COMMITTEE FOR A RESPONSIBLE FEDERAL BUDGET

CRFB Reacts to the President's FY 2012 Budget
February 14, 2011

This morning, President Obama released his FY 2012 budget, proposing $3.7 trillion in spending (23.6 percent of GDP) and collecting $2.6 trillion (16.6 percent of GDP) in 2012, resulting in a $1.1 trillion (7.0 percent of GDP) deficit. Over the decade, deficits would total $7.2 trillion (average of 3.7 percent of GDP), and debt will reach $19.0 trillion (77 percent of GDP) by 2021.

Though we applaud the President's recognition of the need to focus on fiscal reforms, this budget does not go nearly far enough. If both the President and Congress continue to focus their attention on the discretionary parts of the budget, we will fall dangerously behind on the need to put in place critical entitlement and tax reforms.

Though the proposed policies would increase the deficit slightly in FY 2012, over a decade the Administration proposes a total of $1.1 trillion in savings. These measures, along with the White House assumptions about economic growth, would help to bring the deficit down to 3.2 percent of GDP by 2015 ($112 billion above their own target of primary balance) and more or less stabilize the debt around 77 percent of GDP through the decade.

"It is encouraging that the Administration identifies some areas for real savings. However, the total level of savings is far short of what is needed and too many heroic assumptions are used to achieve them," said Maya MacGuineas, president of the Committee for a Responsible Federal Budget. "This budget fails to meet the Administration's own fiscal target, it fails to tackle the largest problems areas of the budget, and it fails to bring the debt down to an acceptable level."

"While we can certainly appreciate the difficult political environment in which the budget is introduced, the glaring omission of any significant entitlement reforms and the excessive use of 'fill-in-the-blank' budgeting does not help to advance the conversation," said MacGuineas

"The Administration does have some good proposals in here. Not only are they tough on discretionary spending, but they try to advance the notion of pay-as-you-go by identifying some offsets for perennial budget punts such as the doc fix and AMT patch. But none of these changes go far enough, and spending still rises dramatically under this budget," MacGuineas continued.

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"We hope the President will spend the remainder of this year working closely with leaders of both parties to develop a comprehensive fiscal plan that includes the things this budget is missing – Social Security reform, tax reform, large health care savings, additional specific defense cuts, and a reevaluation of government priorities," said MacGuineas.

CRFB will be releasing a complete analysis of the President's Budget later in the week, discussing its strengths as well as its weaknesses. Here is our first take:

The Good

The President's Budget has plenty for people to be positive about, including what appears to be a serious effort to control domestic discretionary spending. The budget includes a 5-year non-security discretionary spending freeze which saves $400 billion over the decade, and it includes over 150 specific discretionary spending cuts (totaling $25 billion next year) to help achieve the goal. Additionally, it limits defense spending over the coming decade.

The budget also recommends a number of mandatory spending cuts including various student loan reforms, cuts to agriculture subsidies, reforms to the Pension Benefit Guarantee Corporation, and various user fees and auctions.

The budget puts forward the important principle of pay-as-you-go (PAYGO) budgeting by offering proposals to pay temporarily for AMT patches (3 years) and the "doc fixes" (2 years), and calls for offsets to further doc fixes as well as for any highway spending in excess of what is currently affordable. While we believe this is the right principle, the real test will be the extent to which the Administration goes to enforce their call for offsets.

Fig. 1: Budget Totals in the FY 2012 Budget (Billions and Percent of GDP)

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2012-2021
Outlays	$3,819	$3,729	$3,771	$3,977	$4,190	$4,468	$4,669	$4,876	$5,154	$5,422	$5,697	$45,952
	25.3%	23.6%	22.5%	22.4%	22.3%	22.6%	22.5%	22.5%	22.8%	23.0%	23.1%	22.7%
Revenue	$2,174	$2,627	$3,003	$3,333	$3,583	$3,819	$4,042	$4,257	$4,473	$4,686	$4,923	$38,747
	14.4%	16.6%	17.9%	18.7%	19.1%	19.3%	19.5%	19.6%	19.8%	19.9%	20.0%	19.0%
Deficits	$1,645	$1,101	$768	$645	$607	$649	$627	$619	$681	$735	$774	$7,205
	10.9%	7.0%	4.6%	3.6%	3.2%	3.3%	3.0%	2.9%	3.0%	3.1%	3.1%	3.7%
Debt	$10,856	$11,881	$12,784	$13,562	$14,301	$15,064	$15,795	$16,513	$17,284	$18,103	$18,967	n/a
	72%	75%	76%	76%	76%	76%	76%	76%	76%	77%	77%	n/a

Importantly, the budget stabilizes the debt. According to OMB's estimates, under the President's budget the debt would rise to 76 percent of GDP by 2013 (from 62 percent at the end of last year), but then remain at or below 77 percent of GDP for the remainder of the decade.

Though we support these positive developments, they all come with caveats. Though the Administration officials do bring discretionary spending under control, they don't actually cut it as likely will be necessary. Though they put forward the principle of PAYGO, they don't follow through by offering real policies to fully offset doc fixes or AMT patches over the ten-year window, and don't even attempt to offset the 2001/2003/2010 tax cuts they continue for those making below $250,000 a year. And while they do stabilize the debt within the 10-year window, they do so at too high a level, and in a way where it will not remain stable outside the budget window.

The Bad

Unfortunately, the Administration does not achieve either of the fiscal goals it established for its own Fiscal Commission. For one, the budget does not reach primary balance in 2015. Instead, at just over $600 billion, the deficit remains more than $100 billion away from primary balance. Secondly, the budget does not make meaningful improvements to the long-term fiscal outlook. Few of the policies in the budget would have a substantial effect on the trajectory of spending or revenues outside of the ten-year window.

As noted above, the level at which the budget stabilizes the debt – 77 percent of GDP – is way too high. It is well above historical levels (about 40 percent of GDP) and the traditional target of 60 percent of GDP – and could threaten the government's ability to borrow in case of a real emergency down the road. It also begins to creep up again at the end of the ten-year window, and likely will grow substantially beyond this window.

Unfortunately, the budget doesn't make any meaningful improvements to the largest problem areas of the budget. The budget does keep defense costs from increasing, trim Medicare and Medicaid spending a bit, and limit tax expenditures for high earners. But these measures only scratch the surface when the Administration should be calling for real defense cuts, serious changes in federal health spending, and fundamental tax reform – as well as Social Security reform designed to achieve 75-year sustainable solvency.

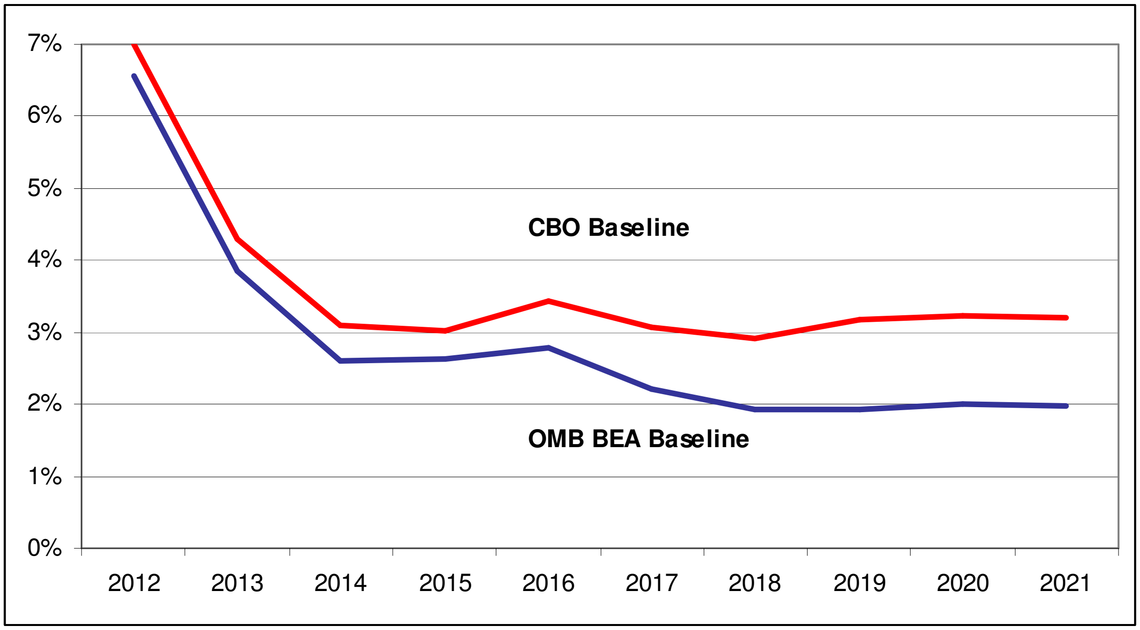
The Troublesome

One of our largest concerns in this budget is that, when the layers are unpeeled, it may not do nearly enough to stabilize the debt (even at the too-high level it claims to). Not only does the budget appear to rely on rosy baseline assumptions, but it also assumes away certain costs.

For one, the Administration seems to assume away the costs of physician payment updates in Medicare (the doc fix) beginning in 2014, as well as the costs of fully funding highway spending. We fully support the principles of fully offsetting doc fixes and adequately financing the highway trust fund, but failure to identify where the money comes from (in the case of the doc fix, the Administration does identify enough savings for the first two years, but not beyond) is akin to a budget gimmick. Taking these two programs together, the Administration is assuming over $400 to $650 billion (depending on what you assume about additional highway spending) in unspecified savings. That is an immensely large magic asterisk.

Though our full analysis will go into more detail with regards to the economic assumptions in the budget, it is clear that the Administration does have a much more optimistic view of the starting point than the Congressional Budget office. Under CBO's "current law" projections (those which allow for the expiration of the 2001/2003/2010 tax cuts and other measures) the deficit reaches 3.2 percent of GDP by the end of the decade and the debt reaches 77 percent. Under OMB's current law projections, the deficit reaches 2 percent and the debt 70 percent. This alone has us concerned that CBO's estimate of the President's budget won't be nearly as charitable as OMB's – and reality might not be either.

Fig. 2: Comparison of CBO and OMB BEA Baseline Deficits (Percent of GDP)



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The President's budget has been described as a down payment on fiscal reform, and it does present some policies which would move in the right direction, but even as a down payment, this is not nearly enough. We are disappointed that the budget passes over the major areas in need of reform, and that even to stabilize the debt at a level that is too high, it relies both on optimistic assumptions and on unspecified savings.

It's time for the White House to get serious about bringing down the debt through a combination of entitlement reform, tax reform, and serious cuts to the discretionary budget. It is urgent that they spend the next year working in a bipartisan manner to enact a comprehensive fiscal plan into law.