

The federal budget

Phoney war

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The real battle, over health care, is just beginning

THE first hundred days were busy, Barack Obama noted, but the pace would be just as hectic in the second hundred: they would be spent building “a library dedicated to my first hundred days”. The president delivered the joke at the White House press corps’ annual shindig, but it makes an apt metaphor for the past week. He and his officials have released a blizzard of tax and health-care proposals that largely repackage, or add detail to, the ambitious draft budget he released in February.

That draft sought to extend health insurance to the millions of Americans who lack it, cut taxes for the majority of workers and spend more on education and energy research. To pay for it, Mr Obama would raise taxes on the rich and on corporations, cut wasteful programmes and auction off permits to emit carbon dioxide.

That agenda has since hit several road blocks. The president’s budget proposed limiting the deductions wealthy taxpayers can take for, among other things, charitable contributions. After an uproar from charities, Congress signalled it would not go along. Mr Obama called for cutting agricultural subsidies for richer farmers. Farm-state legislators rejected that, too. Mr Obama would like to raise \$210 billion from companies with foreign operations, by such means as limiting the deferral of tax on income earned overseas. Senior senators in both parties fret that this would drive American firms overseas.

Mr Obama has taken flak for talking about sacrifice but not asking for any. On May 7th he responded by listing \$17 billion in cuts to programmes deemed inefficient or wasteful, from the F-22 fighter jet to jailing immigrant criminals. True, it was a pittance next to a budget deficit already soaring towards \$2 trillion and 12% of GDP, a post-war record. But Mr Obama’s budget director, Peter Orszag, argued that wasteful spending encourages broader fiscal laxity just as broken windows encourage criminality. “We can no longer afford broken-window budgeting,” he said. Many in Congress, however, seem happy to leave the windows broken, and rushed to defend the threatened programmes.

Most problematic of all, prospects for a cap-and-trade bill this year have deteriorated. Mr Obama wants to auction off, rather than give away, permits to emit carbon dioxide. But a bill that could allow that, sponsored by Henry Waxman and Ed Markey, senior Democrats on the House Energy and Commerce Committee, is solidly

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Old and costly

opposed by Republicans and by many Democrats in coal- and oil-producing states. This suggests that the bill has little chance of becoming law this year, robbing Mr Obama of funds he planned to use to make his workers' tax cut permanent.

These setbacks should not be read as defeat, however. In the coming months, Congress and the administration are likely to hammer out compromises on many disputed items. Democrats in Congress will be under pressure to deliver at least \$17 billion of discretionary spending cuts, even if they are not the ones Mr Obama requested, because they have passed a budget resolution requiring even larger cuts.

Moreover, the real test for Mr Obama is health care, and there momentum appears to be on his side. This week health-care-industry officials promised, at his urging, to cut cost-inflation by 1.5 percentage points a year, or \$2 trillion over ten years. The promise was largely meaningless: if \$2 trillion in savings was lying around, a profit-maximising industry would have found them. And it remains dead-set against Mr Obama's wish for a public insurance plan that competes with private ones. But the event had symbolic importance. Jim Horney, of the liberal Centre on Budget and Policy Priorities, says it shows the industry will not try to kill this health reform as it killed Bill Clinton's attempt in 1994.

If Mr Obama's health-care ambitions fail, cost will probably be the reason. Mr Obama insists that his reform should be paid for rather than add to the budget deficit, so his budget earmarks \$634 billion in cuts to existing health programmes and various tax increases. But that is unlikely to be enough to pay for a plan that would cover most uninsured Americans.

Passing the tax increases necessary to pay for expanded health care will be hard if the economy remains weak, and the more so because that will also mean a bigger deficit. Mr Orszag has already raised his budget-deficit estimates by \$200 billion over the next three years, largely because the economy is generating less tax revenue per dollar of output than previously thought. The deficits would be even bigger if he used a more pessimistic, and therefore realistic, economic forecast.

Meanwhile, the threat to America's long-term fiscal health is growing. On May 12th the administration released updated figures on the health of the Social Security and Medicare programmes for the retired. The recession has slashed payroll-tax revenue, which means that the future, unfunded cost of the programmes has increased. It now exceeds \$104 trillion, or 8% of future GDP, compared with 7.6% last year. People are also living longer, which adds to the costs. Mr Orszag, never slow to press a point, wrote on his blog that this "should reinforce all our efforts to get health reform done this year."