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The Belden Center for Private Enterprise Education
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The entrepreneur

This issue courtesy of Eugene Smith, President, G.T. Press, Dallas, Texas.

A Program For Reducing The Federal Budget

Staying On Top Is Harder Than Getting On Top

The Harding University Economics team will attempt to win its sixth first place trophy at the National Students for Free Enterprise Competition next summer. The university economics teams have won first place eight times at the regionals and five times at the nationals which were started in 1978. Harding teams, the winningest in the country to date, were national runners-up in 1978 and 1983.

The 1986 team is composed of Kevin Thompson, co-captain from San Diego, California; Stephanie Carter, co-captain from Bentonville, Arkansas; Melissa Brenneman from Spartanburg, South Carolina; Glenda Collier from Memphis, Tennessee; Bruce Picker from Searcy, Arkansas; Joel Reed from New Haven, Indiana; and their sponsor, Dr. Don Diffine, professor of economics and director of the student-staffed Belden Center for Private Enterprise Education.

1986 Free Market Calendar A Daily Chronicle Of Enterprise

In a joint venture project with Louver Manufacturing Company (Lomanco) of Jacksonville, Arkansas, the Harding University Students in Free Enterprise Economics Team has launched a major project: "The 1986 **FREE MARKET CALENDAR — A Daily Chronicle of Enterprise.**"

The 1986 **FREE MARKET CALENDAR** offers 365 brief reminders of great enterprising events and relevant comments on the idea of freedom applied to the marketplace. It should hang on the walls of offices, factories, and school rooms all over the country. A limited amount of copies are available for $2.00 to cover printing, postage, and handling costs.

by
Murray L. Weidenbaum, Director
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The annual budget debate has become a sad spectacle. We all know what has to be done — and neither the Congress nor the White House is doing it. It is not a question of bringing an outlandish $200 billion deficit down to merely an outrageous $180 billion or a bloated $150 billion annual level. It is a matter of restoring our country's finances to some semblance of order.

If anyone has any doubt as to whether those large budget deficits merit strong action to reduce them, he should take what I call the "peanut test": What would have happened if Jimmy Carter had proposed the same $200 billion deficits? Why, he would have been tarred, feathered, and run out of town on a rail.

Are we so partisan as to believe that Democratic deficits are malignant but Republican deficits of the same magnitude are benign? Indeed, there is enough blame to extend to both sides of the political aisle and to both ends of Pennsylvania Avenue. And it will take strong bipartisan support to get the deficit back merely to the double digit level of the 1970s.

To be sure, recent experience has shown us that $200 billion deficits do not spell the collapse of the American economy. Yet I am not of the school of thought that claims the effects, albeit severe, will only occur in the distant future. To be convinced that deficits do matter, we need only to get out of our offices and look around. We know which sectors have been hardest hit by the resultant high interest rates and strong dollar: (1) agriculture, the most capital-intensive part of the economy, and (2) traditional durable goods industries, which find it difficult to compete with foreign firms that benefit from the low exchange rate of their local currencies.

I concede that you can fuel lots of fascinating academic disputes by trying to measure precisely how much of our economic problem is due to those budget deficits. The key fact remains, however, that curtailing the deficit is the basic responsibility of the Congress — it is the key economic lever that the legislators control directly.

ECONOMIC GROWTH AND DEFICITS

To those who contend that economic growth will cure our fiscal problems, I respond that the deficit is more likely to reach $300 billion during the 1980s than $100 billion. The next recession — which we can neither pinpoint nor rule out — will push the budget deficit to a new peak. History argues for at least one more recession in the 1980s. It will only take a downturn of average duration to accelerate government spending and slow down revenue sufficiently to produce a $300 billion deficit.

Our supply side friends tell us that we might as well take an extremely optimistic view because economists are not very good at forecasting the future. The official forecasts of various administrations have been somewhat short of perfection, usually substantially overestimating the rate of economic growth, but occasionally underestimating it. However, the prevailing forecasts of experienced private analysts have been relatively close to the mark.

In the Fall of 1982, for example, private forecasters projected a 3.2 percent rate of economic growth for 1983. The actual figure was 3.7 percent — not too far from the mark. In the Fall of 1983, most private forecasters projected an acceleration in the pace of the recovery in 1984; the Blue Chip figure was 5.1 percent. The speed up occurred, even more rapidly, at a rate well over 6 percent. Again, the forecasts were a good indication of the future direction, but surely did not achieve pinpoint accuracy.

Today, most experienced forecasters are projecting a slowdown in the pace of economic growth to 3.5 percent. It is premature to evaluate that number, but the direction of change certainly seems reasonable. In any event, the accuracy of recent predictions provides no basis for requiring economic forecasters to rend their garments, don sackcloth and ashes, and recite the Book of Lamentations — as some critics suggest.

Even on the basis of the more optimistic projections contained in the January budget — and after all the spending cuts proposed by the Administration — the deficit for fiscal 1986 is estimated at $178 billion. That is $3 billion higher than the 1984 level and only modestly below the total anticipated for the current year.

The way to reduce deficits is not to increase the burden on the taxpayer but rather to curb the many ineffective programs in the budget.

Thus, it will take additional action to bring those deficits down significantly. Having participated closely in the preparation of the budget in several administrations, I have come away with the abiding belief that the correct response is not to increase the burden on the taxpayer, but rather to curb the many low-yield, postponable, and ineffective programs that remain in the budget.

FISCAL 1986 SPENDING

Let us turn to the fiscal 1986 budget. The new federal budget is a good news, bad news document. The good news is that, finally, some large fiscal bullets are being bitten. President Reagan is proposing real, substantial cuts in government spending. The bad news is that the federal deficit will remain in the neighborhood of $200 billion a year for the rest of the 1980s. Remember, that pessimistic finding is grounded on two optimistic assumptions: (1) upbeat but reasonable forecasts of continued economic growth for the next several years and (2) the approval by Congress of $50 billion of proposed cuts.

We need to get the budget under better control. Nobody's first choice is to raise taxes. A comprehensive round of outlay reductions is required. The fiscal 1986 budget, although a good start, is inadequate.

Most of the attention is being given to the proposed reductions from the fiscal 1986 levels of spending. That ignores the spending growth that has taken place since 1980. In the past four years, many budget categories have mushroomed, and they are continuing to grow rapidly in fiscal 1985.

Many program areas have grown much faster than the 30 percent rise in rate of inflation since 1980. In this five year period, national defense outlays are up 89 percent, foreign aid and other international programs are up 60 percent, social security and medicare are up 71 percent, and farm programs (mainly subsidies) are up 291 percent.

I find little to criticize in the specifics of the proposed budget cuts for 1986, as far as they go. I strongly endorse these proposals to slay or at least wound many sacred cows.

But it is also clear that — even if all the proposed cuts are approved — expenditures for many programs will continue to be far above the amounts devoted to those purposes at the beginning of this decade. For example, the proposed "cutback" in farm subsidies would still leave annual outlays for that program at a level 182 percent above 1980 — far more than necessary to offset the effects of inflation.

Thus, when President Reagan says, "You ain't seen nothing yet," that statement could properly be applied to the current effort to control federal expenditures.

The key to dealing with the deficit problem is not to emphasize the hole in the doughnut — the painful cuts that are being proposed. Rather, policymakers need to carefully examine the doughnut itself — the many doubtful items of federal expenditure that remain in the budget. For every sacred cow that is now being offered for slaughter, another remains shielded from the federal budget knife . . . The best way to reduce the deficit — and to lay the foundation for responsible tax reform in the years ahead — is to carry through that necessary pruning of federal spending programs.

In expanding the current focus of budget cutting, the Congress should consider the unevenness of budget restraint to date. The proposed reductions or eliminations in SBA, Export-Import Bank, etc., are severe — although, in my view, desirable. But if these special-interest programs are to be curtailed, what about the many other special-interest activities that have survived budget review?

If the budget cuts are considered unfair, it is not because they cover too many programs, but too few.

For example, in some federal lending programs the interest rate is so low that it is equivalent to forgiving half or more of the loan — 66 percent in the case of Bureau of Reclamation credit. If the budget cuts are considered unfair, it is not because they cover too many programs, but too few.

If it is desirable to reduce farm subsidies — and I believe it is — why is the Federal Government continuing to authorize new Corps of Engineers projects which will increase the amount of land on which surplus crops will be raised? Why phase out general revenue sharing — which comes with few strings attached — but only make modest reductions in categorical grants to states and localities? Can it be that the federal agencies, when we get down to the wire, are more concerned with keeping control over state and local governments than with reducing the deficit?

A SPECIFIC PLAN FOR BUDGET CUTTING

Here are six specific proposals to achieve comprehensive budget cuts.

Slow down the rapid pace of defense spending. The target for defense spending announced in the 1980 campaign — 5 percent a year increase plus allowance for proposed inflation — has been overshot substantially. Surely our defense posture has not deteriorated since 1980. Large reductions in new appropriations are needed to return the Pentagon's spending level to the original trendline — 5 percent real annual growth from 1980. Rather than the $277.5 billion of outlays projected for fiscal 1986, this would infer holding to $234.6 billion, a reduction of $42.9 billion.

The Pentagon's purse strings need to be tightened in order to serve the goal of good management of federal money. The Department of Defense is scheduled to end fiscal 1986 with over $55 billion of unused appropriations. The technical term is "unobligated balances."

That sum is more than the total amount that will be used (committed or "obligated") in the entire fiscal year by the Departments of Commerce, Education, Energy, Interior, Justice, Labor, State, and Transportation. There will be enough left over to finance all of the operations of the Congress, the Judiciary, the Executive Office of the President, the Environmental Protection Agency, the General Services Administration, and the Small Business Administration and over $1 billion of miscellaneous activities. This is a clear indicator of the generous cushion in military budgets.

The most harmful effect of the runaway military budget is not the adverse economic and financial results, such as higher interest rates. Instead, it is the erosion of public support for the defense establishment. In the dangerous world in which we live, it troubles me to see the sharp shift in sentiment on this matter over the last four years.

At the beginning of this decade, public opinion polls consistently showed strong support for increasing the military budget. The National Opinion Research Center reported that, in 1980, 56 percent of the public thought that not enough money was being spent on defense.

That attitude has changed dramatically. The same poll shows a strong shift in sentiment toward cutting defense spending. In 1984, only 17 percent of the American public believed that the United States is spending too little on defense. A Harris poll in early 1985 has that figure down to 9 percent. This compares to 88 percent who favor no increase at all or even a reduced military budget.

Secretary of Defense Caspar Weinberger loves to remind us that we cannot balance the federal budget simply by reducing military outlays. He is right, but substantial defense cuts are an essential ingredient of any successful effort to reduce overall federal spending. Otherwise, supporters of civilian programs that are being cut can properly raise the "fairness" issue; at the same time, voter support for defense spending will continue to erode.

Eliminate the COLAs in entitlements. It is time to acknowledge that the public has an erroneous concept of "social insurance" programs. Social security recipients believe they are "entitled" to their monthly checks because they paid for them during their working years. The truth of the matter is that most of the people on the social security rolls have long since gotten back all they paid in — plus employer contributions and interest. The difference is made up by the generation now working. Is that the economic equivalent of welfare? Yes, it is.

Retroactive benefit increases for cost-of-living allowances (COLAs) are not part of most private insurance systems. The beneficiaries did not pay for them. Thus nobody is "entitled" to them. The Congress should begin to reduce and then to phase out automatic annual cost-of-living benefit increases. Such action would also increase public support for continued actions against inflation.

Apply some insurance principles to Medicare. Every automobile insurance policy has a deductible in it to avoid overwhelming the system with minor claims. The same approach should be used in health insurance, notably Medicare. A recent survey of 250 large corporations reported that 52 percent already require their employees to pay some deductible for medical expenses. A greater use of cost-sharing would force hospitals and physicians to think of the individual patient and not big government in incurring costs and making charges.

Eliminate the "double whammy" in federal lending programs. The demand for federal credit programs continues to grow rapidly. These activities have been typically set up because some people are not deemed credit worthy by private financial institutions. To grant that type of aid is a political judgment properly made by Congress. The catch is that these credit programs almost always loan out the government's money at interest rates much lower than private lenders charge — lower even than the Treasury pays for the money in the first place.

These interest rate subsidies are more than an expensive extra "goody." They encourage people to get government loans, rather than to look to private credit markets or to their own resources. As a minimum, federal credit programs should charge the same interest rates as the Treasury pays. Ideally, they should match the going rate in competitive financial markets. That would really reduce the demand for federal loans.

Phase out subsidies to businesses and farmers. The average taxpayer has a lower income than the beneficiaries of most federal programs aiding agriculture and industry. The small family farmer does not receive much of these large subsidies. It is hard to justify these outlays when we learn that they result in such inequities as the American consumer paying 20 cents for a pound of sugar when the world price is less than a nickel.

Similarly, most businesses — small and large — do not benefit from the government's assistance to a lucky few firms. Getting interest rates down via budget cuts would do the most good for farmers and business firms alike.

Do not ignore the many other areas where spending continues to grow rapidly. For example, in the supposedly bare bones budget for fiscal 1986, outlays for foreign military aid are up 215 percent over 1980. Civilian space support activities are up 148 percent. The highly-publicized proposed cuts notwithstanding, housing assistance is up 124 percent. USIA and other foreign information activities are budgeted for a 95 percent rise over 1980, and the State Department for an 80 percent increase.

Where should the Congress stop in making budget cuts? An adequate and comprehensive budget restraint effort should be based on the old maxim, "Good budgeting is the uniform distribution of dissatisfaction." Not enough of the spending agencies and their supporters are dissatisfied.

I know that I am urging the Congress to make many tough and even initially unpopular decisions. But the meter is running. Interest payments are mounting steadily. Delay means choosing in the future between even larger and tougher spending cuts and substantial and more unpopular tax increases. Every examination of the soft spots in the budget shows that they do not deserve being funded by increasing the tax burden on the American public. The only satisfactory answer to a budget that is fundamentally out of control is to control it now!

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