Center for Economic and Policy Research

THE COST OF THE WAR ON TERRORISM AND THE COST OF SOCIAL SECURITY

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The war on terrorism will be costly, but everyone recognizes that it will be affordable. This implies that Social Security will be affordable as well.

For more than a decade, politicians and budget analysts have issued dire warnings about the financial burden that Social Security will impose on future generations of workers. As the baby boomers retire, and more importantly as life expectancies increase, the cost of supporting a relatively larger population of retirees will inevitably grow. There is no dispute on this point. However, there are serious differences as to how the nation should view this prospective burden.

This is where the war on terrorism can assist in understanding the problems facing Social Security. In the wake of the September 11th attacks, the nation has significantly increased its military spending. In addition, President Bush has created a whole new category of expenditures under the general heading of "homeland security." Comparing the size of these spending increases to the projected shortfalls facing the Social Security program can give the nation a better sense of the magnitude of the problems facing Social Security.

President Bush proposes to increase defense spending by $48 billion in 2003. This is approximately $38 billion more than the increase that would be needed to keep pace with inflation. He also proposes to increase spending on homeland security by $19 billion, raising it to $38 billion in 2003. Since spending in this area had been close to zero prior September 11th (there were some relatively minor expenditures that were not lumped in this category), almost the whole $38 billion can be viewed as an increase in spending. Together, the two sources of increased spending come to $76 billion, which is equal to 0.69 percent of the GDP projected for 2003. In other words, the war on terrorism will increase defense related expenditures in 2003 by an amount equal to approximately 0.69 percent of GDP, compared to the situation that existed prior to the September 11th attacks.

Coincidentally, this is almost exactly equal to the size of the seventy-five year shortfall projected by the Social Security trustees in their most recent report. According to the 2001 Trustees Report, if taxes were increased by an amount equal to 0.70 percent of GDP, the program would be fully solvent for the next seventy-five years (Table VI.E5.). This means that if the Social Security trustees projections prove to be exactly on the nose, if the country increased taxes by an amount that is virtually identical to the expenditures associated with the war on terrorism, Social Security would be fully solvent over its seventy-five year planning horizon.[2]

This comparison can be useful. Clearly the expenditures associated with the war on terrorism are not trivial. They will impose a burden on the budget. However, this spending has not been associated with the sort of apocalyptic adjectives which often been used to describe the burden that Social Security will impose on the nation.

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[2] It is worth noting that the Social Security trustees assume that the economy will grow at much slower rate in the future than it has in the past. They project the growth rate will average less than 1.7 percent annually over the planning period. If the economy grows at a rate similar to what the Congressional Budget Office and others project, the shortfall in the program will be considerably less than what the trustees project.

Of course, there is not likely to be any tax increase, or any other major change to Social Security, occurring in the next year. Many politicians and budget analysts have warned that the problem will get worse if the nation delays, and that the necessary tax increases, or benefit cuts, will be larger the longer we wait to take action.

This point is true, but the question is how much difference will delaying action make? Here again the war on terrorism provides a useful yardstick. It is possible to calculate how much of a tax increase would be needed to make the program solvent over its current seventy five year planning horizon, if action is delayed for a period of time. The table below shows the tax increases, measured as a share of GDP and relative to spending for the war on terrorism, which would be needed to make Social Security fully solvent, if we waited 10, 20, or 30 years before taking any action.

The Cost of Social Security and the Cost of the War Against Terrorism

Year of Tax Increase	Size of Increase	Ratio—The cost of SS/Cost of War
2002	0.70% of GDP	1.01
2012	0.86% of GDP	1.25
2022	1.09% of GDP	1.58
2032	1.42% of GDP	2.06

The table shows that the size of the tax increases which would be needed to balance Social Security do increase if the nation delays action. However, the cost of waiting may be considerably less than is widely believed. If the country waits ten years before taking any action, and the trustees projections prove correct, then it would take a tax increase equal to 0.86 percentage points of GDP to maintain the program's solvency. This is 25 percent more than what the nation is expected to spend next year in the war on terrorism.

If the country waits until 2022, then the size of the tax increase needed to balance the Social Security trust fund rises to 1.09 percent of GDP. If it waits thirty years, until 2032, before taking any action, then the cost would rise to 1.42 percent of GDP, an amount slightly more than twice the expenditures for the war on terrorism that are currently projected for next year. These are clearly not trivial sums, but if the war on terrorism proves increasingly expensive in future years, it is entirely possible that it could cost even more than the tax increase of 1.42 percentage points of GDP which would be needed to balance Social Security, if we wait until 2032 to take action.

The point of this exercise is not to trivialize the problems facing Social Security or to argue against spending related to the fight against terrorism. However, from the standpoint of the federal budget, a dollar spent in each area is exactly the same. If the prospect of higher taxes to support Social Security at some future point poses a significant threat to our economic well being, then it must be the case that the expenditures currently planned for the war against terrorism also pose a threat to our economic well being. This is an inescapable logical truth.

Alternatively, if the expenditures made to combat terrorism can be relatively easily accommodated, it must also be the case that the tax increases that may be needed to keep Social Security solvent can also be relatively easily managed. In other words, the dire warnings issued by politicians and budget analysts have no merit.