



CBO Explodes the Myth that Health Care Reform Will Repair the Budget Outlook

By Chuck Blahous

A report this last week by the [Congressional Budget Office](#) (CBO) has exploded the fashionable myth that the federal government has no serious budget problems that comprehensive health care reform won't solve.

As the CBO report makes abundantly clear (and as most budget analysts have known for some time), population aging is the leading factor threatening to drive the government to fiscal extremity in the upcoming decades, well before health care cost inflation becomes the dominant problem.

In recent years, there has rapidly spread a fundamental misconception of the factors driving the federal fiscal imbalance. Crudely stated, this mythical take on the federal budget is as follows:

- We don't really have a spending problem (other than on health care).
- We don't really have an "entitlement" problem.
- We don't really have a large fiscal problem arising from population aging.
- We don't really have a large Social Security problem.
- Virtually our entire federal fiscal problem derives from Medicare/Medicaid, the largest health care entitlements.
- The only reason that the Medicare/Medicaid programs exhibit large fiscal problems is that they are symptoms of a larger national health care problem.
- Hence, national health care reform is the key to fixing the government's dire fiscal outlook.

The number of those parroting this line in recent years is too many to count. It has included respected experts at [one think tank](#) after [another](#). The myth entered mainstream respectability, however, when a [controversial 2007 CBO report](#) purported to show that most of our fiscal problem was primarily attributable to excess health care cost growth alone, with a relatively minor role played by population aging.

Since the myth became fashionable, it has been invoked to derail serious efforts to bring the unsustainable growth of federal spending under control. When there were rumors earlier this year, for example, of the Obama Administration tackling serious entitlement reform -- including Social Security reform -- the left end of the blogosphere

quickly moved to [ridicule any suggestion](#) that there was a broader need to rein in entitlement spending, especially in Social Security.

The problem is: the myth isn't true, wasn't ever true, and there is no remaining basis for claiming that it is true, especially in the wake of the latest CBO report.

Like most myths that catch on, this one has done so because it contains a *kernel* of truth. It's certainly the case that over the long-term the imbalance in Medicare/Medicaid is larger than it is in Social Security. All three programs are designed to pass rising costs mostly to taxpayers, but Medicare/Medicaid are further buffeted by excess health care cost inflation, beyond the effects of population aging that also threaten Social Security. Moreover, it's fair to note that we have a better chance at changing the rate of health care cost growth than we do population aging.

None of these mitigating factors excuse, however, glossing over the vast majority of our imminent fiscal challenge that arises predominantly from population aging, nor does it excuse exploiting the myth to actually *worsen* – rather than to correct – the federal government's unsustainable spending commitments.

To explain all of the logical mis-steps underlying the myth would duplicate the excellent work already done by others, including the Concord Coalition in [“*Honey, I Shrunk the Demographics*,”](#) AEI's Andrew Biggs in [“*Entitlements: Not Just a Health Care Problem*,”](#) and my old boss, Keith Hennessey, in [“*Demographics is a Bigger Problem than Excess Health Care Costs*.”](#)

We can, however, summarize here the chief points that refute the myth:

- The “it's all health care” myth was based on calculations wrongly attributing the interactions between population aging and health care cost growth *entirely* to excess health care cost growth. (If each factor increases costs by 25 percent, for example, the combination increases costs by more than 50 percent, because the effects are multiplicative.) The result thus understated the role of population aging, and overstated the role of excess health care cost inflation.
- Population aging will hit us most forcefully over the next 25 years as the Baby Boomers retire. By 2032, the worker-beneficiary ratio in Social Security will be down to [2.1:1](#), whereas it's over 3:1 today. From that point on, the worker-collector ratio lies nearly flat – it would remain at 2:1 through 2083. Obviously, if one assumes that one phenomenon (excess health care inflation) continues (for the most part) forever, and compares it to another that largely ceases to accumulate after 25 years (population aging), then, trivially, the former will look much larger if one extrapolates far enough.
- Unfortunately, our fiscal problems don't only arise 50-100 years from now, at the point when excess health care cost inflation – even if we assume it continues forever without limit – becomes the dominant factor. The government has a massive fiscal problem to solve over the next generation, and during *that* period, population aging is the much bigger problem.

One could add to these points the fact that Medicare/Medicaid are *not* simply passive victims of cost inflation in private sector health care. The structure of federal health care entitlements has been found to *feed* excess health care cost inflation generally.

All of this is important because this is not just an academic discussion between analysts. It's important because the myth has been used to promote policies threatening disastrous fiscal consequences. Specifically it has been used to:

- *Delay* action on Social Security, causing its shortfall to further worsen;
- *Avoid* spending restraint in other areas of the budget;
- *Avoid* the reality that the government must scale back the growth of its benefit promises in each of Social Security, Medicare and Medicaid;
- Argue that government health care programs are largely the victim of problems in private sector health care, rather than the other way around; and to
- Argue to actually *expand*, rather than *constrain*, the federal role in health care, as well as to increase already-unsustainable federal health care commitments.

Enter the Congressional Budget Office of 2009, in a remarkable about-face, moving aggressively to correct the misimpression left by its controversial 2007 report. The long-term domination of the effects of excess health care inflation is still there in CBO's 2009 projections; but CBO has taken pains to explain that this more distant, difficult-to-quantify phenomenon is well surpassed in urgency by a more imminent and certain fiscal threat: population aging.

The cover of the 2009 report illuminates the sobering predicament of the federal government – even before a massive expansion of federal health care expenses (possibly \$1 trillion over ten years) is contemplated. It shows that under current policies (the plausible one of CBO's two scenarios), federal debt will rise at an unsustainable rate, exceeding 100% of GDP well before 2025, and skyrocketing beyond that.

To what factor does CBO attribute the sustainable growth of federal spending over this period? CBO doesn't mince words:

“Aging is the more important factor over the next 25 years or so. If the interaction is allocated between the two factors, aging accounts for about 64 percent of the projected growth in spending in the major entitlements by 2035.”

CBO is being gentle. Population aging is a much higher proportion of the problem through 2025, which is already past the point where the federal budget picture becomes wholly unsustainable.

CBO's latest report still finds that over the long run, health care cost inflation is the bigger factor – but even to get to that point, the federal government must resolve the fiscal crisis it faces over the next 15 years and immediately beyond.

Another passage in CBO's report undercuts the notion that an expanded federal role in health care will do anything but worsen the problem. To the extent that CBO finds that health care cost inflation will slow in the long term under current law, it is because "state governments and the private sector would have more flexibility than the federal government to respond without statutory changes." Specifically, CBO found that federal programs would contain cost growth *less* effectively than the private sector (p. 29 of the CBO report).

This week's CBO report should put the final nail in the coffin for a myth that has already done much fiscal damage, and threatens to do far more. The reality is that:

- The federal government faces a dire fiscal predicament over the next few decades;
- The spending explosion producing this predicament is driven mostly by population aging; and
- Health care reform will *not* fix this.

My onetime colleague Andrew Biggs points out that this story resembles that movie scene in which Butch Cassidy and the Sundance Kid are debating whether to jump off a high cliff into roaring rapids. The Sundance Kid protests, "I can't swim!" -- to which Butch Cassidy reassuringly says not to worry, for "The fall will probably kill you!"

And that's the reality here. Granted, excess health care cost inflation will probably *eventually* be our biggest problem. That's only true, though, if we enable the federal budget to survive the challenges of population over the next few decades. In other words, we need to survive the fall before learning to swim even becomes relevant.

The sooner that this reality sets in across the political spectrum, the sooner we can have an informed discussion of the fiscal choices facing our federal government.