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PROJECT ON DEFENSE ALTERNATIVES

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Pentagon cuts in context No reason for “doomsday” hysteria

PDA Briefing Memo #50
11 October 2011

Summary: Should the Joint Select Committee on Deficit Reduction fail to produce a \$2 trillion savings plan that becomes law, the Budget Control Act (BCA) provides for the automatic imposition of caps and reductions on defense and non-defense spending that would save as much. This is “sequestration” – the only provision of the BCA that would actually guarantee substantial cuts in defense spending. The caps would hold DoD spending to a level nearly \$1 trillion below the 10-year plan submitted by President Obama in February 2011. Defense leaders have decried the prospect as catastrophic. However, the measure is equivalent to rolling the Pentagon budget back to the level of 2007 (adjusted for inflation) and holding it there in real terms.

Measured against the 2011 budget, sequestration would entail a DoD reduction of 13.6%. Total base budget spending over the next decade would be just 6% less than last decade, adjusted for inflation. A reduction on this scale would hardly set records. By comparison, total spending on the Pentagon during the years 1992-2001 was 24% lower than spending during 1982-1991.

What makes sequestration impractical (and marks it as a scare tactic) is the precipitous manner in which it would implement cuts. A gradual approach could accomplish equivalent savings without comparable disruption. As devised, the provision is meant to motivate, rather than mitigate, revenue increases and cuts to entitlement programs.

The BCA also contains provisions for more moderate, minimum cuts in total discretionary spending, which would save \$841 billion. But these provisions do not dictate a Pentagon share. Should lawmakers nonetheless decide to extract proportionate savings from the Pentagon’s base budget, it would receive about \$620 billion less during 2012-2021 than first proposed in the President’s February budget submission. Compared to current spending, the cut would average 8% in real terms. Decade to decade, the base budget for 2012-2021 would show no change from the total for 2002-2011, in real terms.

The August 2011 Budget Control Act (BCA) entails the possibility of significant reductions in the Defense Department budget. The tables in this memo allow comparison of prospective DoD budget cuts to recent and historical budgets.

The tables test two controversial options:

- Limits on the defense budget proportional to the discretionary spending caps set out in the BCA
- Sequestration – the so-called “doomsday” scenario for DoD

Proportional caps

The Budget Control Act (BCA) establishes initial caps on all discretionary spending. These caps would achieve \$841 billion in savings over ten years, measured against the CBO baseline (which is current policy projected forward with adjustments for inflation). The Joint Select Committee on Deficit Reduction is charged with finding at least another \$1.2 trillion in savings – although this remainder can come from a combination of more spending cuts (both discretionary and mandatory) and revenue increases.

The initial caps do not specify any cuts to the Pentagon budget, *per se*, although there are subcaps on “security spending” during the first two years, 2012 and 2013. These caps leave open the possibility that lawmakers might partially or entirely exempt the Pentagon, while making other accounts in the “security basket” carry an extra burden. And after 2013, they are free to make non-security spending absorb all the cuts.

Already, Congress seems inclined to “go light” on the Pentagon. Nevertheless, the scenario examined below assumes that lawmakers will seek proportional reductions in DoD spending across the entire decade. In other words: It assumes that, in adhering to the BCA’s caps on discretionary spending, lawmakers will limit DoD’s budget in accord with its recent share of discretionary spending. How would absorbing a “fair share” of cuts affect the Pentagon budget?

Sequestration: the “doomsday” scenario

Should the Joint Select Committee fail to produce a plan that becomes law, the BCA mandates automatic caps and reductions on “defense” and “non-defense” spending. These would result in \$2 trillion in savings measured against the CBO baseline. Affected would be discretionary and some mandatory spending, but not Social Security or Medicaid. These caps would override the caps mentioned above. More important, the option to sequester these funds is unique in that *it alone ensures limits on the National Defense account (050)*.

Sequestration makes cuts to the Pentagon budget (051) unavoidable because the Pentagon’s budget constitutes 95% of the National Defense account. However, as OMB Director Jack Lew makes clear: “The sequester is not meant to be policy.” Instead, “it is meant to be an

unpalatable option that all parties want to avoid.” But would its likely impact on Pentagon budgeting be extreme, as Defense Secretary Panetta and other Pentagon leaders contend?

Total DoD Budget Authority (051) Under Different Scenarios 2012-2021	
(Trillions of “then year” dollars)	
Original Obama FY 2012 plan	\$6.14
CBO baseline (equals 2011 budget plus inflation)	\$5.99
BCA Minimum Cuts, DoD fair share	\$5.52
DoD under Sequestration Caps	\$5.18
See: Table notes and sources, at end	

To facilitate broader comparison, the ten-year spending totals can be calculated as average annual budgets in 2012 dollars. This gives a number that can be taken as a 2012 base budget which, if allowed to grow over the next decade at the rate of inflation, would produce a total ten-year expenditure equal to that of the chosen option. In other words, this method produces a “soft freeze” equivalent for each option.

Pentagon Top Line Under Different Scenarios	
2012 “Soft Freeze” Equivalents	
(Average annual budget 2012-2021 in Billions 2012 USD)	
Obama FY 2012 plan	\$551.5
CBO baseline	\$538.5
BCA Minimum Cuts, DoD Fair Share	\$495.5
DoD under “doomsday” sequestration caps	\$465.0
See: Table notes and sources, at end	

For comparison, the following actual historical budgets and averages are expressed in 2012 dollars:

- 2008 DoD base budget: \$497 b.
- 2007 DoD base budget: \$468 b.
- DoD annual average 2002-2011: \$494 b.
- DoD annual average 1992-2001: \$400 b.
- DoD annual average 1982-1991: \$526 b.
- Cold-war average (including wars): \$456 b.

Imposing proportional cuts on DoD as part of BCA's initial caps is the equivalent of rolling the DoD budget back to its 2008 level and holding it there with increases for inflation. The "doomsday" scenario rolls it back just one more year. So, in the current debate, the 2007 Pentagon base budget has become synonymous with "doomsday."

- Relative to the CBO baseline (current spending rolled forward adjusted for inflation), the two scenarios entail an 8% and 13.6% reduction, respectively.
- Against President Obama's FY 2012 budget (which he abandoned in April 2011), the reductions would be 10% and 15.7%, respectively
- While the period 1992-2001 saw a 24% real reduction in defense spending from the preceding decade, sequestration would entail for 2012-2021 a less than 6% reduction from 2002-2011.

In sum, sequestration would entail rolling back recent DoD budget *plans* by something on the order of 13.6% to 15.7%, depending on the reference point. However, measured decade-to-decade, it would entail a reduction in *actual* spending of only 6%. Although significant, this degree of retrenchment is neither disastrous nor unprecedented.

What makes sequestration hard to digest is the manner in which the Budget Control Act would implement it. It would require an immediate drop in 2013 National Defense spending to about \$492 billion. The FY 2011 level is about \$552 billion (including the Pentagon and some other accounts). A cut exceeding 10% enacted in a single year would pose considerable management challenges.

Done differently, however, substantial reductions from today's extraordinary levels of defense spending could serve as a viable alternative to seeking deeper cuts in other programs or seeking higher taxes or both. A sensible approach would be to walk the budget down gradually over the next four years and then allow subsequent upward adjustments for inflation. This would make practicable a return to 2007 levels of spending.

A sensible path to the deeper cuts that sequestration entails would be to:

- Step 1 Reduce DoD funding to \$520 billion (current USD) in 2012
- Step 2 Walk the budget further down to \$490 billion (current USD) over the subsequent three years in \$10 billion steps.
- Step 3 After 2015, allow the new DoD budget to grow by inflation

This approach would entail a 15% reduction in real (inflation-adjusted) terms spread over four years. The result for the decade 2012-2021 would be total expenditures equal to those allowed under sequestration – and accomplished without pushing the Pentagon off a wall. Measured against the CBO baseline for 2012-2021, the reduction in total ten-year expenditures would be

nearly 14%. Measured against actual spending during 2002-2011, the cut would be less than 6% in real terms.

Table notes and sources

Neither the CBO baseline, nor the Budget Control Act present figures specifically for the DoD budget (function 051). Instead, these are derived from "security spending," the national defense function (050), and overall discretionary spending, using recent historical percentages. Also, the BCA's sequestration caps on "national defense" include both discretionary and mandatory parts of the budget. To derive discretionary budget estimates, the mandatory portion is subtracted out, using recent historical percentages.

Sources: Budget Control Act of 2011, US House of Representatives, Committee on Rules, August 2011, pp. 14-17, 43-52; Congressional Budget Office, Estimated Impact of Automatic Budget Enforcement Procedures Specified in the Budget Control Act (Washington DC: CBO, 12 September 2011); Jack Lew, "Security Spending in the Deficit Agreement," OMBlog (Washington DC: Office of Management and the Budget, 4 August 2011); Douglas Elmendorf, "CBO Analysis of August 1 Budget Control Act," letter to the Honorable John Boehner and the Honorable Harry Reid, 1 August 2011; Congressional Budget Office, The Budget and Economic Outlook: An Update (Washington DC: CBO, August 2011);

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