

The Defense Budget's Double Whammy: Drawing Down While Hollowing Out from Within

By Clark A. Murdock, Kelley Saylor, and Ryan A. Crotty

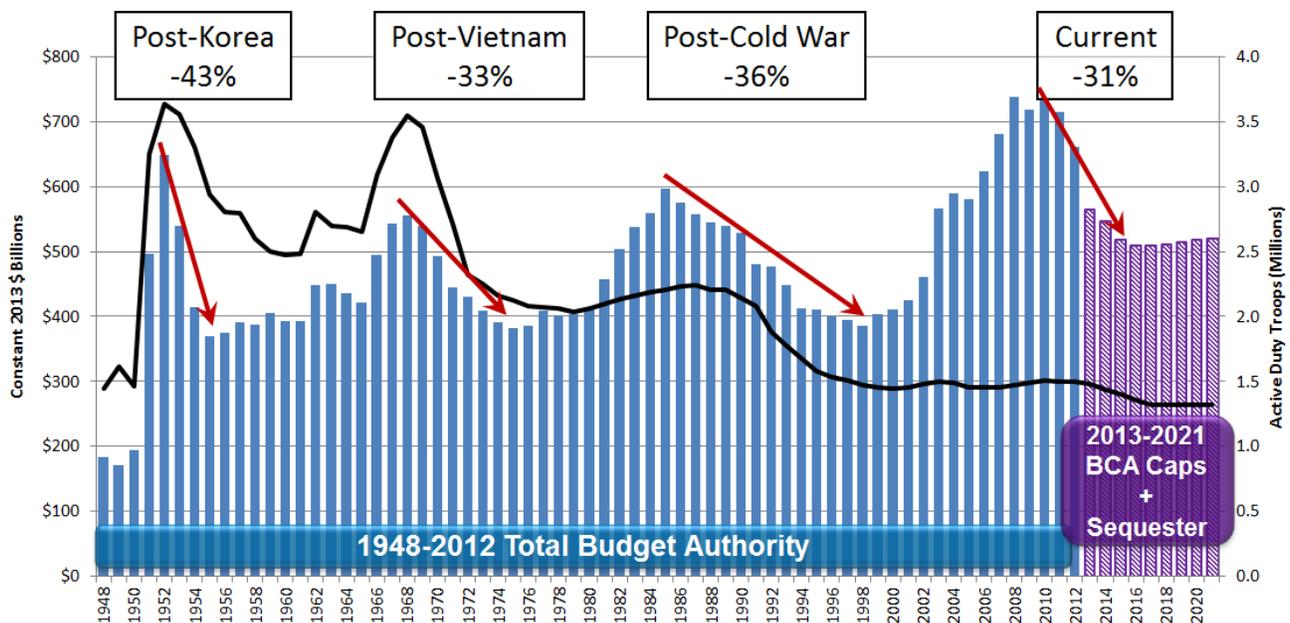
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A Falling Topline

After a decade of steadily increasing defense budgets—the base budget of the U.S. Department of Defense (DoD) increased about 40 percent in real terms from 2001 to 2012—DoD must reduce spending by \$487 billion from FY2012–FY2021 in order to comply with the Budget Control Act of 2011 (BCA). If sequestration is triggered—as it will be on January 2, 2013, in the absence of a “grand bargain” or alternative act of Congress to address deficit reduction—it will impose approximately \$500 billion in additional defense budget cuts from FY2013–FY2021.

While the prospect of a drawdown of this magnitude has raised alarm bells inside DoD, prompting official predictions of an impending “disaster” or “catastrophe,” the combination of BCA caps and sequester cuts would result in a defense budget drawdown of about 31 percent from the FY2010 peak to the FY2017 trough, resulting in a drawdown that is actually below the historical range (from 43 percent after the Korean War to 33 percent after Vietnam [see Figure 1]). This cut is significant to be sure, but it does not reach that of previous postwar drawdowns.

Figure 1: Defense Drawdowns Compared



Note: Topline in out-years includes the Congressional Budget Office (CBO) estimate of overseas contingency operations (OCO) based on a phased drawdown to 30,000 troops in 2017 and remaining flat thereafter.

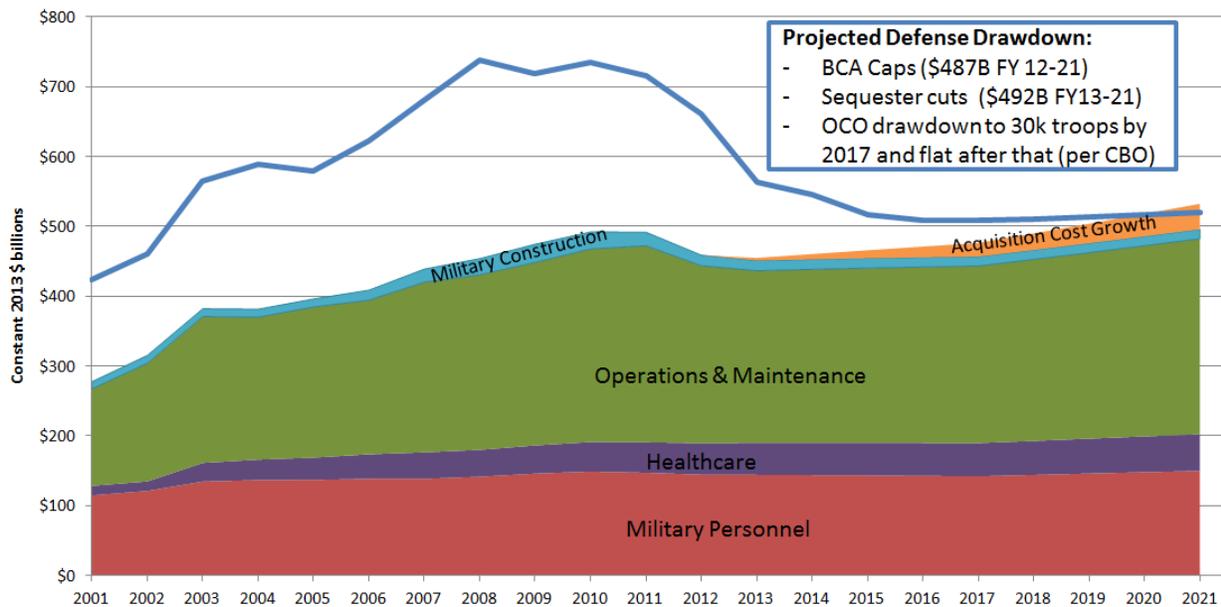
A Hollowed-Out Defense Budget

Figure 1 highlights the difference between the current drawdown and previous ones: the reduction in the topline is to \$500 billion (in constant 2013 dollars) as opposed to the \$400 billion of past drawdowns, even though the number of active-duty service members has declined consistently from roughly 2.5 million in the early 1960s to 1.36 million (projected) in 2016. Indeed, in 2016, DoD will be spending about \$100 billion more for an active-duty force that is 34 percent smaller than it was in 1978 and 6 percent smaller than in 2000.

Thus, this drawdown will be much more serious than those of years past. Why? Because the aggregate impact of inflation in the cost of personnel, health care, operations and maintenance (O&M), and acquisitions results in a defense dollar that “buys” less and less capability.

This internal cost inflation is driving DoD toward a zero-sum trade-off between personnel end-strength and modernization (see Figure 2).

Figure 2: Internal Cost Inflation against the Projected Defense Topline



Among the largest contributors to internal cost inflation is the military personnel (including health care) account. As DoD’s own [“Defense Budget Priorities and Choices: January 2012”](#) has noted, “the cost of military personnel has grown at an unsustainable rate over the last decade... Within the base budget alone... personnel costs increased by nearly 90 percent or about 30 percent above inflation [since 2001], while the number of military personnel has increased by only about 3 percent.”

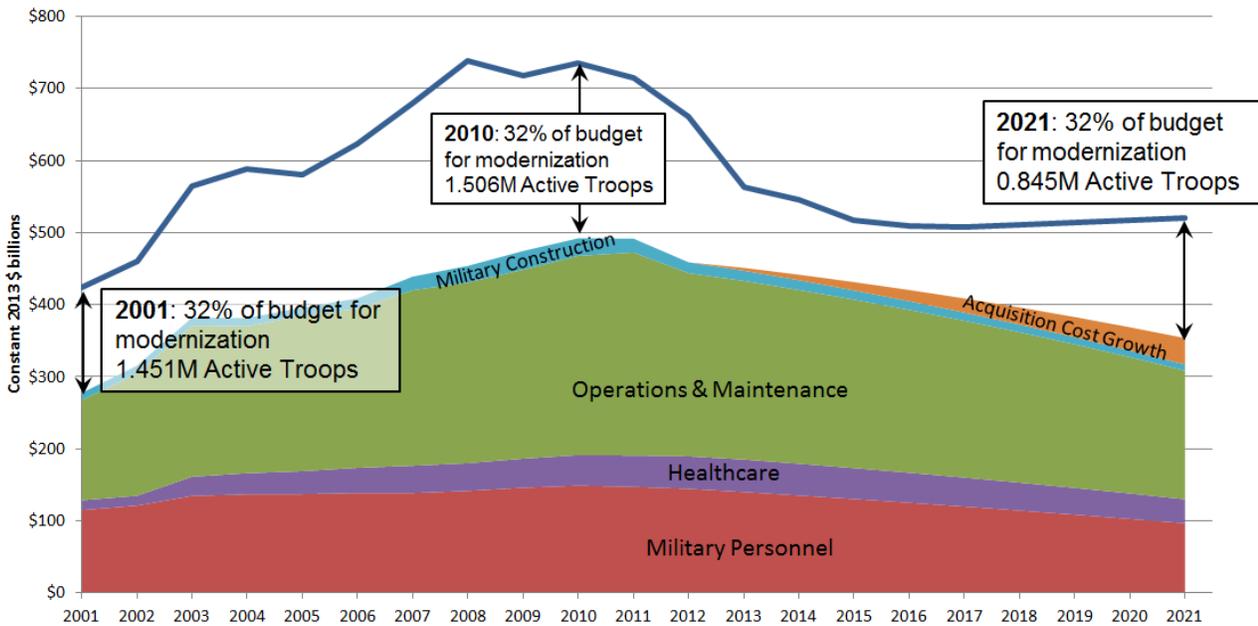
Operations and maintenance (O&M) costs have similarly ballooned over the past few decades. The Congressional Budget Office (CBO) reports in [“Long-Term Implications of the 2012 Future Years Defense Program”](#) that O&M costs per active-duty service member doubled from \$55,000 to \$105,000 (in constant 2012 dollars) between 1980 and 2001. These costs rose to \$147,000 in DoD’s 2012 base-budget request and were projected to “grow at more than one and one-half times the historical (pre-2001) rate through the Future Years Defense Program (FYDP) period, reaching \$161,000 in 2016.” While the rate of growth is expected to slow beyond 2016, CBO expects per capita O&M costs to reach \$209,000 by 2030.

In combination, inflation in these accounts will squeeze out all funding for modernization (procurement and research, development, test, and evaluation [RDT&E]) in 2020, as depicted in Figure 2, if current trends are allowed to continue. This will, in the absence of extensive reform, force DoD to choose between sustaining end-strength and sustaining modernization. It cannot do both.

The Zero-Sum Trade-Off

The CSIS study team calculates that restoring modernization’s share of the FY2021 defense budget to 32 percent (the level of effort in the FY2001 budget) would require cutting end-strength by 455,000 active-duty service members, leaving the services with an end-strength of 845,000 (see Figure 3). This zero-sum trade-off will produce far more severe and disruptive consequences than is generally recognized by the department, requiring, at the very least, a wholesale recalibration of U.S. defense strategy and force posture.

Figure 3: Restoring Modernization in the Base Budget



The Squeeze on Discretionary Spending

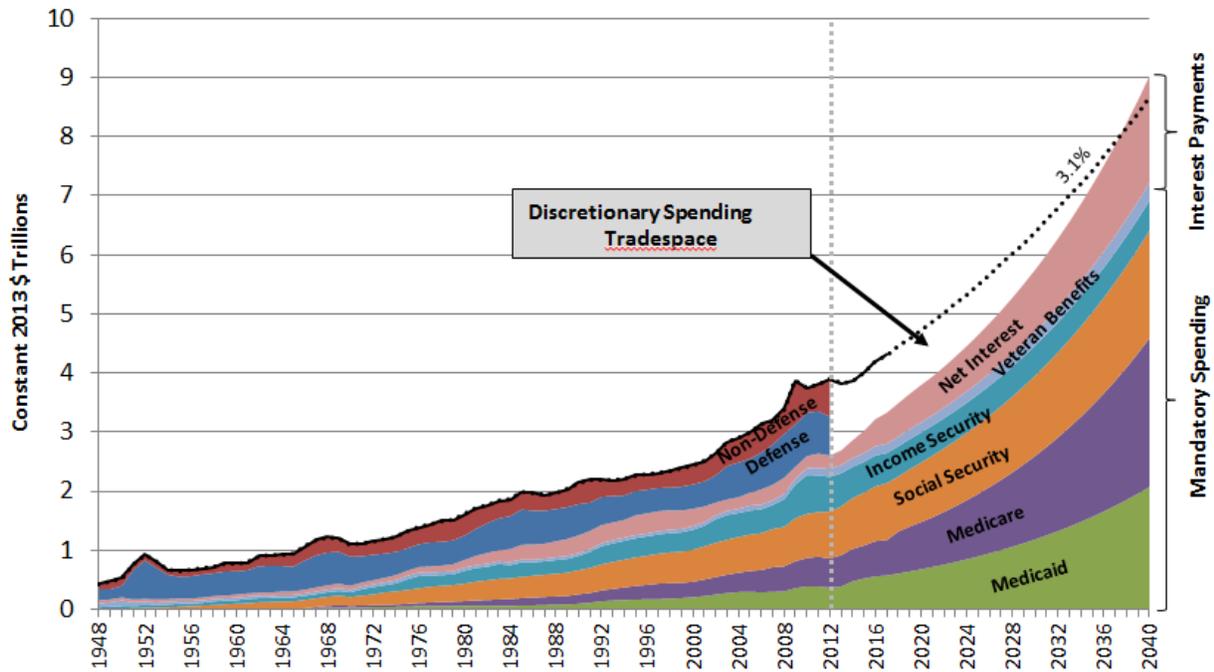
This choice between modernization and end-strength will almost certainly remain even if sequestration is averted by congressional action. This is because discretionary spending tradespace (for both defense and nondefense accounts) is being squeezed out by mandatory spending—which includes spending on veteran benefits, income security, social security, Medicare, and Medicaid—and interest payments. And given Democratic aversion to entitlement cuts and Republican antipathy to tax increases, the defense budget, which constitutes 54 percent of discretionary spending, will likely be forced to absorb additional reductions under any scenario. (Estimates of the scale of alternatives to sequestration range from a total of \$1 trillion to \$1.5 trillion. Senate Armed Services Committee chairman Carl Levin has suggested that an additional \$100 billion reduction over 10 years would be “realistic”.)

Regardless of the distribution of any cuts, however, mandatory spending and interest payments are expected to consume the entirety of the U.S. budget by 2036, leaving no discretionary tradespace for either defense or nondefense accounts (see Figure 4).

For this reason, DoD must undertake drastic and immediate measures to address the inflationary pressures that will otherwise crush the defense budget both from above and from within, as well as begin to prepare for a new reality of reduced means and difficult choices. Failure to do so will have profound consequences for the continued strength of the U.S. military and for U.S. security, as well as for the stability of the international system.

To help the DoD recognize, accept, and plan for the twin threats of fewer defense dollars and weaker defense dollars, the Defense Drawdown Working Group (DDWG) has proposed a cost-capped methodological approach for determining which military capabilities must be retained under a sequestration-level drawdown. This methodology is explained in detail in [“Preparing for a Deep Defense Drawdown: The Defense Drawdown Working Group and the ‘Cost-Capped’ Methodology.”](#)

Figure 4: Pressure on the Topline



Note: Topline assumes that total federal spending from 2018 to 2040 grows at 3.1 percent above GDP (the average annual growth rate planned for 2013–2017 in the FY2013 budget request).

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