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A REVIEW OF THE CARTER BUDGET (FY 1980)

INTRODUCTION

President Carter describes his FY 1980 budget as "lean and austere." A third characteristic might be optimistic. Several of the cuts proposed by the President will require not only congressional agreement but also changes in existing substantive legislation, a more difficult task. Many of these economy measures have been offered and rejected during past congresses. In addition the administration's economic forecast, when compared with other prognostications, appears distinctly roseate.

The president proposes a FY 1980 deficit of \$29 billion. Revenues will be \$502.6 billion and budget authority \$615.5 billion. Budget outlays will total \$531.6 billion, an increase of \$38.2 billion over 1979. Off-budget agencies will spend an additional 12 billion dollars.

Increases in social security payments, due to increased benefits and a greater number of beneficiaries, compose over one-third of the growth in spending. (Table 1) Defense spending rises by \$11.3 billion. Medicare/Medicaid, veterans benefits, and interest on the national debt are additional major elements in the outlay expansion.

PRINCIPAL ELEMENTS OF SPENDING GROWTH

TABLE 1

A) <u>Social Security</u> (benefit increases due to inflation adjustment plus increase in number of beneficiaries)	\$12.9 billion
B) <u>Defense</u>	\$11.3
C) <u>Medicare/Medicaid</u> (higher medical care costs plus growing number of beneficiaries, especially Medicare)	\$ 4.1
D) <u>Veterans Benefits</u>	\$ 0.2
E) <u>Interest</u>	\$ 4.2

Source: Minority Staff, House Budget Committee.

The current services budget, an estimate of the cost of merely continuing existing programs, including those indexed to inflation, serves as a standard by which to measure the president's budget.

TABLE 2

	<u>President's Budget</u>	<u>Current Services Budget</u>
Revenue	502.6	504.5
Budget Authority	615.5	618.2
Outlays	531.6	544.1
Deficit	29.0	31.6

Source: The Budget of the U.S. Government, 1980.

The administration has offered additions of \$7 billion to the current services outlays estimate. The increases are spread among defense, veterans compensation, medicare/medicaid, the proposed National Development Bank, and several other smaller programs.

Cuts of more than \$11 billion enable the administration to lower outlays below the current services estimate and produce a lesser deficit. Table 3 illustrates the sources of the discretionary \$7.7 billion cuts. Three billion is due to the 5.5 percent limit on federal pay raises and the freeze on employment. The administration also expects to save 600 million dollars through the elimination of 158,000 public service jobs. The \$700 million reduction in agriculture price supports is highly dependent upon the

weather, exports, and the market, all factors not easily divined. Historically, the presidents' budgets have been overly optimistic concerning farm price supports. Further cuts are achieved through curtailment of the national petroleum reserve program and a reliance on more rigorous government purchasing policies.

DECREASES NOT REQUIRING SUBSTANTIVE LEGISLATION

TABLE 3

<u>Program</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>
Energy Supply.....	*	-.3	-.5	-.5
Agricultural price supports....	.3	-.7	....	....
National forests.....	.1	-.3	-.3	-.2
Rail transportation.....	.3	-.5	.2	-.3
Impact aid.....	....	-.2	-.3	-.3
Higher education.....	....	-.4	-.3	-.1
Public service employment.....	....	-.6	-1.5	-.4
Pay restraint, Defense.....	....	-1.8	-2.8	-3.7
Pay restraint, Civilian agencies	....	-1.2	-1.8	-2.4
Other.....	-*	-1.6	-.7	-.5
Total.....	.5	-7.7	-8.1	-8.2

*\$50 million or less

Source: The Budget of the U.S. Government, 1980.

Unlike the discretionary cuts, the remaining 3.8 billion in cuts (Table 4) must be accompanied by substantive legislation. The impressive reductions in medicare and medical expenses are based on assumptions concerning both the passage and effectiveness of Hospital Cost Containment legislation. Last year's effort at such a bill failed. Further cuts in the health field are dependent on congressional approval of legislation requiring employees to provide the primary health insurance for employees over sixty-five. The 300 million dollar reduction in veterans medical care is based upon another proposal permitting the Veterans Administration to collect from private insurers charges incurred by veterans treated at VA hospitals.

Carter also seeks legislation which would reduce school lunch subsidies by \$400 million. Federal payments to school districts encompassing federal facilities, known as impact aid, will be slashed by \$200.00 million. Congress has resisted such attempts in the past.

PROPOSED DECREASES REQUIRING SUBSTANTIVE LEGISLATION

TABLE 4

<u>Program</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>
Hospital Cost Containment:				
Medicare.....	-.4	-1.5	-2.8	-4.3
Medicaid.....	-.1	-.2	-.4	-.6
Other health financing cost-savings.....	...	-.4	-.5	-.5
Veterans medical care.....	...	-.3	-.3	-.3
School lunch and related.....	...	-.4	-.4	-.4
Social security and railroad retirement.....	*	-.7	-1.8	-3.1
Public assistance.....	*	-.2	-.2	-.3
Other.....	...	-.1	-.2	-.2
Total.....	<u>-.4</u>	<u>-3.8</u>	<u>-6.6</u>	<u>-9.7</u>

*\$50 million or less

Source: The Budget of the U.S. Government, 1980.

Changes in social security, such as eliminating minimum benefits, the lump sum payments, and post-secondary school student benefits will, according to the administration, save the government over one-half billion dollars in 1980. However, two days after the budget was presented, the Washington Post (January 24, 1979) reported that Al Ullman, chairman of the House Ways and Means Committee, refused to consider the social security cutbacks. Assuming that Ways and Means does not consider the social security reforms (there have been conflicting reports) the budget deficit as of January 24, has already risen to 29.6 billion.

Ullman's refusal illustrates the tenuousness of the Carter spending cuts. The reductions, and thus the size of the deficit are dependent on several highly unpredictable factors, most notable of which is congressional cooperation. It is possible that the austerity of the proposed budget might be destroyed simply through Congress' failure to accept Carter's legislative proposals.

Another factor which might quickly bloat the deficit is the economy. The economy and the budget are interdependent. Changes in the size and financing of the public sector affect aggregate demand, inflation, and the credit markets. The FY 1980 budget is itself a tool designed to reduce the rate of inflation.

The president's budget, submitted nine months prior to the start of the fiscal year can be significantly altered by unanticipated, or incorrectly anticipated, changes in the economy. A

recession, for instance, would shrink expected revenues and swell anticipated outlays, such as unemployment insurance. The result would be a larger deficit.

The economic assumptions within the 1980 budget are favorable to the achievement of the \$30 billion deficit goal. As Table 5 illustrates, the administration projects 2.2 percent increases in real GNP for 1979. Chase Econometrics, Data Resources (DRI) and the Congressional Budget Office are predicting a recession. Higher real growth, and lower unemployment means greater government revenues and fewer outlays.

COMPARISON OF ECONOMIC ASSUMPTIONS

TABLE 5

	<u>1978</u>	<u>4th/4th*</u> <u>1979</u>	<u>1980</u>
<u>%Change in Real GNP</u>			
<u>President's Budget</u>	4.0	2.2	3.2
DRI (Dec. 27)	3.8	-0.5	6.5
Chase (Nov. 22)	3.7	-0.2	3.2
Wharton (Dec. 28)	3.9	1.4	na
CBO (Jan. 2)	4.0	1.1	3.9
<u>%Change in Nominal GNP</u>			
<u>President's Budget</u>	12.7	9.8	9.8
DRI	12.3	6.9	14.1
Chase	12.6	6.8	9.8
Wharton	12.6	8.4	na
CBO	12.5	9.3	6.7
<u>Unemployment (4th quarter average)</u>			
<u>President's Budget</u>	5.8	6.2	6.2
DRI	5.8	7.1	6.8
Chase	6.0	7.5	7.7
Wharton	5.8	6.1	na
CBO	5.8	6.7	6.7
<u>Inflation (CPI)</u>			
<u>President's Budget</u>	9.2	7.4	6.3
DRI	9.1	7.8	6.9
Chase	9.1	7.5	6.1
Wharton	8.9	8.3	na
CBO	8.8	8.2	7.6

*The 4th/4th rate indicates the rate of growth from the last quarter of one year to the last quarter of the following year.

Source: House Budget Committee

The president's forecast of the unemployment rate for both 1979 and 1980 is substantially lower than DRI's, Chase's, and the Congressional Budget Office. Only Wharton, at 6.1 percent, is in the same range. It is estimated that for each annual increase of 0.1 percent in the unemployment rate outlays will increase by \$350 to \$450 million. Thus, if the Chase prediction of an unemployment rate of 7.7 is correct, total 1980 outlays will rise another \$5.0 to 6.75 billion.

Should the unemployment rate exceed the projected 6.2 percent the administration will, according to Labor Secretary Ray Marshall, use triggering mechanisms to increase public jobs.¹ Such a program would require a supplemental budget request.

Again, the president is among the most optimistic in his view of inflation. Wharton and the CBO both foresee rates of over 8 percent in 1979, compared to the administration's 7.4. The administration also predicts a further moderation in 1980, when the inflation rate will be 6.3 percent.

Over thirty percent of the total 1980 outlays are tied to a cost of living index. Should the actual inflation rate exceed the expected total outlays, then the budget deficit will rise substantially.

The cost of the real wage insurance program is budgeted at \$2.5 billion. This will be composed of \$2.3 billion in reduced tax receipts and outlays of \$0.2 billion to workers whose rebates exceed their tax liabilities. It is estimated that for each one percent of inflation above the anticipated 7.5, the program will cost an additional \$5 billion dollars.

The interest on the national debt in 1980 will be \$11.1 billion. In deriving this figure Carter broke with tradition and chose, as the interest rate not the current Treasury bill rate, but instead, an assumption of the future level of that rate. Since the interest rate is affected by the rate of inflation, a higher than anticipated rate of inflation will produce higher than anticipated interest costs.

The deficit of \$29 billion is not a sum etched in marble. It is a tentative calculation, based upon extremely optimistic assumptions. The administration has given itself the benefit of every doubt in deriving the budget totals. The possibility that the budget deficit will be much larger than \$29 billion, is a strong one. The Congressional Budget Office, for instance, has predicted a deficit of \$41 billion.

1. Washington Star, January 22, 1979, p. A-11.

HIGHLIGHTS OF THE BUDGET

REVENUE

The Administration has no plans for a tax cut in 1980. In fact, it is implementing cash management policies, such as requiring state and local governments to deposit social security taxes at an accelerated rate, designed to increase total revenues. Carter has also proposed an oil pollution liability and compensation fee and an increase in the railroad retirement tax. The former is to finance cleanup of oil spills and the latter is deemed necessary to the solvency of the retirement fund.

DEFENSE

Carter's budget, in accordance with his pledge to NATO, increases real defense spending by 3.1 percent. Procurement funds, increased by 7.8 percent in real terms, are to finance among other items, a Trident submarine, a conventionally powered aircraft carrier, improvements in the Minuteman missile, and an air launched cruise missile. Funds for research, development, test and evaluation were increased 4.2 percent in real terms.

Despite the seemingly impressive gains, the Carter defense budget barely exceeds the current services estimate. Much of the increase in procurement and research has been financed through a lid on military personnel costs. Outlays for personnel rise by less than 1 percent in 1980, 1981, and 1982.

Although 1980 outlays increased by 9.9 percent, budget authority rose only 8.1 percent. The growth in outlays substantially exceed authority again in 1981 and 1982. The effect of this squeeze in authority might be a handicap in developing long term defense projects.

ENERGY

The 1980 budget contains \$15 billion in new borrowing authority for the Tennessee Valley Authority. Solar energy outlays, increasing by nearly \$180 million, will produce a 40 percent increase in research and a 22 percent increase in application funds.

Nuclear energy outlays were cut \$125 million below the 1979 level. The reductions were accomplished through the cancellation of the Clinch River breeder reactor and the decision not to reprocess spent fuel from commercial nuclear power plants.

COMMUNITY AND REGIONAL DEVELOPMENT

The primary interest in this function is Carter's proposed National Development Bank. The bank with budget authority of \$3.5 billion, would offer grants, guaranteed loans, and other financial assistance to businesses located in economically depressed areas. The budget would also increase, by \$150 million, HUD's community block grant. Also contained within the budget are \$150 million in authority and \$76 million in outlays for the proposed Inland Energy Assistance program. The purpose is to "provide funds for non-costal states, communities, and Indian tribes to develop and carry out plans for mitigating the adverse effects of rapid population growth due to the development of energy resources."

EDUCATION TRAINING EMPLOYMENT AND SOCIAL SERVICES

The FY 1980 budget includes \$400 million in authority, along with a supplemental request of \$258 billion in FY 1979, for special grants to school districts with a high concentration of needy students. Education of the handicapped receives an appropriations authority increment of \$58 billion. Budget authority for an additional 20,000 guaranteed student loans is also provided.

The administration plans a decline in outlays for public service jobs of one half billion dollars. The 1980 outlays of 4.9 billion will provide jobs for 467,000 down from the current 625,000. It is anticipated that the private sector, spurred by the \$600 million Target Employment Tax Credit program, will take up the slack.

The summer youth employment program will lose funding for 250,000 jobs. The minimum eligibility requirement will now be fifteen, rather than fourteen.

HEALTH

In addition to the legislative savings of the Hospital Cost Containment proposal, the Carter health budget calls for Medicaid coverage for an additional 2 million children, under the auspices of the Children's Health Assessment Program (CHAP). Medicaid eligibility will also be extended to 100,000 low income pregnant women.

The mental health and anti-smoking programs, under the patronage of Rosalyn Carter and Joseph Califano, respectively, receive a boost in budget authority.

INCOME SECURITY

The administration has proposed legislation which will eliminate several social security expenditures. Other social security and welfare programs are, by law, indexed to the rate of inflation.

Carter has budgeted outlays of 6.7 billion, the same as the 1979 sum, for the aid to Families with Dependent Children Program. Improvements in cash management and a crackdown in abuses are expected to achieve the necessary economies.

GENERAL PURPOSE FISCAL ASSISTANCE

The administration proposes to establish a targeted fiscal assistance program designed to replace the expired Anti-recession Fiscal Assistance Program (ARFA). The targeted assistance would be applied specifically to cities which became highly dependent upon ARFA. Supplemental authorizations and outlays of 250 million are requested for 1979. Outlays of 150 million are projected for 1980. Carter also plans to offer an additional \$250 million in New York City loan guarantees.

LONG TERM OUTLOOK

The Carter budget introduces, in the 1980 budget, a three year perspective. Thus the budget is a plan for not only 1980, but also 1981 and 1982.

According to this longer term outlook the budget will produce a surplus of \$37.8 billion in 1982. A balanced budget will be missed by a scant 1.2 billion in 1981. Carter points out that as a percentage of GNP, government spending will decline from 21.2 to 20.3 percent.

There are two caveats to this encouraging prediction. One is that the 1982 projections are based on the same optimistic economic and legislative assumptions as the short term budget.

Secondly, there are no tax cuts planned. The anticipated growth in revenues is reliant upon increased social security taxes, inflation-inspired rises in personal income, and remunerative cash management policies. The ratio of receipts to GNP, in contrast with the spending, rises from 20.1 percent in 1980 to 21.6 percent in 1982.

The president's budget now goes to the Senate and House Budget committees where it will serve as the starting point for their deliberations. Congress will present its own budget on May 15. Since actual appropriations will be based on the congressional budget, the May 15th document will better reveal the economic role chosen by the government.

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