

**The Scouting Report**  
**Obama's First Budget**  
**March 4, 2009**  
**Barry Bosworth and Fred Barbash**

12:29 Fred Barbash-Moderator: Our guest today is Barry Bosworth, Senior Fellow, Economic Studies, Global Economy and Development who holds the Robert V. Roosa Chair at Brookings.

A former presidential advisor, Barry Bosworth is an expert on fiscal and monetary policy, economic growth, capital formation, and Social Security. His recent projects include studies of U.S. saving behavior and economic growth in China and India.

Welcome Barry and welcome guests. Let's get going with your questions

12:29 Barry Bosworth: Hi Fred - thanks for having me. I look forward to answering guests' questions.

12:30 [Comment From Laurie] The pundits are all calling Obama's budget ambitious, and everyone seemed surprised by the scope of the numbers and the ambitious nature of the programs. What's your overall reaction to the budget?

12:30 Barry Bosworth: It is very ambitious, but it is common to propose a large number of programs in the first year of the new administration, but they are not going to be completed except over several years.

12:31 Barry Bosworth: While Obama discussed them in the election campaign, they are not issues on which there is any kind of consensus on the precise means of addressing them, so the President needs to start the conversation. It will lead to more detailed proposals, congressional hearings and debate; but enactment will absorb much of his term.

12:31 Barry Bosworth: As we have learned from the unfortunate delays with the stimulus program, nothing happens quickly. For the short run, attention will be concentrated to the economy, which is still spiraling down into a deep recession. Until that is fixed, we will not know how much we will have in the way of resources to addresses issues like, health, education and climate change. It is hard to make detailed budget plans in the midst of an economic disaster with falling incomes and rising unemployment.

12:31 [Comment From Martin] Is there an easy way to compare at the Department and Major Agency levels the proposed budget with their current year budgets? The President's Budget does not make that comparison except in some text commentary.

12:32 Barry Bosworth: Martin, not really. In April, when the full budget is released, there will be a supplemental chapter with full details on current services budgets for all the agencies.

12:33 Fred Barbash-Moderator: Barry: There's been some criticism about the assumptions for economic growth over the horizon underpinning the administration's budget. Do you think the OMB is being realistic?

12:34 Barry Bosworth: Fred, the future is always uncertain but I think they made a mistake to be so optimistic. Their forecast will become the standard by which Obama's economic program is deemed a success or failure. They set an extraordinarily high bar compared to outside forecasts.

12:35 Barry Bosworth: I know they want to be optimistic, but the president stressed the severity of the crisis and the difficulties in the future. Why promise such a rosy scenario? The latest GDP release for the 4th quarter of 2008 also gives evidence of a worsening situation.

12:36 [Comment From Daniel] How should Obama propose to raise new revenue? He's been talking about raising taxes for folks making more than \$250K/yr. Do you think this proposal has legs?

12:38 Barry Bosworth: That is principally a scheduled termination of a tax cut enacted during the Bush administration, Daniel. I do believe it's a reasonable first step but it leaves them with a large revenue gap. The tax cuts for middle and low-income earners will be paid for by revenues from a cap-and-trade carbon program which at this point Congressional passage is highly speculative.

12:39 Barry Bosworth: We may end up considering other newer broad-based taxes such as a value-added tax.

12:39 [Comment From Mark] When is it time to evaluate how effective Obama's economic policies are? How long is his "honeymoon" period?

12:40 Barry Bosworth: Mark, we should know something by next year at this time. The stimulus program is unfortunately delayed until the last half of 2009.

12:41 [Comment From Mark] It would seem that between the payment on the debt, and entitlement programs, there will be an enormous squeeze on discretionary spending - any thoughts on which agencies are going to be squeezed the hardest - is DoD untouchable?

12:41 Barry Bosworth: Discretionary spending has become so small, Mark, as a share of the total that cuts in that area cannot resolve the deficit.

12:42 Barry Bosworth: Defense will be subject to some changes in new program areas where the cost overruns have been excessive. But the basic level of defense spending will continue to be determined largely by what happens internationally.

12:42 [Comment From paul] Do you think Obama can really cut our deficit in half by the end of his first term?

12:43 Barry Bosworth: Paul, no.

12:43 Barry Bosworth: But I am more pessimistic on what I fear will become a terrible economic downturn. I don't understand why the Administration believes that the problems will be resolved by 2011.

12:44 [Comment From denise] It seems that Obama's budget proposal is pretty controversial. What kind of support does he have from members of Congress? Do any Republicans support his ideas?

12:45 Barry Bosworth: The key elements were fully discussed in the election, Denise. And the support seemed quite strong. The devil will be in the details.

12:47 Barry Bosworth: Reductions in carbon emissions, in particular, will be highly controversial. And Republicans have traditionally opposed any such program. Instituting a functioning carbon tax or cap-and-trade system will be difficult and I expect the debate to extend over a couple of years. Similarly, we have never been able to agree on how to reform our health care system. Even though we agree that the current system doesn't work well.

12:47 Barry Bosworth: At this point, Obama has articulated the goals but not the means. The question is what will happen to public support when he gets to the second step.

12:48 [Comment From Mark, DC] I keep hearing that there's really nothing the government can do to address the financial crisis – that it wasn't the New Deal that pulled us out of the last great depression, but really WWII. What's your view?

12:49 Barry Bosworth: I agree. Roosevelt did a lot to relieve suffering but the government was unable to enact the large fiscal actions required to end the Depression until the outbreak of war.

12:51 Barry Bosworth: The financial crisis, however, is a problem that has been faced by many other countries and the US in its own history. At present, that problem seems to be a lack of agreement to spend the large amounts that be required. However, we resolved the S&L crisis in a timely fashion but not without substantial public cost...which now looks like small potatoes.

12:52 Barry Bosworth: Japan is a good example of a country that dithered as we have over the past year. The lack of decisive action leads to a compounding of the problem of uncertainty in the markets and a systemic deterioration of expectations.

12:52 [Comment From Christine] What do you think of Obama's budget team? Does he have the right people around him? The right mix of advisors? Is he getting all sides of the picture?

12:53 Barry Bosworth: Christine, they seem fine but there's too few of them. The ones that have been appointed are experienced and largely centrist.

12:54 Barry Bosworth: The range of views is not as wide as in the Congress but I don't know that a president needs that within his own cabinet. He is certainly aware of the diversity of views that any budget proposals will face.

12:54 [Comment From Dave] What kind of role will china, its economy and its currency play in our nation's recovery?

12:56 Barry Bosworth: Dave, China has enacted a stimulus program that represents an even larger share of their economy than the one here in the US. But we both face enormous challenges. We cannot continue to consume more than 100% of our nation's

output and rely on foreign financing. We have to scale back our consumption and build an export-oriented economy. China represents the opposite extreme. It has to focus on expanding the domestic side of its economy.

12:57 [Comment From richard] Are you in favor of government bailouts of financial institutions?

12:58 Barry Bosworth: Unfortunately, yes, if there are large systemic consequences of their failure. But I do feel that they should pay a higher price. Leaving management in place and stock holders with a residual value makes it difficult to convince the public that these actions are reasonable.

12:59 [Comment From Bob] Re: WWII pulling us out of the Depression--that's the new conservative line, but what did WWII kick off if not MASSIVE government spending programs on bullets and tanks and an army of workers? Isn't it more accurate to say that Roosevelt's New Deal programs didn't spend ENOUGH, as borne out by the fact that after the '36 elections he had to pare them back and the economy went south again? Thanks.

12:59 Reader Poll: Do you think Obama's budget plan is realistic?  
Yes (50%)  
No (50%)

1:00 Barry Bosworth: I don't mean to respond that war was good! but solving a Depression requires spending on an extraordinary scale. Seemingly, countries are only willing to do it in the context of war. In the past decade, Japan has faced the same difficulties of convincing its citizens of the need for strong actions both in terms of fiscal stimulus and rebuilding the financial system.

1:01 [Comment From Ron in IL] What's up with all the talk about how Sweden handled their financial crisis? Is that an apt comparison?

1:02 Barry Bosworth: Yes, Sweden also made a huge mistake that ended in a financial crisis and most of its banks failed. The government is generally credited with a strong and effective response to rebuild the financial system and return the economy to growth; however, Sweden still went through a terrible recession and very large increases in unemployment.

1:03 [Comment From Vic] For years, politicians have been saying that the era of big government is over. Does this budget signal a fundamental change? Are people more willing to invest in a government role? Or is this just a response to the times we're in?

1:06 Barry Bosworth: Vic, I don't see the big change. To begin with, the government is dealing with a crisis with a series of hopefully temporary actions. The two major long-term problems -- health care and climate change -- are likely to be difficult but they shouldn't imply a large increase in the share of government in the economy. The cost of health care is already enormous and one objective is to reduce those costs; similarly the fundamental policy objective on climate change is to get people to cut back on emissions.

1:07 Barry Bosworth: If we use taxes or similar measures to increase the price of carbon emissions, it shouldn't require a larger government. I don't see the debate as fundamentally about the size of government.

1:08 [Comment From Jen] You've had a long and distinguished career as an economist. I wonder if you ever imagined that a crisis like this--of this depth--would occur?

1:09 Barry Bosworth: No. I did not see this coming and it is a defining event of our generation. Realistically, if Obama can lead us out of this disaster, he will go down as one of our great presidents, regardless of what happens with the rest of his program.

1:10 [Comment From erica] What do you think the biggest problem with Obama's budget is?

1:11 Barry Bosworth: At this point, the lack of details and the rosy assumptions I mentioned earlier. They are reserving funds for health reform but it is not at all clear what reform will consist of.

1:12 Barry Bosworth: As we said earlier, they may regret putting such a rosy outlook. It doesn't seem to match with the president's candor in his public statements.

1:12 [Comment From Chico] Who stands to gain the most from the budget? And who stands to lose the most?

1:14 Barry Bosworth: Chico, most fundamentally, all of us who need a job or want to keep ours are the beneficiaries. The budget does embody some shift in the distribution of taxes from a tax cut for low- and middle-income workers and a tax increase for those at the top of the distribution. But these are second-order effects compared to the gains of a program to successfully restore economic growth.

1:14 [Comment From Sammy] Can you please explain the risks of a rapid over inflation?

1:16 Barry Bosworth: I believe that inflation risk are rapidly fading, Sammy. At present, it would me more realistic to project a decline in prices. However, if the stimulus program should succeed, and the economy returns to a high-growth path, policies will have to be reversed. I believe that will be easy to do.

1:17 Barry Bosworth: The monetary authorities will be able to slow the growth in credit in such a world. We have learned that the monetary authorities are effective in pulling but not pushing on a string. The problem is that monetary policy is quite ineffective as a source of stimulus.

1:18 [Comment From Charles] Will the US ever be in the black again? Is it necessarily a bad things if we persist in deep debt indefinitely?

1:20 Barry Bosworth: Probably not in my lifetime. It only happened for a brief period at the end of the prior decade and immediately led to years of bad policy -- excessive tax cuts, budget deficits and risk-taking. A sustainable fiscal policy would be one that kept the debt at a constant share of our nation's income. That means that as a minimum, we have to reduce the deficit to about 3% of GDP.

1:21 Barry Bosworth: The current deficit is 12% of GDP and next year is projected at 8% so you can see we have lots of room to do better -- but Obama's budget projects a 3% balance by 2014. However, as I said, that strikes me as a rosy scenario. Three percent is a good target, though.

1:22 Fred Barbash - Moderator: OK, folks, we have time for just another question or two.....

1:23 [Comment From Chico] From your earlier answer you sound quite optimistic that the budgeted programs will restore growth. What kind of odds do you place on seeing "Obama-villes" popping up around in particularly poor areas?

1:25 Barry Bosworth: Chico, if they do pop up, I'd call them Bush-villes. But I think we know how to solve the problem. But we are unsure of its precise cost and how long it will take. We can do better than we did in the 1930s and there is a much better social safety net.

1:25 [Comment From rachel] Any chance I'll lose all of my money in Citibank? How long can the government really and truly back the banks?

1:26 Barry Bosworth: No, Rachel, you won't lose your money. But if I were you, I would not buy their stock.

1:26 Fred Barbash-Moderator: Barry: Thanks very much. This has been very productive and very enlightening. And thanks to all the guests.

1:27 Barry Bosworth: I also want to thank all the questioners, and thanks to you, Fred. I enjoyed this webchat :-)

1:27 Fred Barbash - Moderator: Please tune in next week at the same time for another chat!