

The Pentagon's budget

A superpower still has to set priorities

New
Economy

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The Bush administration's proposed spending plans for the Pentagon have produced a series of dramatic headlines around the world relating to an apparently unprecedented US defence build up. The fiscal 2003 budget request for the Pentagon fleshed out the budgetary details of Secretary of Defence Donald Rumsfeld's Quadrennial Defence Review (QDR), released on 30 September, 2001.

The QDR was a cautious document on the whole. While it unveiled several new initiatives, they were largely conceptual ones. It increased the military's emphasis on homeland security, as planned even before the attacks on the US on September 11th of that year. It also adopted a somewhat less demanding type of two-war scenario as the proper standard for sizing American armed forces. In addition, the QDR placed greater emphasis on missile defence, defence research and development, and joint-service training and experimentation.

However, the Bush defence review essentially reaffirmed the Clinton administration's weapons modernisation agenda and force

structure. After rampant early speculation that overseas troop deployments would be reduced, the size of US ground forces would be curtailed significantly and a generation of weapons programs would be skipped, Rumsfeld's defence plan proved far more cautious and far more consistent with that of his predecessors.

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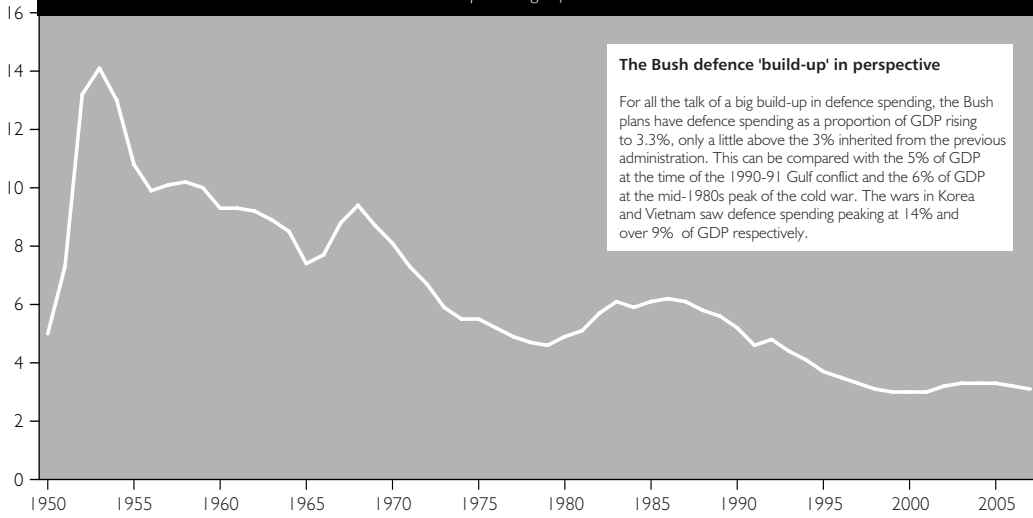
Funding the Bush strategy

The September review was silent, however, on the question of costs. Only with its budget proposal for 2003 and beyond, released in February 2002, did the Bush administration attach figures to the plan. Where the Clinton administration's national security budget had grown to about \$300 billion a year by 2001 (including about \$15 billion in annual funding for nuclear weapons activities at the Department of Energy), President Bush's budgets were \$329 billion in 2001, \$351 billion in 2002, and \$396 billion for 2003.

Equally striking are the price tags envisioned for the years ahead: \$405 billion (2004), \$426 billion (2005), \$447 billion (2006), and \$470 billion (2007). These budget plans show that the Bush administration is planning on

Figure 1 US defence budget 1950-2007

percentage of GDP



The Bush defence 'build-up' in perspective

For all the talk of a big build-up in defence spending, the Bush plans have defence spending as a proportion of GDP rising to 3.3%, only a little above the 3% inherited from the previous administration. This can be compared with the 5% of GDP at the time of the 1990-91 Gulf conflict and the 6% of GDP at the mid-1980s peak of the cold war. The wars in Korea and Vietnam saw defence spending peaking at 14% and over 9% of GDP respectively.

Source: National Defense Budget Estimate for FY 2003 March 2002
 Note: Revised economic forecasts may change the % GDP in future years.

the assumption that defence spending will climb significantly in future years.

In a sense, the increases are not quite as great as they seem. The figures for 2001-2003 include the costs of the anti-terrorism war. These combined costs are now running at about \$30 billion a year, not counting the costs of any possible war against Iraq. Moreover,

due to the effects of inflation, the \$470 billion budget for 2007 represents the equivalent of about \$425 billion expressed in 2002 dollars. However, despite these factors the increases are significant. The Pentagon's budget in 2007 would be a full \$100 billion greater than that envisioned by the Clinton administration for that year in its own long-term plan.

Table 1 Understanding the increases in 2003 Defence Budget Proposal

Department of Defence Funding only, billions of dollars

Enacted budget for 2002		331.2
Upward adjustment for inflation		6.7
'Must pay' bills		
Over-65 health care	8.1	
Civilian retirement/health care	3.3	
Military and civilian pay raises	2.7	
Subtotal		14.1
Realistic costing		
Realistic weapons costing	3.7	
Readiness funding	3.1	
Depot maintenance	0.6	
Subtotal		7.4
Cost of war (including \$10 billion contingency fund)		19.4
All other requirements (eg weapons acquisition)		9.8
Savings from transfers and program cuts, delays		(9.3)
Total 2003 budget request		379.3

Source: Department of Defence, 'FY 2003 Defence Budget', February 2002

Where will the money go?

Why does President Bush wish to increase defence spending to such levels? He does not plan to increase the size of the military, which remains one-third smaller than in Cold War times. Moreover, with the exception of missile defence, Bush administration officials have not yet added any major weapons systems to the modernisation plan they inherited from their predecessors; in fact, they have already suggested reducing acquisitions by eliminating the Crusader artillery program. The Bush administration claims that in general it is only fully funding the force structure and weapons procurement agenda that was laid out in Secretary of Defence William Cohen's 1997 Quadrennial Defence Review, as well as the immediate exigencies of the war on terrorism.

It is true that defence costs rise faster than the rate of inflation, and the war on terrorism has put an unexpected strain on the budget in the form of operating costs and the replenishment of weapons stores used in Afghanistan. It also the case that the Clinton administration reduced procurement of weapons systems while the military used the stockpile of new systems acquired largely during the Reagan buildup.

The Administration also wants to learn the lessons of Operation Enduring Freedom. That conflict demonstrated, more than any other before, the importance of unmanned aerial vehicles, real-time battlefield information networks, certain precision munitions, and good equipment for special operations forces. These and most other 'transformation' initiatives proposed by the Bush administration merit support. Because of these various factors, real defence spending should indeed continue to increase, as it has been doing since 1999. It makes perfect sense that today's military, though only two-thirds the size of the cold war force, might cost nearly as much.

An alternative to the Bush strategy and budget

The 1997 Quadrennial Defence Review, developed during a period of fiscal restraint, did not provide enough funds for its own proposed plan. However, Congress and the Clinton administration later added more than \$20 billion to the annual real dollar budget, and Secretary Rumsfeld added another \$20 billion for 2002, without counting added costs due to September 11th. So the yearly baseline had already grown by \$40 billion, even as the plan for forces and weapons remained mostly unchanged, without counting the additional spike in budget resources appropriated for 2003.

Secretary Rumsfeld and President Bush now tell us that this is still not enough. Alleging a decade of neglect, they claim that further spending increases are needed for military pay, readiness, infrastructure, health care, research and development and weapons procurement. However, the needs are not sufficient to require such large increases. Consider each broad category in turn.

Pay

After the largesse of the last few years, military pay has never been higher in real terms. Partly as a result, recruitment and retention have improved markedly. Most additional increases should be targeted at those few technical specialities where the Pentagon still has trouble attracting and keeping people, rather than the entire force.

In that regard, the Bush administration's plan to add a total of \$82 billion to military pay over the 2002-2007 period is excessive. A large portion of service personnel already make more money than they would if employed in the civilian sector. Since troops are receiving improved housing and health benefits at present as well, further routine pay raises should be held to no more than the rate of inflation. Over the 2004-2007 period, this approach would save about \$25

billion relative to the Bush administration's plan.

In addition, another \$5 billion could be saved through 2007 by modestly reducing the number of military personnel. This should not be done by cutting the number of major combat units below current levels, but rather by acknowledging the enhanced fighting efficiency of modern weapons systems and the need for lighter forces that the Administration outlines in its own QDR.

Operations and maintenance

This part of the budget funds a wide array of defence activities related to so-called military readiness, including training, equipment repair, fuel, and other necessities for overseas deployments, and most spare parts purchases. It also funds the salaries and health care of civilian employees of the Department of Defence. Even though readiness funding per troop is by far at its highest real dollar level ever, the Bush administration proposes adding \$146 billion to this budget over the 2002-2007 period.

About \$15 billion could be saved in the next few years by reforming military health care. Such reforms could build on ideas proposed by the Congressional Budget Office (CBO) – including merging the independent health institutions of each military service, employing market-based care wherever possible, and considering the introduction of a small contribution by military personnel. At a time when Congress has legislated a huge increase in the defence health budget by giving free lifetime care for military pensioners, reform is all the more important.

In addition, giving incentives to local base commanders to streamline their operations might help limit real cost growth to 2 per cent

rather than 2.5 to 3 per cent a year in other parts of the budget, saving \$10 billion more. These incentives could take the form of allowing base commanders to keep a certain fraction of expected savings from reforms they introduce for other uses at their bases.

Research and development

President Bush has rightly emphasised research and development ever since he began running for president, but again, the 2002 budget already added large sums to this area. Current real spending on research, development, testing, and evaluation already exceeds the levels of President Bush Senior's administration and roughly equals those of the peak Reagan years. Further real increases are not needed. For example, economies should be possible by canceling one or two major weapons and slowing at least one or two missile defence programs out of the eight now underway. Rather than add \$99 billion to the pre-existing plan, about \$55 billion should suffice for 2002-2007 (reflecting primarily the increases in the 2002 budget that would be sustained thereafter).

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Procurement

The Clinton administration spent an average of about \$50 billion a year to buy equipment; the figure is now about \$60 billion. According to the CBO, however, the expensive modernisation plans of the military services might imply an annual funding requirement of \$90 billion or more. Accordingly, the Bush/Rumsfeld budget envisions procurement funding of \$99 billion in 2007.

A great deal of the procurement dollars committed over the next five years will go to expensive next-generation fighter aircraft and naval ships. While modernisation is important,

two mitigating factors should make it possible to reduce the administration's procurement budget from nearly \$100 billion to \$75 billion. First, the lack of a peer competitor with an advanced air force or navy means current US forces remain the best in the world by a large margin. Second, Operation Enduring Freedom has underscored the potential of relatively low-cost systems, such as Global Positioning System (GPS) guidance kits added to 'dumb bombs', Unmanned Aerial Vehicles (UAVs) which cost a fraction of manned fighter planes, and real-time communications networks among sensors and weapons platforms. Such capabilities, added to a force built around existing weapons platforms, can make those platforms much better at a relatively modest cost.

The emergence of a potential powerful competitor, such as China, is a realistic concern that should not be ignored by the Administration. Accordingly, many of the advanced systems should be developed and procured, but they need not be purchased to replace existing systems on a one-for-one basis. Reducing Joint Strike Fighter procurement from 3,000 to 1,000 would provide a large force of next-generation aircraft to be directed against any powerful threat. For a fraction of the cost of the remaining 2,000 JSFs, the Defence Department could purchase an upgraded version of today's highly effective fighters or further develop inexpensive alternatives to modern fighter aircraft. The F-16 Block 60 could replace aging aircraft and provide enhanced capabilities through advanced communications and sensor upgrades, for example, while the services could also further develop the use of UAVs as weapons platforms.

Modernisation is important, but the services need to prioritise. They should recog-

nise, as former Vice Chairman of the Joint Chiefs of Staff Bill Owens has argued, that the electronics and computer revolutions promise major advances in military capability without inordinate expenditures of money.

A missed opportunity

It is ironic that the events of September 11th have caused such a radical change in the Administration's position on defence spending when the budget increases that largely account for that change are going to programs that have little or no relevance to the war on terrorism. It is natural to raise spending in times of war, but Congress and the President cannot abandon fiscal responsibility and sound military planning.

Defence budgets may decline in the years ahead, especially as September 11th recedes. If that happens, the Bush administration may then regret that it sacrificed its opportunity to promote the kind of defence reform it championed on the campaign trail and during its first few months in office. The country could be left with a defence program that is too large and expensive for the resources at hand. That could lead to cuts that will be even more difficult to make in the future. It could also lead to whittling away at needed programs rather than a clear process of prioritising various defence requirements and eliminating those that are less important.

President Bush, Vice President Cheney, and Secretary Rumsfeld all have considerable experience in the private sector. Yet they seem to be ignoring an important principle of corporate management – institutions need incentives to become more efficient. Give an organisation all it wants and it will fail to prioritise; impose some financial discipline and it will innovate and reform ●