THE WALL STREET JOURNAL.

Legacy of Deficits Will Constrain Bush's Successor

Soaring Costs Threaten to Impose A Harsh Reality

By MICHAEL M. PHILLIPS and JOHN D. MCKINNON
February 1, 2008; Page A3

WASHINGTON -- George W. Bush took office in 2001 with budget surpluses projected to stretch years into the future. But it's almost certain that when he returns to Texas next year, the president will leave behind a trail of deficits and debt that will sharply constrain his successor.

On Monday, the president will unveil a $3 trillion-plus budget request for his final year, which is likely to show a deficit of more than $400 billion. New details of the budget emerged yesterday, with officials saying the White House plans to keep a lid on nonsecurity discretionary spending. It wants to cut about $200 billion from the government's medical programs for seniors and the poor. (See related story.)

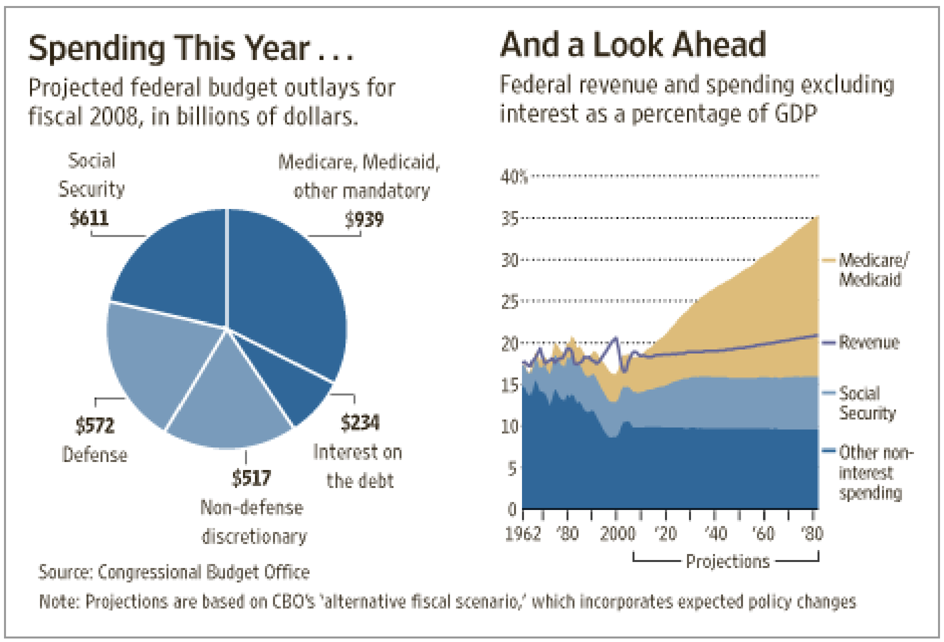
George W. Bush

The longer-term picture is darker. Despite his efforts, Mr. Bush failed to work out a deal with Congress to tackle the spiraling costs of government health and retirement programs. The next president, if he or she serves two terms, could find the U.S. government so deeply in hock that it would face losing its Triple-A credit rating, something that has never happened since Moody's Investors Service began grading U.S. securities in 1917.

As a result, the ambitions of Mr. Bush's successor to cut taxes, institute universal health care or aid troubled homeowners might have to give way to the reality of soaring costs for Social Security, the Medicare program for the elderly and the Medicaid program for the poor.

"We kicked this can down the road about as long as it can be," Senate Budget Committee Chairman Kent Conrad, a North Dakota Democrat, said at a hearing this week. "It will absolutely bedevil the next administration."

Republicans, in particular those to the right of the president on fiscal matters, are vocal in criticizing the increases in spending that Congress and President Bush have carried out over the last seven years. Sen. John McCain, the leading Republican presidential contender, told reporters recently that while history hasn't made a final judgment on President Bush, it will "judge him harshly on the spending point of view."



The president's critics say his failings are twofold: He has squandered surpluses that could have helped pay down the $5 trillion federal debt. And he has let two terms pass without persuading Congress to take action that would preserve the government's social programs. According to the Concord Coalition, a fiscal watchdog group, the shortfall in Social Security and Medicare through 2080 will total $72.3 trillion, a number that dwarfs the impact of Mr. Bush's spending and tax cuts.

TODAY'S MOST POPULAR

1. A Rebellion and an Awkward Embrace
2. Microsoft Makes Grab for Yahoo
3. Jimmy Carter's Lust and North Korea's Nukes
4. Commentary: Who Was Hillary Clinton?
5. Commentary: Romney's Convictions

MORE

PEOPLE WHO READ THIS...

Also read these stories:

- Bush's 2009 Budget Will Top $3 Trillion
- Infamous Trader Gets Hero Treatment
- Candidates Take Aim at Republicans
- Arizona Is Focus of Immigrant Debate
- Merrill Buys Back CDO Securities

Mr. Bush's defenders say he did the best he could in the wake of the Sept. 11 attacks, and that he has recently tightened up on spending. The budget deficit in fiscal 2004 measured 3.6% of gross domestic product; last year it narrowed to 1.2% of GDP, low by historical standards. The deficit is expected to rise to 2.5% of GDP, or about $350 billion, this fiscal year, assuming Congress passes an expected economic-stimulus package.

"You could say, 'Gee, he inherited surpluses and now we have a deficit,'" said Rob Portman, the former head of the White House budget office under Mr. Bush. "On the other hand, you could say he inherited a recession" in 2001. Mr. Portman called the country's fiscal health "relatively strong" and said the president has left a solid base for "the next president and the next Congress to deal with the real problem, which is the unsustainable growth in mandatory spending."

In his State of the Union address this week, Mr. Bush signaled he wasn't going to use his last year trying to revamp entitlement programs. Instead, he called on lawmakers to "offer your proposals and come up with a bipartisan solution."

When Mr. Bush took the oath of office in 2001, the nonpartisan Congressional Budget Office projected $5.6 trillion in federal budget surpluses through 2011. Through most of his tenure, the president managed to have his guns, butter and tax cuts without creating enormous budget deficits, at least as measured by their share of GDP. One reason was a surprise increase in federal tax receipts from corporations over the last couple of years. Now those revenues have flattened out and the economy is teetering on the edge of recession.

Mr. Bush and Congress, meanwhile, increased federal spending by 25% between 2001 and 2007, adjusted for inflation, according to Brian Riedl of the conservative Heritage Foundation. By Sept. 30, the U.S. will have spent almost $800 billion on the wars in Iraq and Afghanistan. A new Medicare prescription-drug benefit for seniors costs almost $80 billion a year. Mr. Bush's signature tax cuts, in 2001 and 2003, sapped tax receipts and sliced the projected budget surplus by about $1.7 trillion through 2011, according to the CBO.

Harvard economist N. Gregory Mankiw, a former Bush economic adviser says the seniors' drug program was "a step in the wrong direction from the standpoint of fiscal imbalance."

Phill Swagel, assistant secretary of the Treasury for economic policy, says the president has had a "pro-growth agenda" and "tried to take the right steps" on long-term fiscal problems, albeit with limited success.

Mr. Bush came into office in 2001 vowing to save Social Security from financial ruin. "My opponent completely ignores the long-term problems of Social Security," he said of Democratic nominee Al Gore during a New Mexico campaign stop in the waning days of the 2000 campaign. Eventually, the retirement bills for baby boomers would come due, he warned. "And our children and grandchildren will pay them with massive new taxes."

In 2005, Mr. Bush tried to tackle Social Security, on the theory that it should be easier to fix than Medicare. The latter is more expensive, and salvaging it would require the government to find a way to stem rising medical costs.

Mr. Bush approached the subject from a free-market point of view, calling on Congress to divert some of the Social Security payroll tax into individual investment accounts. Many Democrats and seniors saw it as an attempt to kill the program rather than fix it.

"The president put a proposal on the table, and I think he gets credit for that," says Alice Rivlin, President Clinton's budget director and a former vice chairman of the Federal Reserve. "But he wasn't willing to negotiate with the Congress to make it a serious proposal that both sides could accept. And Congress wasn't ready to negotiate."

Last year, Mr. Bush asked Congress to slow the rate of growth of Medicare spending, aiming to cut $8 trillion from the program's $34 trillion unfunded obligations over the next 75 years. But the president couldn't win congressional support.

Doomsayers have been warning for years of an approaching tsunami of health and retirement costs. What has changed is that the next president will actually have to confront the doom.

This year, the first of 78 million Baby Boomers hit retirement age and become eligible for early benefits, at a pace of 7,776 a day. Barring radical changes, in the final year of the next president's first term, 47.8% of the federal budget will cover the costs of Medicare, Medicaid, the Social Security retirement program and a smaller children's health insurance program, according to projections by the Office of Management and Budget. Today those programs consume 41.5% of the budget.

Ratings agency Moody's has warned that it could eventually downgrade its rating of U.S. debt unless there's a sharp change of course with Medicare, Medicaid and Social Security. The government's triple-A rating allows it to borrow cheaply and sets the benchmark for global financial markets.

In 1999, Moody's started a series of five downgrades of Japanese government debt after the debt reached 90% of the entire economy. "That could happen in the United States if these programs aren't reformed" as 2020 nears, says Moody's Vice President Steven Hess.

Austan Goolsbee, a University of Chicago economist and adviser to Sen. Barack Obama, says that Mr. Bush has left his successor with little wiggle room. Sen. Obama has called for allowing some of the Bush tax cuts to expire as scheduled in 2010. Mr. Obama has also said he would like to remove the salary cap on the payroll taxes that fund Social Security.

Sen. Hillary Clinton, the other contender for the Democratic presidential nomination, identifies spending cuts or tax increases that she says would pay for almost every campaign initiative. For instance, she says she'd pay for a $10 billion-a-year universal preschool education plan by cutting the ranks of federal contractors by 500,000 and cracking down on no-bid government contracts. Mr. Bush "has rightly earned the legacy of being our nation's most fiscally irresponsible president," says Brian Deese, deputy economic director for the Clinton campaign. "As a result, the next president is going to have to deal with that."

Mr. McCain, the Republican front-runner, hasn't laid out a plan to deal with the looming fiscal crunch. But he has suggested that better-off seniors be required to pay more for drugs and outpatient visits, as a way of controlling Medicare costs. Distancing himself from the current administration and his party, Mr. McCain also calls for drug re-importation from Canada and negotiating prices with pharmaceutical companies.

--Alex Frangos and Henry J. Pulizzi contributed to this article.

Write to Michael M. Phillips at michael.phillips@wsj.com and John D. McKinnon at john.mckinnon@wsj.com

RELATED ARTICLES AND BLOGS

Related Articles from the Online Journal

- Bush Looks to Reprise Tax-Relief Measures
- One Budget Cheer
- Tax Challenges for the Next President
- Darman, Architect of 1990 Pact On Deficit Reduction, Has Died

Blog Posts About This Topic

- Bush proposes cuts in health, domestic progams; Debt remains his legacy getrealnews.blogspot.com

- Bush and LBJ- what they have in commonâ€¦ cafepolitico.us

More related content *Powered by Sphere*