

Why Deficits Matter

And What We Should Expect from
our Presidential Candidates in 2008

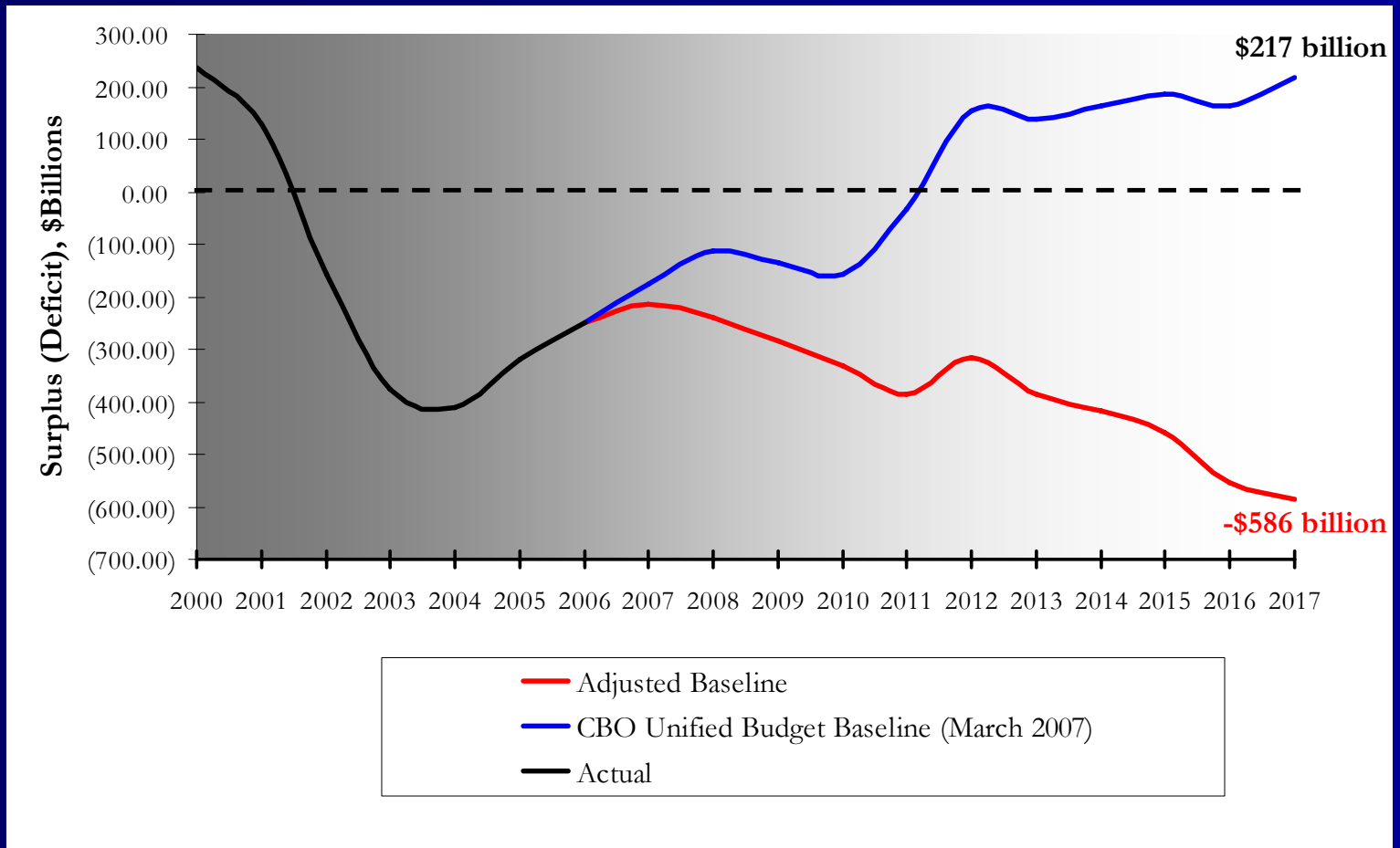
Isabel Sawhill, Senior Fellow, Brookings Institution

July 2007

The Problem

- Current Deficit (FY 2006): \$248 B
- Projected by 2017: \$586 B
- Over longer-run totally unsustainable because of rising costs of entitlements
- By 2030, three major programs absorb all revenues under current law
- Need to reform both revenues and entitlements

Budget Projections



Why Deficits Matter

- Dependence on foreign lenders
- Rapidly rising debt service costs
- Burden on future generations
- Weakened ability to meet contingencies or invest in future

What Candidates Should Do

- Commit to balance in 5 yrs; put nation on sustainable course thereafter
- Pledge to work in a bipartisan way
- Put all options on table
- Be honest about magnitude of challenge and types of changes that will be needed
- Propose reforms to process, while acknowledging that these alone not enough

Prerequisites for a Compromise

- Balance of spending cuts and revenue increases
- Spending cuts can come from holding the line on increased spending and from reforming entitlements, health care in particular
- Revenue increases can come from not extending all of the Bush tax cuts, from closing loopholes, or from new taxes (e.g., on energy consumption)

Social Security Reform

- Adjust age of retirement or index to longevity
- Encourage people to work longer
- Reduce future benefits for better-off while maintaining for less well-off
- Mandate *additional* savings for retirement in personal accounts
- Raise payroll tax cap

Health Reform

- Need for a longer-term vision, e.g.,
 - Basic package for all (evidence-based)
 - Subsidies related to income; access to community rates
 - Limits on spending via a national health care budget or a health care voucher
 - Fund via earmarked VAT so that decisions to spend more on health care linked to higher taxes
 - Health likely to absorb more of our rising incomes; we should have health care system we're willing to pay for.

Questions for the Candidates

- Are you in favor of extending the Bush tax cuts? If so, what spending would you cut to make room for them?
- How do you intend to pay for any new spending initiatives or tax cuts?
- What are your plans for reining in the long-term costs of Social Security and Medicare?
- If you want to preserve Social Security and Medicare, how will we pay for this?