



BIPARTISAN POLICY CENTER

From Merely Stupid to Dangerous: **The Sequester's Effects on National and Economic Security**

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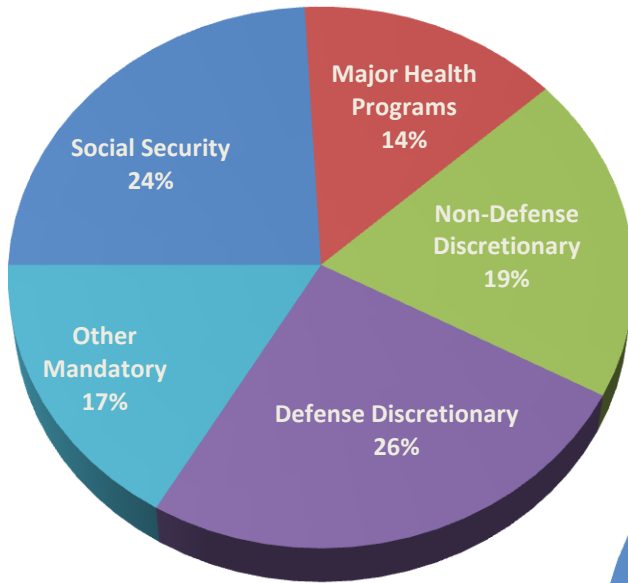
OCTOBER 2013

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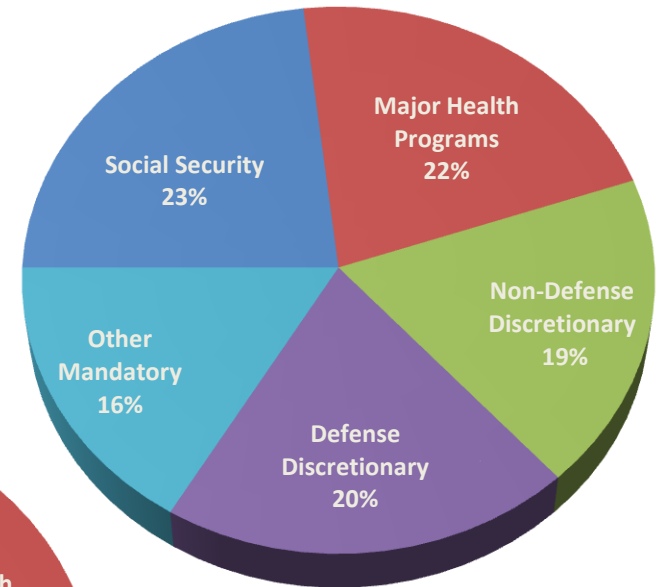
- **Because of the structure of defense spending, our national security forces and defense industry have been able to continue operating under sequestration, but not without permanent damage.**
- **The full brunt of the cuts hasn't hit yet, and if we go down the sequester path for too long, we won't be able to reverse the devastating impacts.**
- **It isn't primarily the size of either the federal budget or the defense budget that poses problems; it is the dramatic change in the composition of those budgets over the decade—entitlements are pushing out investments. And sequester worsens that trend.**
- **Essential government services, especially in defense, are not being performed, and will not be if sequester continues.**
- **The combination of sequester cuts and unaddressed cost increases will erode force readiness, stall modernization, and reduce the fighting forces by at least 50% by 2021.**
- **The impact of the defense sequester on spending, which drives the economic impact, will double in FY 14 and triple in FY 15, compared to FY 13.**

- Our country faces a debt problem: not just how much money we spend, but how we spend it.

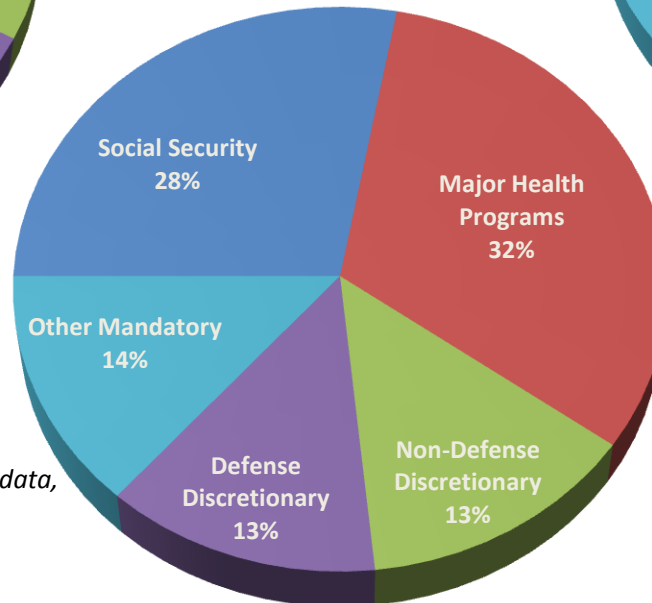
1992



2012

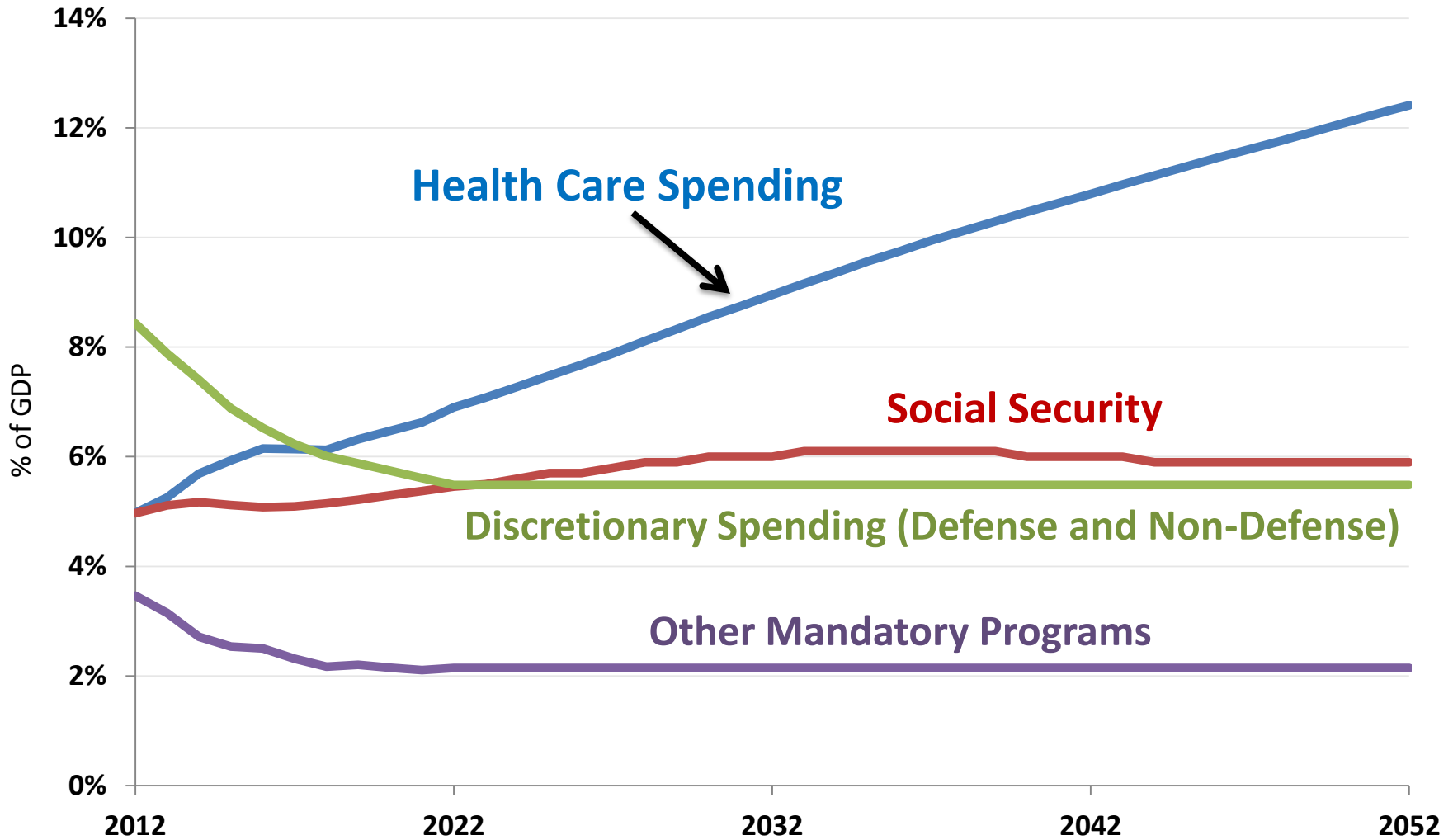


2022 (projected)



Sources: President's Fiscal Year 2014 Budget, Congressional Budget Office historical spending data, Bipartisan Policy Center calculations
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HEALTH CARE COSTS ARE THE PRIMARY DRIVER OF THE DEBT

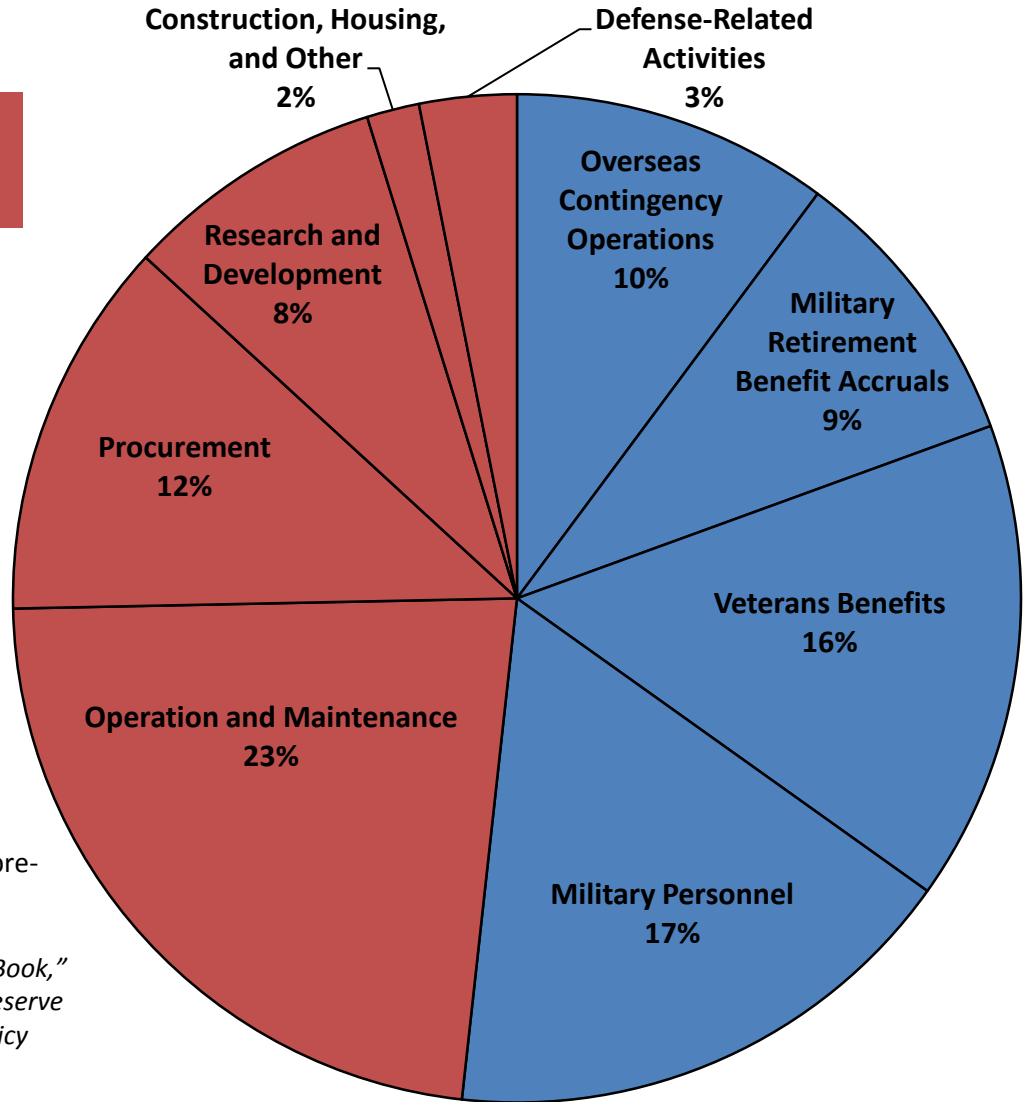


Sources: Congressional Budget Office's Alternative Fiscal Scenario (January 2012), additionally assuming that troops overseas decline to 45,000 by 2015; Bipartisan Policy Center extrapolations

- **Some think sequester is an effective deficit reduction tool.**
- **In reality, sequester:**
 - Barely reduces the U.S. debt
 - Exacerbates the budget's structural problems
 - Corrodes our national security
 - Hampers economic recovery
- **Our study shows the very real harm that is already being done by sequester...**
- **...and that the worst is yet to come.**

Areas subject to sequester cuts

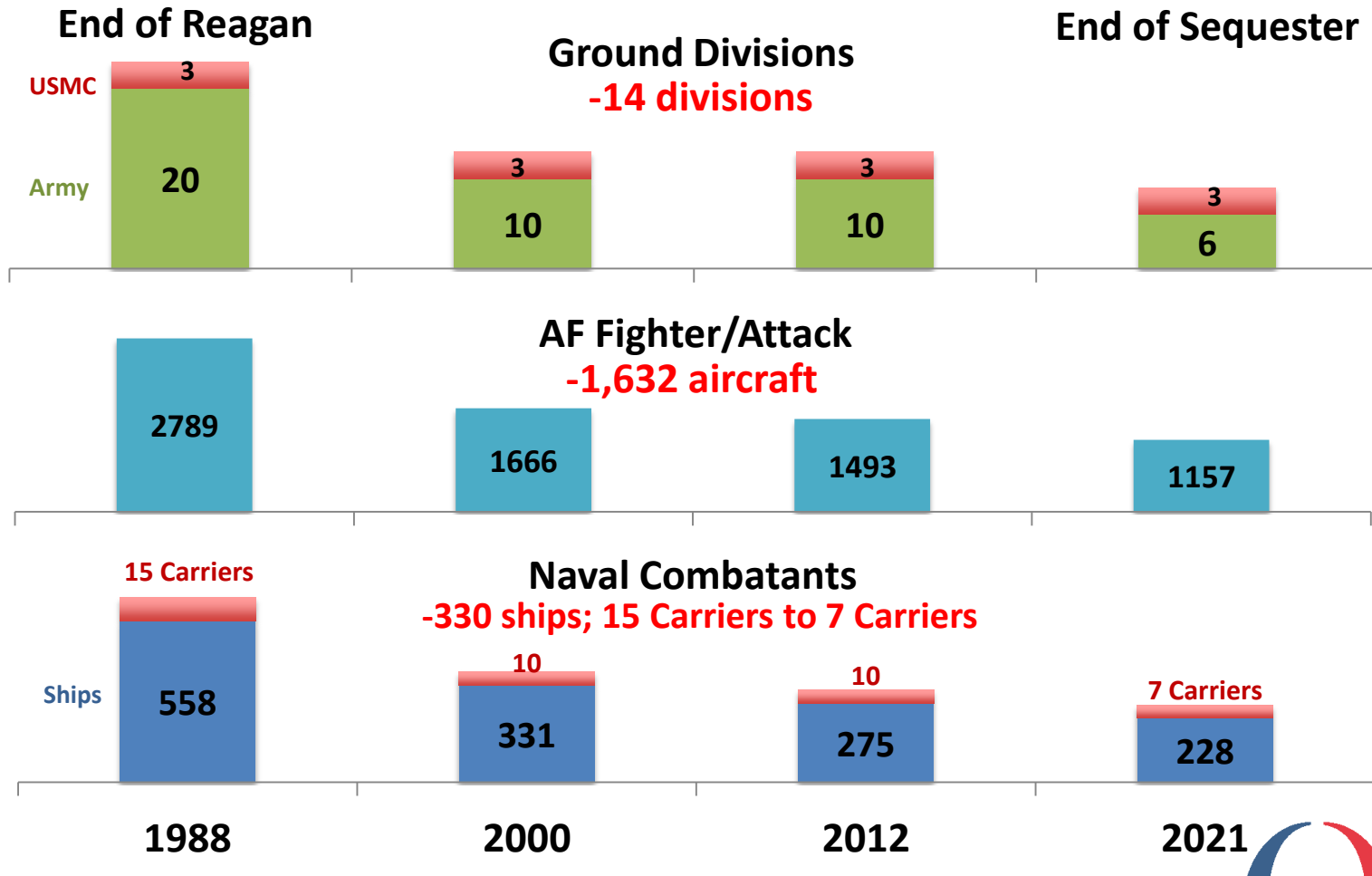
Areas exempt from sequester cuts



Note: Figures based on FY 2013 pre-sequester appropriations.

Sources: DoD Comptroller "Green Book," Congressional Research Service, Reserve Forces Policy Board, Bipartisan Policy Center calculations

- The combination of sequester cuts and unaddressed cost increases will erode force readiness, stall modernization, and reduce the fighting forces by at least 50% by 2021.



- **Lower GDP growth**
 - Reduced spending results in lower output
- **Lower employment**
 - Directly, through defense civilian furloughs (today) and reduced active force levels and reduced civilian workforce (in the future)
 - Indirectly, through lower private-sector employment (defense contractors, service businesses)
- **Erosion of the industrial base**
 - Fewer suppliers, especially negative impact on smaller contractors
- **Effects are only beginning to be felt**



What are the short- and long-term impacts of the sequester on
National Security?

- **Force readiness deteriorating**: Military is approaching post-Vietnam hollow force—most non-deploying units are not combat ready.
- **Modernization stalled**: Research and procurement of weapons systems critical for future missions has been significantly cut, leading to unit cost increases and schedule delays.
- **Decision process broken**: The proven method of linking vital interests, threats, military strategy, requirements, and resources has been broken by sequester's automatic cuts.
- **Structural problems exacerbated**: The combination of sequester and unaddressed structural problems in the defense budget—growing spending on personnel, massive overhead, and inefficient acquisition—will reduce the fighting forces by at least 50% by 2021.

Sequester is driving all key elements of force readiness downwards:



- the number of personnel in their units against the number required;

- the individual skill training of personnel in their military occupational specialty

- the unit training in its mission (both as individuals and as a maneuver unit);

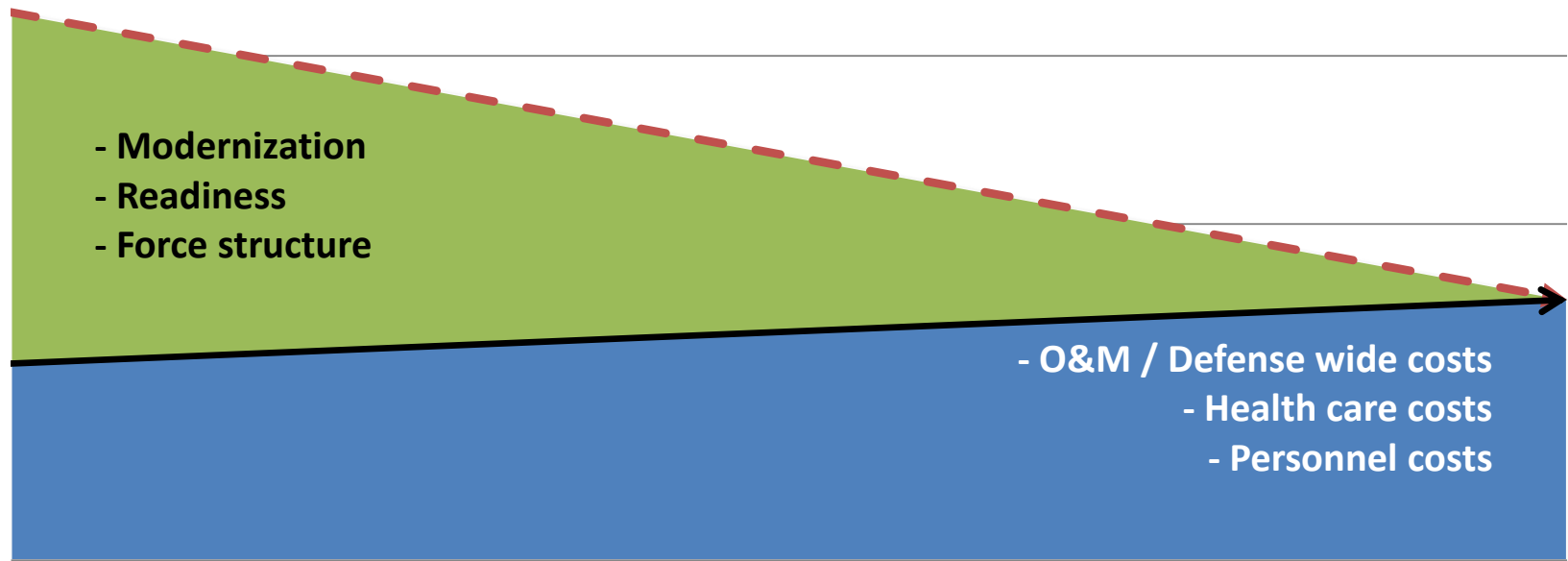
- the equipment the unit is required to have;

- and whether that equipment is operational.

SEQUESTER CUT TO PROCUREMENT OF TOP-TEN PROGRAMS (\$M)

Program	FY 2013 Enacted	FY 2013 Sequester	Prior Year Obligations	Prior FY Cut	Total Cuts
F-35s	\$5,240.0	-\$814.9	\$4,652.6	-\$0.7	-\$815.5
DDG-51	\$3,035.3	-\$502.7	\$2,855.1	\$0.0	-\$502.7
Virginia Class Submarine	\$3,213.4	-\$353.9	\$1,619.5	-\$138.4	-\$492.3
P-8 Poseidon Aircraft	\$2,382.1	-\$122.1	\$422.5	-\$112.0	-\$234.2
F/A-18E/F Hornet	\$2,578.2	\$0.0	\$325.3	-\$221.3	-\$221.3
Littoral Combat Ship	\$1,782.6	-\$43.6	\$671.9	-\$140.6	-\$184.2
CVN Refueling Overhauls	\$1,746.1	-\$93.3	\$282.0	-\$83.0	-\$176.3
UH-60 Blackhawk	\$1,304.4	-\$8.4	\$334.8	-\$120.0	-\$128.3
Trident II Modifications	\$1,198.3	-\$100.3	\$195.0	-\$11.8	-\$112.1
CH-47 Helicopter	\$1,184.5	-\$110.0	\$78.6	-\$1.8	-\$111.8
Totals	\$23,664.9	-\$2,149.2	\$11,437.3	-\$829.6	-\$2,978.8

- Almost every essential program is at risk, either through program reductions or termination.
- Prospective result: Unit cost increases, schedule delays, adverse effects on industrial base.



FY2012

FY2021

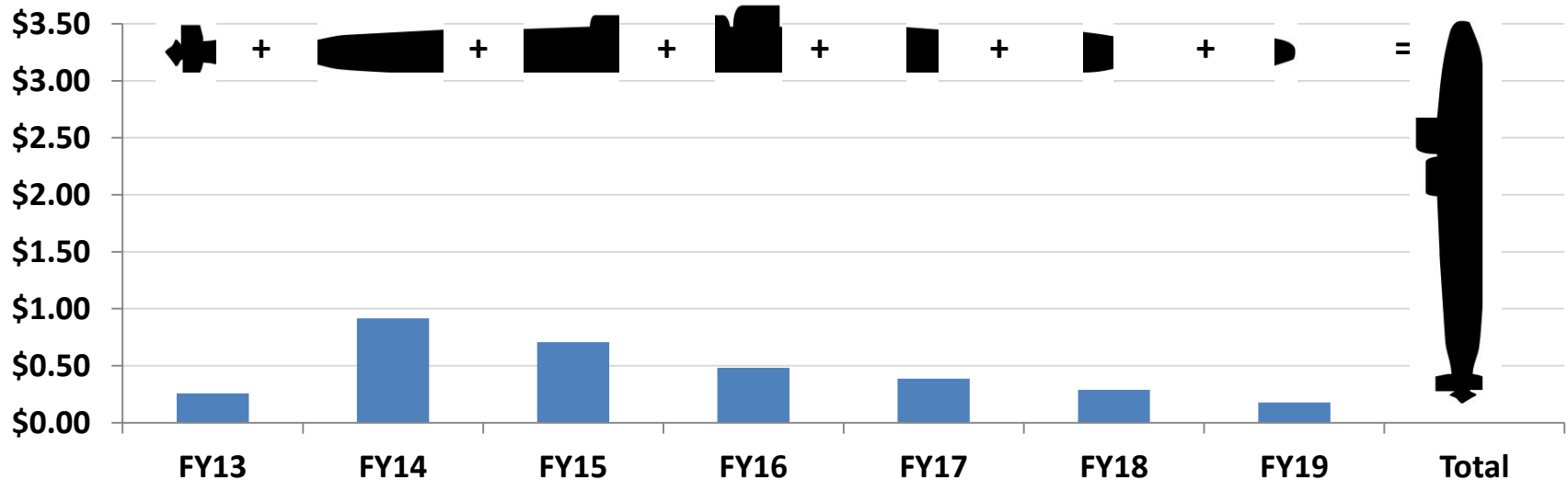
- **By 2021, the personnel, health care, and defense wide costs will consume 100% of the budget without reform to current cost trend**
- **O&M costs per active-duty:**
 - 1980 = \$55K
 - 2001 = \$105K
 - 2010 = \$211K
- **Fully-Burdened costs of active duty:**
 - FY2013 = \$384K



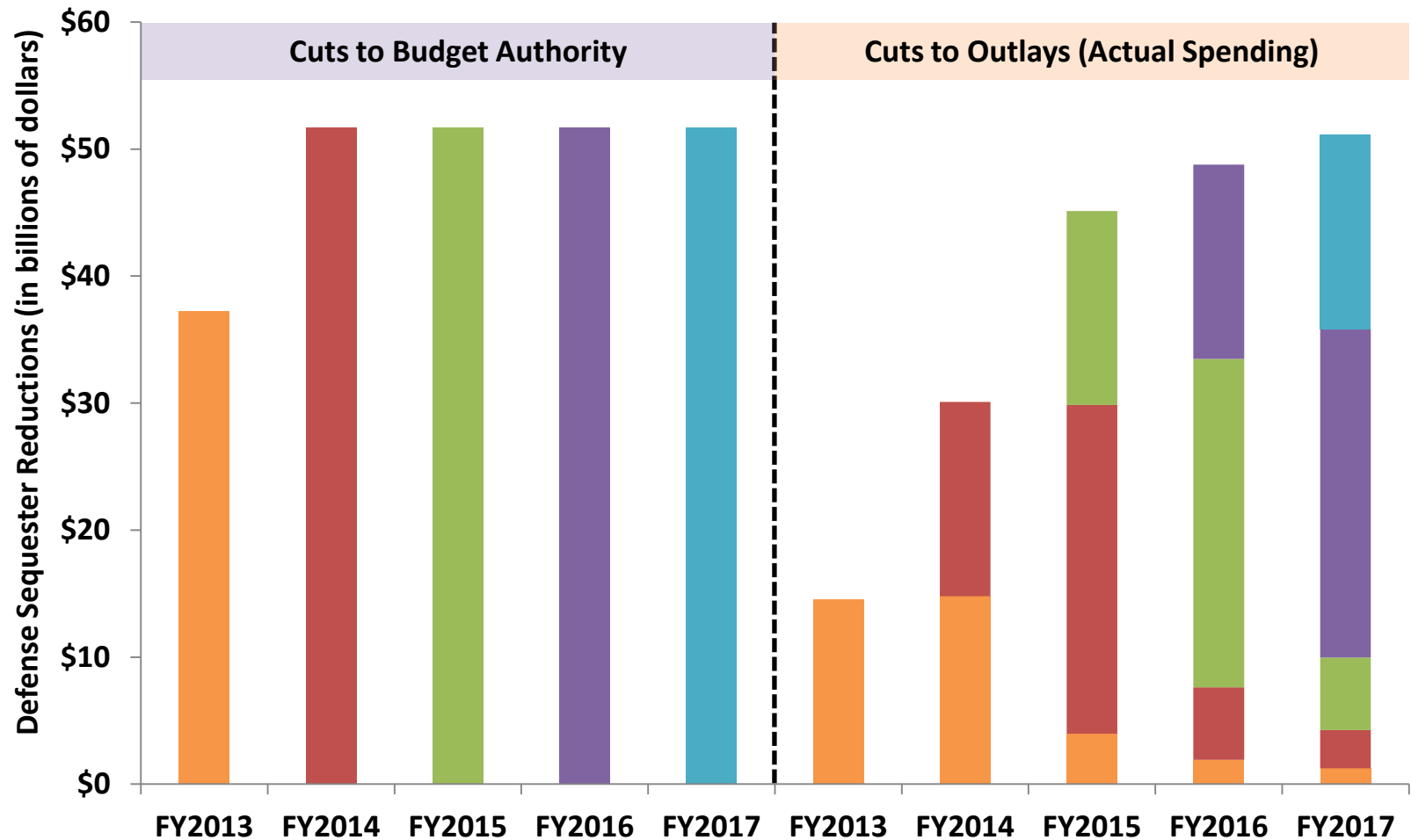
What is the impact of the sequester on **the Economy?**

- Each year, Congress appropriates money to the Department of Defense (DoD) with authorization to spend it according to a specified budget. This is known as *budget authority (BA)*, and is how the sequester cuts are measured.
- But DoD does not spend all this money in that same year. Actual spending is known as *outlays*.
- Weapons systems are effectively bought on installment.

In FY13, Congress gave DoD \$3.2 billion for new submarines.
That money will be spent over 7 years.



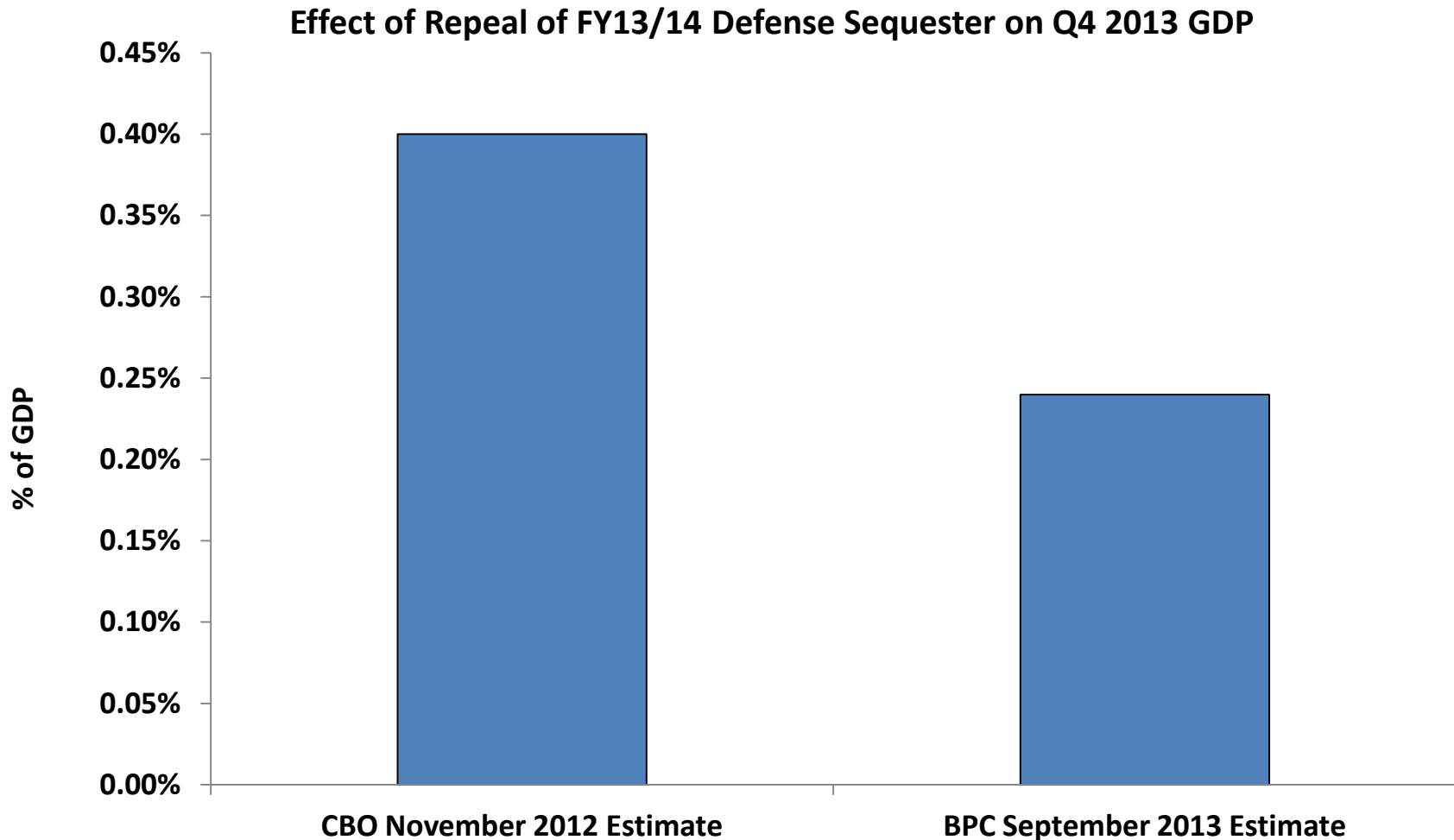
PROJECTED SPENDING REDUCTIONS FROM DEFENSE SEQUESTER THROUGH FY2017 16



Note: Analysis includes sequestration cuts to budget authority of FY13-17 appropriated accounts and unobligated balances, assuming cuts to unobligated balances have the same effect on outlays.

Sources: Department of Defense; Bipartisan Policy Center calculations

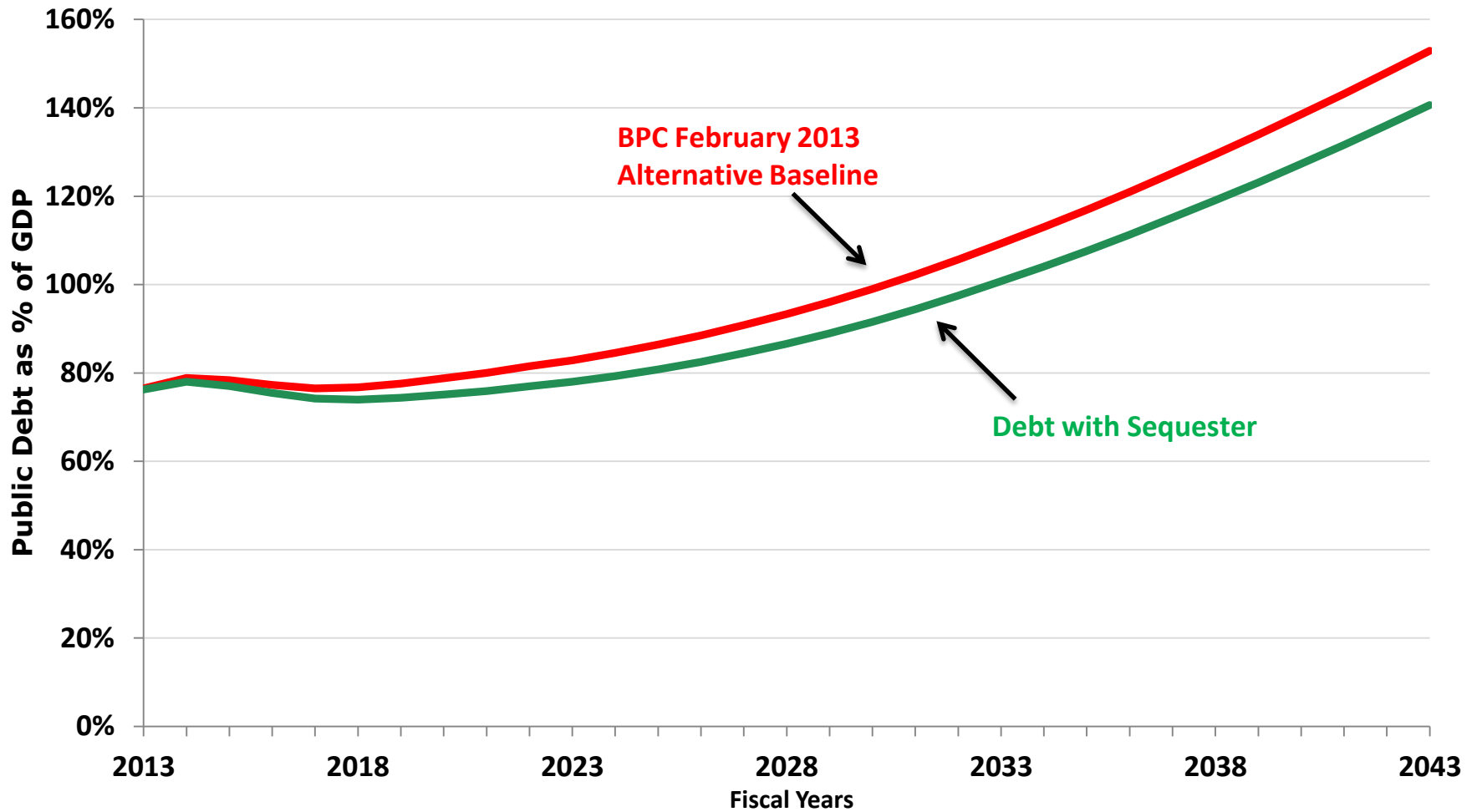
- **There are three possible reasons why there hasn't been an immediate and more severe impact on the defense industrial base:**
 1. The Budget Control Act's sequestration mechanism cut budget authority, not outlays
 - Appropriation categories that matter most to the defense industrial base typically see less than 50% of budget authority disbursed by Treasury as outlays in the first year of new budget authority
 2. Industry cut overhead early and is now buying back stock and increasing dividends
 3. Large defense firms have backlogs of work under prior contract awards that are supporting 2013 sales and earnings.
 - A sampling of larger defense contractors shows that they ended 2012 with a backlog that covered 43%-65% of expected sales



Note: Estimate is of the increase in fourth quarter 2013 GDP if the FY 2013 and FY 2014 defense sequesters had been repealed.

Sources: Congressional Budget Office; Bipartisan Policy Center calculations

- **People are right: The impact has not been as visible as expected, so far.**
 - Because the cuts in spending have been delayed
 - No great harm to the economy – yet
 - But the impact is still coming – it has not been cancelled, but merely delayed
- **When the cuts hit in FY 2014...**
 - People will see them
 - Businesses will feel them
 - More pain is coming and it will be more intense
- **All this despite minimal reduction in the long-term debt**



Note: The BPC Alternative Baseline assumes current law, except that: 1) funding for combat operations overseas winds down; 2) Medicare physician payments are frozen at 2013 levels (“doc fix”); 3) the sequester is waived; 4) expiring tax provisions are extended as they have been in the past; and 5) aid for Hurricane Sandy is not extrapolated for future years.

Sources: Congressional Budget Office (February 2013) and Bipartisan Policy Center extrapolations



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Acknowledgements



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