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The One Reason America Can't Police the World Anymore: Washington Is Broke

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The annual budget battle is at its peak and Washington continues to flaunt its remarkable dysfunction. This fiscal irresponsibility affects more than domestic programs. In the coming years, it is likely to drive U.S. foreign and military policy.

The U.S. government has no more important duty than defending the nation. However, providing for the "common defense," as the Constitution puts it, is remarkably easy. America has vast oceans east and west and peaceful neighbors to the north and south.

Today only Russia, with an arsenal of nuclear-tipped missiles, could launch a serious attack on America. However, Moscow has no incentive to do so, since the result would be devastating retaliation. China's military is expanding but directed at preventing Washington from dominating the People's Republic of China at home and in its neighborhood.

Terrorists abound but mostly result from maladroit U.S. policies that create enemies and make other people's conflicts America's own. Moreover, while such attacks are atrocious, they do not pose an existential threat. Nor do America's conventional forces and nuclear arsenals offer the best response; promiscuous war-making around the world is more likely to accelerate than diminish terrorism. The better option would be to do less militarily, especially in the Middle East.

Why, then, is Washington spending $717 billion in fiscal year 2019 to maintain vast armies, fleets, and air armadas around the world? Not for defense, of America, anyway. It is to protect allies, assert influence, remake failed societies, dictate behavior, promote values, and more. All of these may have some value, though rarely as much as asserted. And none have much to do with protecting America's territory, people, constitutional system, and prosperity.

Unfortunately, attacking is far more expensive than deterring. Most of America's Pentagon outlays go to project power, which is why the United States has an outsize military budget, equal to that of the next dozen or so nations combined. None of them, or any combination of them, could defeat America. Rather, Washington wants the ability to target them. The so-called "defense" budget is the price of America's aggressive foreign policy. Playing global gendarme—is not cheap.

Although Americans should be prepared to pay any price necessary for their defense, not so with remaking the globe. Sending Americans to fight and die for tasks of peripheral importance always was foolish. Even if America once felt wealthy enough to squander its financial resources in such pursuits, those days have ended. Washington is effectively bankrupt, with massive unfunded liabilities. Its fiscal future will only worsen as Baby Boomers continue to retire.

Last year the Republican Party, once the self-proclaimed guardian of the treasury, used control of both ends of Capitol Hill to simultaneously hike federal spending and cut taxes. The result was a deficit approaching $779 billion, up $114 billion from the previous year. The last time Uncle Sam generated as much red ink was 2012 when recovering from the financial crisis.

Unfortunately, the numbers will only go up. The Congressional Budget Office figured the president's 2019 budget proposal will push the deficit to nearly $1 trillion—without another financial crisis. And the numbers will continue to rise, to $1.527 trillion in 2028, or nearly twice last year's level. There will be an extra $12.4 trillion in red ink over the coming decade.

This debt increase would be accompanied by rising interest rates, which already have begun their inexorable rise as the Federal Reserve begins unwinding its radical expansionary policy dating back to the financial crisis. CBO figured "net interest," which disguises federal costs by subtracting interest paid to Uncle Sam, will rise from $315 billion last year to $819 billion in 2028.

That would roughly double the share of GDP devoted to interest from 1.6 percent to 3.1 percent of GDP. At that level, interest would be Washington's third-largest program, smaller only than Social Security and Medicare. In another two decades, interest payments would match Social Security, currently the most expensive federal program. Interest payments would then consume 6.3 percent of GDP, the highest ever.

Alas, the numbers probably will be worse. The president's budget targets domestic discretionary spending, as have most presidents, with little result, since Congress is not prepared to shut down the Washington Monument, furlough congressional staffers, and kill politically popular grants. More important, that area is not where the money is, accounting for just 15 percent of outlays. Zeroing out such expenditures would still leave a deficit.

Washington could stumble along and hope for better than expected economic news: higher productivity, lower interest rates, and faster economic growth, all of which would ease fiscal pressures on Washington. However, the reverse also is possible. In fact, the president's trade war increases the chances of negative changes, while escaping a recession during the next decade will require more than a little luck. To combat the latter policymakers likely would hike outlays to "stimulate" the economy, adding to a deficit already expected to exceed a trillion dollars annually.

Of course, Congress could cut domestic expenditures. To achieve anything approaching a responsible budget requires addressing the four big domestic boulders, which along with military outlays make up 85 percent of the budget: interest, which cannot be reduced without repudiating debt; Social Security, the traditional "third rail" of U.S. politics; Medicare, the equally popular elder health care program; and Medicaid, the perennially under-funded promise of medical services for the poor. Spending pressures are inexorable. Entitlement outlays automatically rise as the population ages—both a larger percentage of the population is older and people on average live longer—so Social Security and Medicare will drive the budget.

More likely, Congress will act like, well, Congress, and both spend more and collect less than under current law. If so, the "Extended Alternative Fiscal Scenario" predicts that the deficit as a percentage of GDP will rise from 78 percent last year to 105 percent in 2028, 148 percent in 2038, and an astonishing 210 percent in 2048. Even the CBO's best case, under "Extended Baseline," which simply runs out existing law, including expiration of tax cuts, forecasts 152 percent of GDP in 2048. That is higher than in Greece at the onset of its fiscal crisis, which generated economic hardship, social dislocation, and political disruption. America's average over the last half-century was just 41 percent; only during World War II and in its immediate aftermath did the federal debt exceed 70 percent, peaking at 106 percent in 1946.

With larger deficits and debts, interest rates likely would be higher and GDP growth lower. Once the spiral starts it will be difficult to stop. First, warned CBO, "rising interest rates and increased federal borrowing boost net interest costs substantially." Net interest costs rose 20 percent last year alone. No surprise, noted the agency, "the higher the government's interest costs, the more difficult it would be to achieve any particular target for deficit reduction." Indeed, CBO observed, "Rising interest costs would boost deficits and debt and rising debt would push up interest costs." The latter would be "a major contributor to that growing gap" between outlays and revenue in the coming years.

Second, noted CBO: "Large federal budget deficits over the long term would reduce investment, resulting in lower national income and higher interest rates than would otherwise be the case. If the government borrowed more money, a greater amount of household and business saving would be used to buy Treasury securities, thus crowding out private investment. Both the government and private borrowers would face higher interest rates to compete for savings." This would cut savings, and private investment, including in capital goods. Which, in turn, would cut productivity and real wage growth, and hence economic output.

The crisis might not stop there, however. Such circumstances, concluded CBO, would increase "the chance of a fiscal crisis." The spiral toward disaster could be rapid: "Higher interest rates would increase concerns over repayment, which would continue to raise interest rates even further. Even in the absence of a full-blown crisis, such risks would lead to higher rates and borrowing costs for the U.S. government and private sector." Rising Treasury rates would lower the securities' value, undermining the stability of financial institutions. Large-scale Federal Reserve purchases could accelerate price inflation and/or dollar depreciation.

Such a situation "would ultimately be unsustainable," CBO observed politely. Imagine a 2008-style crisis, but with the debt burden twice as great.

Of course, Congress could raise tax hikes, but they are no more popular than spending cuts. Moreover, the growing deficit is mostly a result of increased spending. Over the coming decade, CBO estimates that outlays will rise faster than revenues, $2.2 trillion compared to $1.9 trillion. The disparity grows even greater in future years, as "revenues would grow faster than the economy but more slowly than spending," according to CBO. Under the so-called "Extended Baseline," revenues will average 19.8 percent and outlays 29 percent of GDP by 2048. Over the last fifty years, these numbers averaged 17 and 20 percent, respectively.

In this world, what happens to the Pentagon, which spends so much money and time, and so many Americans' lives, protecting other nations, most of which are populous and prosperous?

Cuts are inevitable. The obvious place to start is overseas contingency operations, funded by supplementals to the base-budget appropriations. OCO monies peaked in 2007 and 2008 at 28 percent of Pentagon outlays. From 2001 to 2018 they averaged about a fifth. These funds mostly go for wars of choice, social engineering, and other dubious ventures without much to do with America's "common defense." (This practice creates another problem, obscuring military spending and its purpose. As CBO, explained, use of OCO "creates an inaccurate picture of what future defense spending might be in the absence of military conflicts.")

However, far more serious reductions are required. The base-budget underwrites a system of guarantees, alliances, and deployments which are not sustainable—and wouldn't be in America's interest even if they were. The starting point, though, is to revise foreign policy. That is, cutting expenditures without trimming tasks risks creating a dangerous mismatch, forcing Washington to either abandon commitments made or uphold them without the necessary force. Instead, the administration should drop obsolete alliances, adjusting its force structure accordingly. That requires a serious debate over America's role in the world and the inevitable trade-off between military adventurism, domestic social programs, and private incomes.

Uncle Sam is like the congenital wastrel who keeps buying rounds at the neighborhood bar. As long he can run a tab—or his credit card charge goes through—he keeps going, heading toward inevitable disaster. The longer Washington waits to reform its ways, the bigger and more disruptive changes ultimately will have to be. Approving future cuts now, even with the effects delayed, would provide greater certainty and lower long-term interest rates. Moreover, people could begin to adapt—at home to income cuts, abroad to burden-shifting.

To stabilize Washington's finances, all programs need to be addressed. However, military outlays deserve an especially thorough review. America First, as the president proclaims, should not mean ignoring the needs and rights of others. But it should recognize that the U.S. government's highest duty is to its own people. America First also means that war, given the unique costs—lives lost, risks taken, money wasted—is a last resort undertaken only for the most serious, even vital purposes.

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