

# Bloomberg

## ‘Spending Cuts’ Lose Something in Translation

By: Caroline Baum December 19<sup>th</sup>, 2012

---

Oh for those halcyon days when Bill Clinton was in the White House, Republicans controlled both houses of Congress, the economy was booming, unemployment was low, the peace dividend was working its magic and the federal budget was in surplus. (OK, so I omitted the tech bubble.)

If we could just restore those Clinton-era tax rates on top earners, why, happy days would be here again!

Not exactly. The \$1.2 trillion of revenue President Barack Obama hopes to generate by raising taxes on the rich, revised from an initial \$1.6 trillion, represents only a small down payment on a budget solution. By minimizing the real source of the problem, which is runaway growth in entitlements, especially health care, Obama isn't doing the country any favors.

Let's look at some of the numbers. In 1998, the first time the federal government ran a surplus in three decades, outlays totaled \$1.65 trillion compared with receipts of \$1.7 trillion. For fiscal 2012, which ended Sept. 30, the respective numbers were \$3.5 trillion and \$2.4 trillion.

Yes, tax receipts have been depressed as a result of five years of recession and slow growth. But even if they were to revert to their historical average of 18 percent of gross domestic product, the dollar amount would be \$2.8 trillion, 14 percent more than actual 2012 revenue.

Meanwhile, spending has more than doubled since 1998, a result of two wars, new entitlements, the worst recession since the Great Depression, multiple bailouts and a White House occupied in succession by a compassionate conservative (Republican George W. Bush) and an even more compassionate liberal (Democrat Obama).

### **Cutting Antonyms**

Looking at projections under what most analysts view as a draconian, recession-inducing scenario -- the \$600 billion fiscal cliff of automatic spending cuts and tax increases -- total spending continues to rise, according to the Congressional Budget Office's 10-year budget outlook.

Even with \$1.2 trillion of discretionary spending cuts over 10 years as mandated by the Budget Control Act of 2011, outlays would reach \$5.5 trillion in 2022, 22.3 percent of GDP, the same result as Obama's proposed budget fix. If Congress were to extend all the Bush-era tax cuts and other special perks, government spending would hit \$6 trillion in 2022.

Even someone following the budget negotiations closely might be surprised to learn that there are no real cuts on the table in the way normal people think of them. That goes for Republican proposals, too. For example, households may decide to reduce their holiday spending this year from \$750 to \$500 and forgo the summer family vacation because times are tough. Those are spending cuts.

Washington is the only place where a cut isn't a cut. Instead, so-called spending cuts are reductions in the growth rate of outlays as prescribed under current law. Nothing is cut.

Starting from current levels, if future spending were to grow at the rate of inflation plus the rate of population growth, 2022 outlays would be \$4.8 trillion, according to Michael Tanner, a senior fellow at the libertarian Cato Institute in Washington. In other words, less than the feared fiscal-cliff outcome.

For all of Obama's insistence on raising top tax rates, the additional revenue he seeks doesn't begin to solve the nation's fiscal problems. By 2022, just three programs -- Medicare, Medicaid and Social Security -- will consume 54 percent of the federal budget, up from 44 percent now, Tanner said. And "the real explosion of entitlement costs takes place just outside the 10-year budget window."

The Democrats' talk of "cuts" to these programs, which provide a social safety net for many Americans, is also misleading. Again, these are cuts in the accelerating growth rate of these programs. And if the projected savings from Obamacare don't materialize, the outlook is even worse.

### **Budget Lingo**

A glance at the historical budget tables published by the White House Office of Management and Budget puts all the talk about spending cuts in perspective. Nominal federal outlays fell by \$61 billion, or 1.7 percent, in 2012, the first outright reduction since the huge post-World War II declines in 1946- 1948. Inflation-adjusted spending has shown only a handful of year-to-year declines, all small, in the decades since the post-war demobilization.

As Tanner noted, inflation and population growth argue for nominal spending increases. But outlays topped 24 percent of GDP in each of the last four years, the highest by far since World War II and well above the 20 percent historical average.

Ever since the election, the president has campaigned to raise taxes on the rich, or families making more than \$250,000 a year. He has encouraged audiences to write to their representative in Congress in support of what he says is his election mandate.

Obama needs to ask something more. First, he should explain that there's a wide gap between the benefits to which Americans have become accustomed, especially those for the elderly, and the tax revenue needed to pay for those services. In other words, Medicare as we know it isn't an option.

Then the president should ask the question: What do you want, and how much are you willing to pay for it? It's something Americans are going to have to decide in the not-too-distant future, so we better start thinking about it now.