



National Security Report

Background and Perspective on Important National Security and Defense Policy Issues,

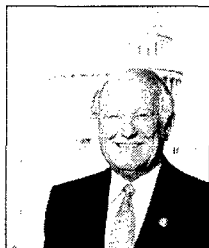
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The FY2000 Defense Budget: Gambling with America's Defense

The following text is adapted from Chairman Floyd D. Spence's opening statement at a February 2, 1999 House Armed Services Committee hearing with Secretary Cohen and General Shelton.

On February 1st, President Clinton delivered his defense budget to Congress, officially beginning the fiscal year 2000 defense budget cycle. Although U.S. military forces continue to confront a series of worsening problems, the President's admission last fall that the services are facing serious quality of life,

readiness and modernization shortfalls, and his recognition that increased defense spending will be necessary to address them, marked an important milestone in the defense debate.

Indeed, the President has taken a small step in the right direction by proposing

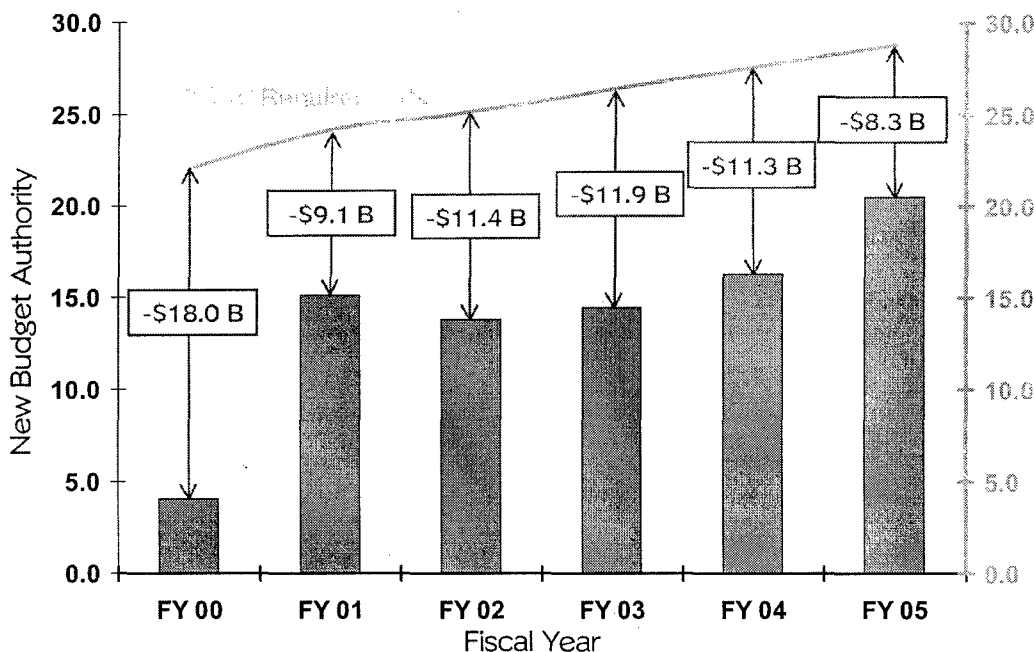
increased funding for defense, including an \$84 billion dollar top-line increase over the next six years. Unfortunately, the President has indicated that \$80 billion dollars of this increase is predicated on social security

reform as well as on renegotiation of the Balanced Budget Act. With fairly significant "strings" like these attached, it is difficult to judge just how sincere the President is about addressing even the Chiefs' unfunded requirements.

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Real Requirements - Continued Shortfalls

Budget Authority in Billions of Current Year Dollars



NOTE: Requirements expressed as additions to the FY 99 President's Budget per Joint Chiefs' Testimony

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The President's FY2000 defense budget falls at least \$18 billion short of what the nation's military leaders have identified as unfunded requirements in the coming year, and nearly \$70 billion short over the next six years. This chart illustrates the gap between the Joint Chiefs of Staff's unfunded requirements and the President's defense budget proposal.

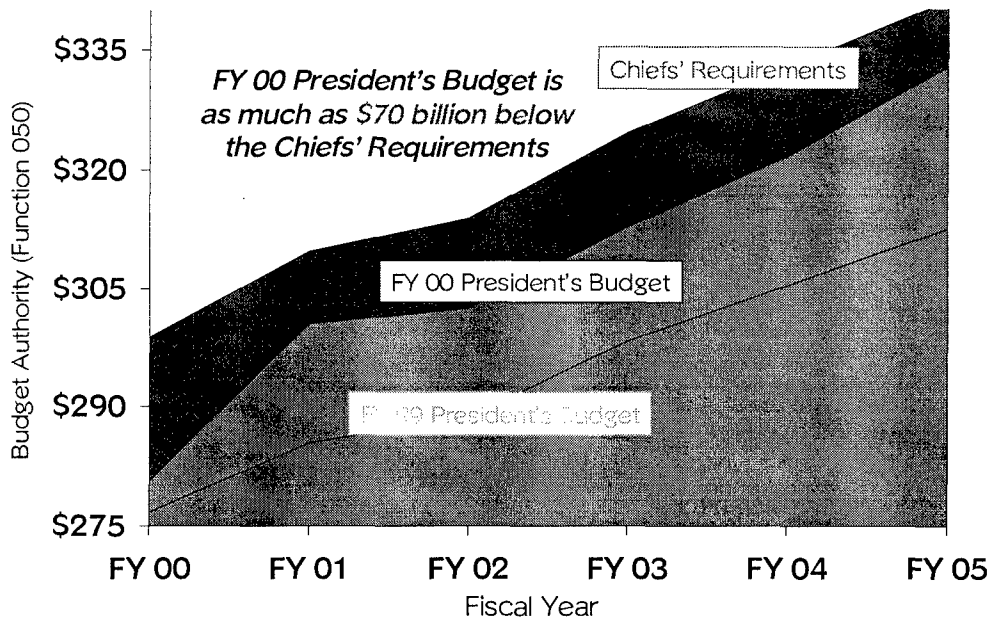
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Real Requirements - Continued Shortfalls

Budget Authority in Billions of Current Year Dollars



NOTE: Requirements expressed as additions to the FY 99 President's Budget per Joint Chiefs' Testimony

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Even if the \$84 billion in new budget authority proposed by the President materializes (in grey), the President's budget falls \$70 billion short of the Joint Chiefs of Staff's unfunded requirements (in red).

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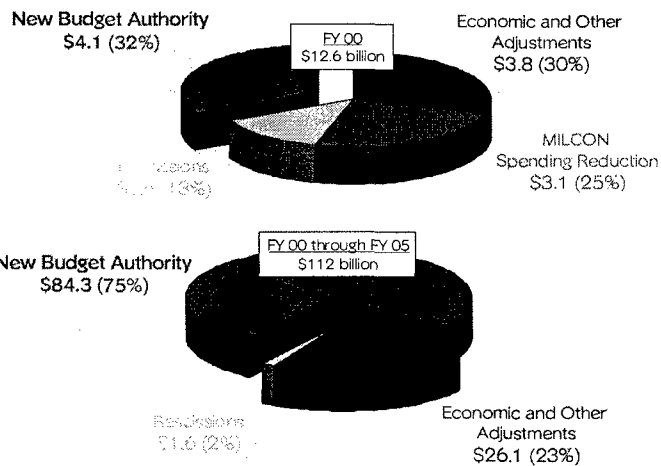
The bottom line is clear, this budget falls well short of adequately addressing the unfunded requirements of the U.S. military.

Simply put, this budget does not represent a \$12 billion dollar increase in fiscal year 2000, nor is it a \$112 billion dollar increase over six years. Instead, it contains a \$4 billion dollar increase in fiscal year 2000, \$2.9 billion dollars of which is suspect, and an \$84 billion dollar increase over the six year plan. The difference is about \$28 billion dollars worth of assumed savings and reductions from *within* the budget, which in no way represent increased top-line spending.

Last fall, the military service chiefs identified more than \$150 billion dollars in critical unfunded requirements, a figure likely to be understated, since several of them have since noted that problems are getting worse. Even if every dime of the Administration's assumed savings from within the budget materialize - from inflation to fuel to BRAC - the six year

Breaking Down the President's Defense "Increase"

Budget Authority in Billions of Current Year Dollars



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The President's FY2000 defense budget proposal has been characterized as an "increase" of \$12.6 billion. In fact, only \$4.1 billion is new spending, while the remaining \$8.5 billion reflects assumed savings, cutbacks, and gimmicks. Even the \$4.1 billion in new budget authority is suspect, as much of it may be predicated on a budget gimmick. Furthermore, the \$84 billion in new budget authority proposed for the next six years is entirely predicated on renegotiation of the Balanced Budget Act's spending caps.

plan still falls more than \$40 billion dollars short of meeting the services' requirements — which translates, on average, to about \$7 billion dollars per year. If the assumed savings do not materialize, the six year plan is almost \$70 billion short, or nearly \$12 billion dollars per year.

Furthermore, despite the Administration's assertion that this budget represents the first sustained defense increase since 1985, two of the next three budgets (including the fiscal year 2000 defense budget) fail to keep pace even with record low inflation. They represent real decline. Indeed, there is no sustained growth in this

budget proposal until beyond fiscal year 2003, which occurs after both the President's term and the Balanced Budget Act expire. In fact, more than \$50 billion of the proposed top-line spending increase occurs after the Balanced Budget Act expires and on the watch of a future Administration.

Unfortunately, the picture is clouded further by the fact that the budget relies heavily on assumed savings, spending cuts and outlay gimmicks.

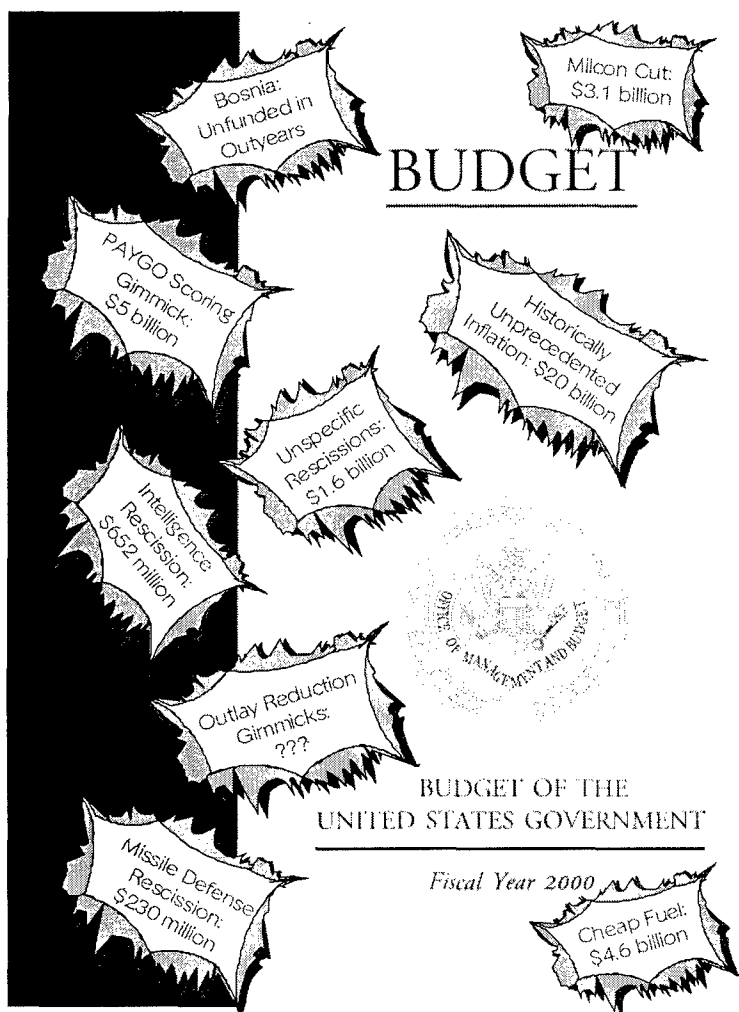
For instance, the Administration's defense budget repeatedly "gives with one

hand while taking away with the other." In order to fit the budget under next year's spending caps, the President's budget would rescind \$1.6 billion dollars of prior year defense spending — no specifics, just a cut. Of particular concern, the outlays associated with such a rescission would result in many more billions of dollars in reductions (certainly more than \$1.6 billion) to the investment accounts.

Also tucked away in this budget proposal is a rescission of almost \$900 million dollars for missile defense and intelligence funding agreed to by the President in last fall's omnibus appropriations bill. According to the Administration, these rescissions would be used to offset the costs associated with the Wye River Agreement. Although the Administration has assured Congress that these funds will be reprogrammed in the outyears, future spending will have to come out of someone's "hide." In essence, the Administration is breaking last fall's budget "deal," sacrificing congressional priorities, and making DOD pay for it twice.

On another front, the Administration's budget goes to great lengths to

Holes in the President's Budget: Billions in Assumed Savings, Spending Cuts, and Gimmicks



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The "MILCON Massacre" will decimate military construction accounts, compel a construction freeze, and will almost certainly increase costs.

demonstrate its commitment to taking better care of the troops and their families by including a robust package of pay and retirement proposals. Yet, this same budget proposes to cut an already anemic military construction program by a whopping 40 percent next fiscal year. This \$3 billion "MILCON massacre" is apparently an effort to "fix" a budget was \$3 billion dollars short of the desired \$12 billion "increase" in fiscal year 2000. This shell game will decimate the military construction accounts, compel a construction freeze (or worse), and will

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Gambling on the Economy - Inflation

derived from annual defense purchases BA deflators - budget authority in billions of current year dollars

Savings from revised defense purchases inflation assumptions

	FY 99	FY 00	FY 01	FY 02	FY 03	FY 04	FY 05	Total
Savings (billions)	-	2.5	2.9	3.1	3.4	3.7	4.0	19.6

Average annual defense purchases inflation rate assumed in the President's Budget for Fiscal Years 2000 through 2005:	1.8%
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Average Annual Defense Purchases Inflation since 1990: 2.0%
 since 1980: 3.4%
 since 1970: 4.9%
 since 1960: 4.3%

The President's Budget assumes the longest period of unprecedentedly low inflation since the Korean War

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almost certainly increase the costs of hundreds of construction programs.

In the area of contingencies, the Administration's six year plan funds Bosnia operations for only about the first 18 months of the six year plan. Unless the Administration has decided to pull the ground troops out of Bosnia in fiscal year 2001, billions of dollars for future Bosnia costs are unfunded and will have to be budgeted later. The Administration has not yet announced whether these funds will come "out of the services' hides," or whether the President will provide resources above the current top-line.

Finally, the Administration's budget includes \$25 billion in assumed economic savings based on lower than anticipated inflation and fuel costs. Most accountants would agree that it is one thing to "bank"

such savings *after* economic assumptions have proven inaccurate, and quite another to project the sustainment of historically unprecedented economic conditions six years into the future and to build the hoped-for savings into the services' budgets. To count on \$25 billion in inflation and fuel savings as the source of future funding for critical defense needs is a gamble. If these savings fail to materialize, where will the funding necessary to fill in the hole come from? Unfortunately, the services' unfunded requirements are real, but the savings may never be.

While the Administration's budget may look good, one does not have to scratch very deeply to reveal serious problems — from being \$70 billion short of the Chiefs' requirements to a heavy reliance on assumed savings, spending reductions and gimmicks. If each annual budget submission in the years ahead

relies as heavily on assumptions and gimmicks as the fiscal year double zero budget appears to, the services are in trouble. Even a cursory look at the Administration's budget indicates a number of outlay problems that are being dumped onto Congress's lap. If recent history is any judge, CBO will score this budget \$4 - \$5 billion higher in outlays than will OMB. Furthermore, this budget increases spending by more than \$8 billion dollars in the high outlay personnel and O&M accounts, yet total outlays for the entire budget function decline by about \$3 billion dollars. This fact alone is a warning flag that there is some "creative accounting" ahead. In the context of an already serious CBO/OMB outlay scoring mismatch, this kind of creative accounting could easily necessitate \$12 - \$15 billion dollars in budget authority reductions to the President's request just to stay within the spending caps.