below looks at planned discretionary spending for the Defense Department in the context of overall discretionary spending. The second table looks at the Defense Department's discretionary and mandatory spending together in the context of total planned federal spending. Both tables are concerned with the period 2012-2016 and show cumulative planned spending for this five-year period. Both tables compare how this period is treated in three successive Obama budget plans – 2010, 2011, and 2012.

**Figure 2-1. Planned DoD Discretionary Budget for 2012-2016
in Three Successive Budget Submissions**

	FY 2010 Plan (billions)	FY 2011 Plan (billions)	2010 > 2011 Change in \$ (billions)	2010 > 2011 Percent Change	FY 2012 Plan (billions)	2011 > 2012 Change \$ (billions)	2011 > 2012 % Change
Dept of Defense	3,128	3,244	116.3	3.7%	3,236	-8.1	-0.3%
DoD Base Budget	2,878	2,995	116.3	4.0%	2,919	-75.7	-2.5%
Total Discretionary Spending	6,275	6,320	45.4	0.7%	6,120	-200	-3.1%
DoD as % Discretionary	49.9%	51.3%			52.9%		
DoD Base Budget as % Discretionary (minus war)	47.8%	49.3%			50.3%		

Source: OMB, US Budget, Analytical Perspectives, "Budget Authority and Outlays by Function, Category, and Program"

The first line in each table shows spending for both the war and non-war portions of the Pentagon budget. The second line – “DoD Base Budget” – shows planned spending for just the non-war portion of the budget.

Evident in both tables is the steady growth in the budget slice allotted DoD from one plan to the next. It is especially pronounced with regard to the Pentagon’s share of discretionary spending (Fig. 2-1). Notably, the projected percentage of discretionary funds to be consumed by DoD (fourth row, Fig 2-1) is underestimated because most future spending for war is represented by a low “place keeper” figure in the President’s budget submissions. However, DoD’s growing allotment of discretionary funds is not due solely to war. As evident in row five: Each successive budget plan gives a greater share of discretionary funds to the Pentagon base budget, too.

Figure 2-1. also shows (in the last two columns) how DoD’s contribution to deficit reduction compares with savings culled from overall discretionary spending. This pertains to the \$78 billion five-year savings offered by Secretary Gates on 6 January 2011. The DoD base budget makes a less than average contribution. And, when the entire DoD discretionary budget (including war spending) is examined (first row, last two columns), Secretary Gates’ promised savings virtually disappear, being almost entirely consumed by an increased allotment of funds to war.

Figure 2-2. incorporates both discretionary and mandatory portions of the Pentagon budget. These are viewed in the context of the entire federal budget, minus interest payments (because these are not subject to cost cutting initiatives).

**Figure 2-2. Planned DoD Discretionary & Mandatory Funding for 2012-2016
in Three Successive Budget Submissions: 2010, 2011, 2012**

	FY 2010 Plan (billions)	FY 2011 Plan (billions)	2010 > 2011 Change in \$ (billions)	2010 > 2011 % Change	FY 2012 Plan (billions)	2011>2012 Change in \$ (billions)	2011>2012 % Change
Dept of Defense	3,152	3,267	114.4	3.6%	3,261	-5.48	-0.2%
DoD Base Budget	2,902	3,017	114.4	3.9%	2,944	-73.06	-2.4%
Total Budget Authority (minus interest)	18,111	18,555	443.3	2.4%	18,146	-409.2	-2.2%
DoD as % BA (minus interest)	17.40%	17.60%			17.97%		
DoD Base Budget as % BA (minus war & interest)	16.25%	16.48%			16.51%		

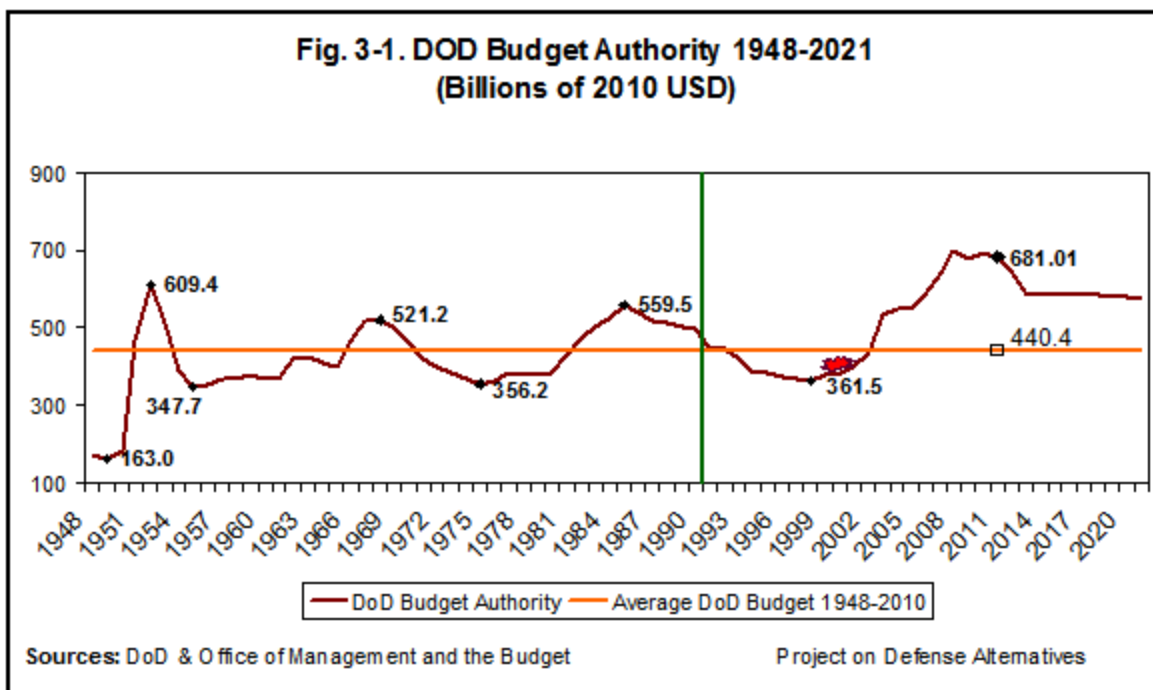
Source: OMB, US Budget, Analytical Perspectives, “Budget Authority and Outlays by Function, Category, and Program”

Once again, total DoD spending barely declines from the FY 2011 plan to the current one. However, the DoD base budget is seen to suffer a slightly deeper cut than does the federal budget overall. This reflects the fact that some mandatory programs – notably health care – offer DoD more serious competition than do discretionary programs. Of course, in the big picture, total DoD funding fares quite well. It is other areas of discretionary spending that are most squeezed between growing health care costs on one side and deficit-reduction efforts on the other.

3. Fixed in Place: The post-1998 Boon in US Defense Spending

The rise in US military spending since 1998 has been unprecedented over a nearly 50-year period. So has the rise in US national debt. Concern about debt and deficit spending has now served to slow the rise in planned Pentagon budgets, and may even mitigate it some, especially if America's current wars draw to a close. Nonetheless, the Fiscal Year 2012 budget plan, submitted by the Obama administration on 14 February, for the most part preserves and extends into the future the exceptionally high-levels of military expenditure established in recent years. National concern about debt and deficits has been mostly deflected to other accounts.

The chart below shows the variance in Pentagon budget authority over a 73-year period, including expenditures for war. The first three peaks represent the Korean war period, the Vietnam war, and the Reagan spending surge. Following the Reagan period is the post-Cold War trough. Subsequently, the budget rises to its present plateau, which sits substantially higher than the entire Cold War period.



Indeed, since 2007, the Pentagon budget has been consistently 20% above the highest budget of the Reagan years and more than 25% above the highest year of Vietnam era spending, adjusted for inflation.

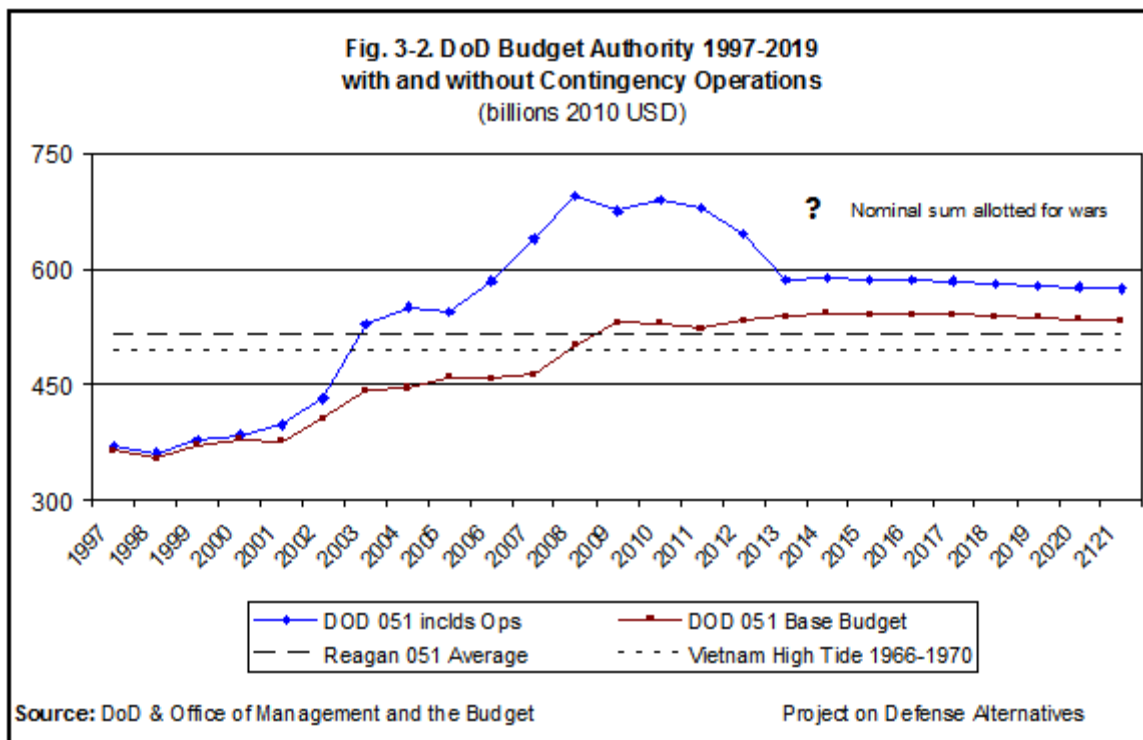
Although spending is shown to decline markedly after 2012, this is an accounting artifact. The future cost of ongoing wars is unknown and budget planners are unwilling to estimate. Instead, they have adopted a low-ball "place keeper" figure for war costs after 2012: \$50,000. Actual war spending for this period is likely to be higher – and perhaps much higher.

The green vertical line marks the end of the Cold War period. The red burst marks the date of the 11 September 2001 terrorist attack by the Bin Laden group.

Notably, the decline in spending after the Cold War is a modest one, given the collapse of the Soviet Union and its global alliance, which had been the principal driver of US defense spending for 40 years. The former Soviet Union, its

European allies, and other allied or friendly states comprised a group of what are today 25 independent nations with a combined population of 550 million people. Not only did the Soviet Union sustain an adversarial global alliance and peer military, it also supported terrorist and insurgent activities worldwide. Nothing of this peer adversary remains today and many former Soviet allies have formally joined the Western camp. Nonetheless, rather than indicating a major strategic transition, the post-Cold War trough in Pentagon spending resembles earlier dips that had occurred while the Cold War was still underway.

US military spending began to rise again in real terms in 1999. Its rise accelerated after the 2001 attacks and then again with the onset of the Iraq war. By 2010, it had grown 91% in real terms – a jump nearly equivalent to the earlier Kennedy, Johnson, and Reagan surges combined. However, as Figure 3-2 shows, the rise was not solely due to the post-9/11 wars. The Pentagon's base budget, which excludes war costs, by itself rose 49% between 1998 and 2009.

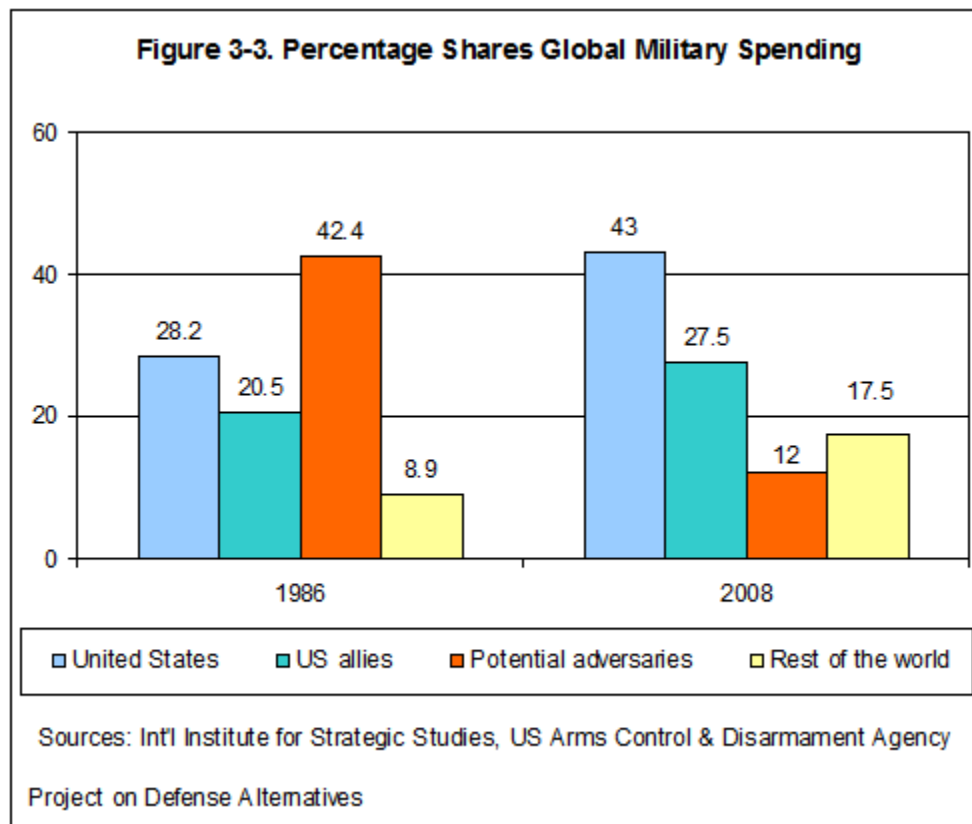


In Figure 3-2, the lower (red) curve, representing base spending, first rises to more than \$531 billion in 2009 (measured in 2010 constant dollars). It then dips slightly in real terms before rising to \$533 billion (2010 dollars) in 2013 and remains above this level in real terms through 2021.

The horizontal dashed line cutting across the chart represents average inflation-corrected expenditures during the Reagan years when Cold War spending peaked. The dotted line below it represents the average for the most costly years of the Vietnam war period.

The 1998-2010 growth in the “peacetime” portion of the budget was due partly to rising personnel and health costs. More important than that, however, were the launch of a sweeping program of military modernization, the Pentagon’s undertaking of new global missions, and the adoption of a more ambitious, proactive, and diffuse military strategy. In Pentagon parlance the new approach has been “capabilities based,” rather than “threat based.” One consequence is that America’s share of global military spending has grown steadily. As shown in the next figure, the gap between US

military investment and that of America's potential adversaries is much more favorable to the United States than was the case during the Cold War. Nonetheless, neither the White House nor much of Congress yet sees in this large margin of advantage an opportunity to press the Pentagon to carry a larger or even proportionate share of the deficit-reduction burden.



US allies include all NATO states plus Israel, Australia, New Zealand, Japan, Taiwan, and South Korea.

Potential adversary states include, for 1986: the Soviet Union and other Warsaw Treaty states, China, Cuba, Iran, Iraq, North Korea, Libya, Syria, and Vietnam. For 2008, the former Soviet Union and Warsaw Treaty states are replaced by Russia and Belarus. Vietnam and Libya are removed, but Venezuela is added.

Sources: International Institute for Strategic Studies, *The Military Balance* 1996/97, 1995/96, 1994/95, 1993/94, 1992/93, 2002-2003, 2008, 2010; Office of the Secretary of Defense, *Military and Security Developments Involving the People's Republic of China* (Washington DC: DoD, 2010); US ACDA, *World Military Expenditures and Arms Transfers* 1995, 1999-2000.

4. Defense Spending and the Production of US National Debt 2001-2010

The year 2000 was the last of recent years that ended with an on-budget federal surplus. During the subsequent 10 years, 2001 through 2010, \$7.9 trillion was added to America's gross federal debt. Surpluses in revenue for Social Security and other trust funds covered some of the deficit spending during these years, thus the accumulation of "debt held by the public" amounted to only \$5.6 trillion. (The remainder is due Social Security.) All told, the amount of gross federal debt grew by 140% during this period, while "public debt" rose by more than 164%.

Notably, about two-thirds of this new, post-2000 debt was incurred before the onset of America's recent economic troubles and before any substantial efforts to redress those problems.

Figure 4-1. below tallies several categories of federal and defense spending during the debt accumulation period. The category "National Defense" encompasses the Pentagon budget plus a small amount of additional spending, mostly related to nuclear weapons. During the period 2001-2010, the National Defense account absorbed about 22.3% of all federal spending. Looking just at discretionary spending, defense accounted for 53.5% of the total. Less than a fifth of this amount was devoted to wars.

Figure 4-1. Defense Spending and Debt Accumulation 2001-2010
(dollar figures in trillions)

Total Federal Spending	24.42
of which Discretionary	10.09
Total National Defense (050) Spending	5.45
of which Discretionary	5.40
of which for Overseas Contingency Operations (OCO)	1.05
National Defense as % of Total Federal Spending	22.3%
National Defense Discretionary as % of Discretionary	53.5%
OCO as % of Discretionary	10.4%
Accumulated Gross Federal Debt	7.9
of which "Public Debt" (ie. not held by other government accounts)	5.6

Sources: *Budget of the US Government, Fiscal Years 2002-2012*; Undersecretary of Defense (Comptroller), *National Defense Budget Estimates*.

As noted above, the surge in debt during 2001-2010 was not due principally to post-2007 economic recovery efforts, although these contributed. Debt accumulation also was due partly to recession-related drops in expected revenue as well as intentional reductions in taxes and tax rates. The final ingredient was an increase in expenditures during these years: total federal spending rose by 91%. (By contrast, inflation was less than 26% for the period and the rise in GDP was less than 50%).

Table 4-2 illustrates one way to measure the contribution of the defense budget to this surge in expenditure and debt. The table takes spending levels in the "surplus year" 2000 as a baseline and aggregates all spending above this level for the subsequent years, 2001 through 2010. It shows that total federal spending above the 2000 baseline during these

years was \$9.9 trillion. Of this, discretionary spending above the 2000 baseline was \$4.25 trillion. Defense was responsible for more than 56% of this additional discretionary spending and 24.3% of the additional federal spending overall.

It is noteworthy that defense's share of additional spending is greater than its share of overall spending (as shown in the previous table, 4-1). This means that the defense account has been among the "leaders" of increased spending during the period, growing at more than the average rate. And, indeed, while the federal budget grew by 91% during the period, national defense grew by 137%. Taking war expenditures out of the picture lightens the weight of defense, however. Apart from war expenditures, the growth in national defense spending equals the average rate of budget growth, making the base defense budget an equal, not exceptional contributor to budget growth.

Table 4-2. Federal & Defense Spending During 2001-2010 Above Levels Set in 2000
(dollar figures in trillions)

Total Federal Spending Above 2000 Baseline	9.91
Total Discretionary Spending Above 2000 Baseline	4.25
National Defense Total Spending Above 2000 Baseline	2.41
National Defense Discretionary Spending Above 2000 Baseline	2.39
National Defense as % of Total Above Baseline	24.3%
National Defense as % of Discretionary Above Baseline	56.2%

Sources: *Budget of the US Government, Fiscal Years 2002-2012*; Undersecretary of Defense (Comptroller), *National Defense Budget Estimates*.

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