

INTERIM REPORT OF THE CSIS
INTERNATIONAL SECURITY PROGRAM

Planning for a Deep Defense Drawdown—Part I

A PROPOSED METHODOLOGICAL APPROACH

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EXECUTIVE SUMMARY

As the defense budget is reduced in the coming years, the Department of Defense (DoD) will be confronted with not one but two budgetary threats: it will face not only *fewer* defense dollars but also a *weakening* defense dollar in terms of purchasing power. This weaker defense dollar, driven by the internal cost inflation of personnel, operations and maintenance (O&M), and acquisition accounts in particular, threatens to hollow out the defense budget from within.

Whether the impending decline in the defense budget is caused by the sequester mechanism imposed by the Budget Control Act (BCA) of 2011 or agreed to by a “grand bargain” over government spending and taxes, it is likely to be of similar (if not greater) magnitude to the first \$487 billion cut imposed by the BCA over 10 years. This will require DoD to engage in serious planning and, in all likelihood, to “change the way it does business.”

To help DoD think through *how* a deeper defense drawdown should be conducted and provide a set of recommendations on *what* decisions the Department should make, Kim Wincup and Clark Murdock, both senior advisers at the Center for Strategic and International Studies (CSIS), formed the Defense Drawdown Working Group (DDWG), consisting of approximately 30 leading defense and budget analysts.

This report, reflecting the feedback of the DDWG, outlines a proposed methodological approach for determining which capabilities must be retained and developed in the face of a deep drawdown in the defense budget (defined as an approximately one-third reduction from the FY2010 peak, implemented over the course of 12 years). The CSIS study team’s approach includes an analytic method for differentiating between capabilities that are must-have, nice-to-have, and not-needed. CSIS will implement its seven-step methodology in a second report, to be published in December 2012, which will recommend a roster of 4-5 distinct force mixes, each representing different strategies for how DoD should spend its scarce resources in 2024.

First, we will appraise the demand for military capabilities, taking into consideration the threats to American interests, the physical environment in which military missions are executed, the changing nature of warfare, and the U.S. national security strategy. This exercise will provide a framework and context for making difficult decisions regarding trade-offs in capabilities.

Second, we will identify those high-leverage capabilities that the U.S. military has today and will still be relevant in 2024. Third, we will identify the additional must-have and nice-to-have capabilities that will provide a joint force commander with the tools to cope with future challenges. In combination, these two steps will produce a portfolio of critical military capabilities that comprises the 2024 Desired Force.

Fourth, we will size the 2024 Desired Force by determining the targeted endpoint of a force that costs about one-third less than that of the FY2010 peak. Fifth, we will build a template for the 2024 Desired Force that includes a breakdown of funds available for acquiring equipment, personnel, and infrastructure; funds available for research, development, test, and evaluation (RDT&E), which will enable the U.S. to force the pace of military innovation and maintain technological superiority; and funds available to support the operational force. Sixth, we will build rough order of magnitude (ROM) cost estimates of the specific capabilities (to include weapons, force structure units, and associated infrastructure) required by the 2024 Desired Force. Finally, we will apply the cost estimates to the 2024 Desired Force, producing the menu of alternative force mixes.

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Cover Photo: The Pentagon, headquarters of the United States Department of Defense, photo by David B. Gleason, 2008, http://en.wikipedia.org/wiki/File:The_Pentagon_January_2008.jpg.

INTRODUCTION

On 29 September 2011, the Center for Strategic and International Studies (CSIS) hosted a day-long conference on Defense in an Age of Austerity,¹ which was sponsored by OSD-Policy, to survey the range of views in the Washington think tank community of how declining defense budgets would affect defense strategy, policy, and force structure. As a follow-on effort, Kim Wincup and Clark Murdock, both CSIS senior advisers, have formed the Defense Drawdown Working Group (DDWG), consisting of approximately 30 leading defense and budgeting analysts (See Appendix C for the DDWG schedule and Appendix D for a list of participants). The principal purpose of the DDWG is to provide feedback on charts, briefs, and draft text produced by the CSIS study team in this self-funded study that will both address *how* a defense drawdown should be conducted and provide a set of recommendations on *what* decisions the Department of Defense (DoD) should make as it implements a significant reduction in defense spending. Although the CSIS study team had not originally intended to produce a two-part report, the study timeline has been accelerated and expanded by recent statements of senior DoD officials indicating that the Department was “thinking” about the possible imposition on 2 January 2013 of the sequester mechanism mandated by the Budget Control Act (BCA) of 2011 and that “serious thinking” or “planning” would be begin in mid- to late-summer.²

Part I of this report is intended to provide a methodological and political approach for identifying the must-have and nice-to-have military capabilities (in combination, the “2024 Desired Force”) that must be retained and developed in the face of a deep drawdown (defined as an approximately one-third reduction from the FY2010 peak, implemented over the course of 12 years).

The DDWG co-chairs (Kim Wincup and Clark Murdock) believe that articulating the CSIS methodological approach for conducting a deep defense drawdown could be helpful to DoD, which must plan for an additional \$500B in sequester spending cuts (over 9 years) on top of the \$487B in cuts it has already made in FY2013-2021 to comply with the Budget Control Act. Part II of this report, which will identify potential defense spending additions (aka “puts” and “adds”) and reductions (aka “takes” and “cuts”), will be released in December 2012.

¹ See Clark A. Murdock, Kelley Saylor, and Kevin Kallmyer, “Defense in an Age of Austerity: Conference Proceedings, Presentations, and Key Takeaways,” Center for Strategic and International Studies, October 2011, http://csis.org/files/publication/111121_Murdock_DefenseAusterity_Web.pdf.

² See Jim Garamone, “Panetta, Dempsey Say Pentagon Feels Sequestration’s Shadow,” *American Forces Press Service*, April 16, 2012, <http://www.jcs.mil/newsarticle.aspx?id=874>; Kate Brannen, “Panetta: Sequestration Planning Could Begin This Summer,” *Defense News*, April 29, 2012, <http://www.defensenews.com/article/20120229/DEFREG02/302290016/Panetta-Sequestration-Planning-Could-Begin-Summer>.

BACKGROUND

On 27 January 2009, Secretary of Defense (SecDef) Robert Gates told the Senate Armed Services Committee (SASC) that "the spigot of defense spending that opened on 9/11 is closing" and that the Department would have to make "hard choices."³ In a 10 February press conference, Gates stated his priorities for making "difficult choices among competing priorities and programs":

[W]e will be looking at the budget in terms of efficiencies to be realized, programs with serious execution issues,⁴ and strategic reshaping to make sure the budget reflects the need to balance current and future capabilities and the president's priorities.⁵

Nevertheless, the FY2010 base defense budget request of \$537B still projected 2 percent real growth, as well as an additional 2 percent for moving personnel-focused spending out of the supplemental into the base budget. On 6 April 2009, Secretary Gates announced the results of his "holistic assessment of capabilities, requirements, risks, and needs" with an unprecedented long list of programmatic "cuts" (the Army's Future Combat System, the Navy's DDG-1000 class ships, the Air Force's Airborne Laser, the presidential and combat rescue helicopters, etc.) and "adds" (more special operations forces, UAVs, theater ballistic missile defense, acquisition and cyber experts, etc.) that he later claimed saved the Department about \$330B in FY2010-2011.⁶⁷

Secretary Gates' FY2011 base budget request of \$549B in February 2010 represented a 1.8 percent real increase, although the 2010 Quadrennial Defense Review (QDR) report (also released in February 2010) stated that the "Department will continue to look assiduously for savings in underperforming programs and activities, divestiture, technology substitutions, less-pressing missions, and program areas so that more resources can be devoted to filling these gaps [for capabilities to meet future needs]."⁸ However, little more was said about what former SecDef Donald Rumsfeld used to call "defense business transformation," since the urgency of

³ Robert Gates, "Hearing to Receive Testimony on the Challenges Facing the Department of Defense," January 27, 2009, http://armed-services.senate.gov/Transcripts/2009/01_percent20January/A_percent20Full_percent20Committee/09-02_percent20-percent201-27-09.pdf.

⁴ Chairman of the Joint Chiefs Mike Mullen was a little more explicit the previous day when he told Reuters that the Department of Defense would be looking very seriously at "programs whose costs have spun out of control." See Andrea Shalal-Esa, "Gates says no decisions yet on F-22, other weapons," *Reuters*, February 10, 2009, <http://www.reuters.com/article/2009/02/10/usa-budget-military-idUSN1046176520090210>.

⁵ Robert Gates, "Secretary of Defense Robert M. Gates and Gen. James E. Cartwright at the Pentagon Briefing Room," February 10, 2009, <http://www.defense.gov/transcripts/transcript.aspx?transcriptid=4350>.

⁶ Robert Gates, "Defense Budget Recommendation Statement," April 6, 2009, <http://www.defense.gov/speeches/speech.aspx?speechid=1341>.

⁷ Robert Gates, "Defense Budget/QDR Announcement," February 1, 2010, <http://www.defense.gov/speeches/speech.aspx?speechid=1416>.

⁸ Department of Defense, *Quadrennial Defense Review Report*, February 2010, 24, http://www.defense.gov/qdr/images/QDR_as_of_12Feb10_1000.pdf.

addressing the federal budget deficit, projected at \$1.3T in FY2011, would quickly change the landscape of defense budgeting. Secretary Gates' rhetoric in his 1 February 2010 statement was considerably stronger:

These budget submissions and strategy reviews are suffused with two major themes. The first is continued reform -- fundamentally change the way this department does business, the priorities we set, the programs we fund, the weapons we buy, and how we buy them. The budget and the reviews are also shaped by a bracing dose of realism -- realism with regard to risk, realism with regard to resources. We have, in a sober and clear-eyed way, assessed risks, set priorities, made tradeoffs, and identified requirements on plausible, real-world threat scenarios and potential adversaries.⁹

Despite the nearly 2 percent projected real growth, Deputy Assistant Secretary (DASD) David Ochmanek told *Inside the Pentagon* in April 2010 that the services were "working under the assumption at the moment of zero real growth."¹⁰ In his oft-quoted speech at the Eisenhower Library in May 2010, Gates lauded former president Eisenhower for his vision -- "Eisenhower was wary of seeing his beloved republic turn into a muscle-bound, garrison state -- militarily strong, but economically stagnant and strategically insolvent" -- and made it absolutely clear that a defense drawdown was beginning:

Given America's difficult economic circumstances and parlous fiscal condition, military spending on things large and small can and should expect closer, harsher scrutiny. The gusher [of post-9/11 defense spending] has been turned off, and will stay off for a good period of time...In this year's budget request, the Defense Department asked for, and I hope will receive, just under 2 percent -- roughly that level of growth [needed to stay where DoD is today]. But, realistically, it is highly unlikely that we will achieve the real growth rates necessary to sustain the current force structure.¹¹

He directed all DoD components to reexamine standard practices: "The Defense Department must take a hard look at every aspect of how it is organized, staffed, and operated -- indeed every aspect of how it does business."¹²

On 9 August 2010, Secretary Gates announced specific cost-reduction measures that were expected to save \$102B over FY2012-2016 because "[i]f we are to make a compelling argument for sustaining the topline of the Department of Defense to Congress, we have to demonstrate that we have, in fact, tackled the things that worry them -- poor acquisition practices, poor

⁹ Robert Gates, "Defense Budget/QDR Announcement."

¹⁰ David Ochmanek, *Inside the Pentagon*, April 29, 2010.

¹¹ Robert Gates, "Remarks Delivered at the Eisenhower Library (Defense Spending)," May 8, 2010, <http://www.defense.gov/speeches/speech.aspx?speechid=1467>.

¹² Ibid.

business practices, excessive reliance on contractors, waste, and abuse."¹³ A complex structure of DoD task forces and working groups, which included a DoD-wide organizational "zero-based self-assessment" review, were formed to execute what became known as the "Gates' Efficiency Initiatives" campaign to find savings to reinvest in force structure and modernization. On 6 January 2011, Gates announced the reversal of several positions that he had taken the previous August: (1) he accepted a \$78B reduction in the FY2012-16 defense budget topline, rather than the 1 percent a year in real growth he had hoped for the previous August; (2) DoD would only be able to use \$70B of its \$102B in efficiency savings because \$28B had to be held back for "higher than expected operating costs" such as health care, pay and housing allowances, and the like; and (3) DoD would reduce Army end-strength by 27,000 and the Marine Corps by 15,000-20,000.¹⁴ At the time, DoD was being funded under a continuing resolution that was providing \$530B (\$18B below what Gates had requested for FY2011 in February 2010). He was now requesting \$553B for FY2012, which was \$23B above what DoD was actually getting but \$13B below what DoD had received in FY2011. The defense drawdown had officially entered its second year.

On 13 April 2011, President Barack Obama thanked Secretary Gates for achieving significant savings in defense spending but asked him to do more as the administration reduced "national security spending" \$400B over 12 years as part of the plan to cut the budget deficit by \$4T over 10 years. Although the 2010 QDR had been completed only a year prior, President Obama said he would make "specific decisions about spending" after DoD "conduct[ed] a fundamental review of America's missions, capabilities, and our role in a changing world."¹⁵ In his 24 May speech that formally launched a "comprehensive review" (to address Obama's mandate for a fundamental review), Secretary Gates acknowledged that the president's proposed \$400B drawdown amounted to a projected 5 percent decline in constant dollars -- that is, "slightly less than keeping pace with inflation" -- and was "nothing close to the dramatic cuts of the past."¹⁶ However, the "escalating costs of so many parts of the defense budget" -- CBO estimated at the time that the FY2012-2016 budget was underfunded by \$64B and would require an additional 4-5 percent over the Future Years Defense Program (FYDP) simply to offset rising costs (largely operations and maintenance [O&M], personnel, and health care) -- was causing it to be "hollowed out from within"^{17,18} and eroding the real purchasing power (in terms of military

¹³ Robert Gates, "DOD News Briefing with Secretary Gates from the Pentagon," August 9, 2012, <http://www.defense.gov/transcripts/transcript.aspx?transcriptid=4669>.

¹⁴ Robert Gates, "Statement on Department Budget and Efficiencies," January 6, 2011, <http://www.defense.gov/speeches/speech.aspx?speechid=1527>.

¹⁵ Barack Obama, "Remarks by the President on Fiscal Policy," April 13, 2011, <http://www.whitehouse.gov/photos-and-video/video/2011/04/13/country-we-believe-improving-america-s-fiscal-future#transcript>.

¹⁶ Robert Gates, "Remarks Delivered at the American Enterprise Institute (Defense Spending)," May 24, 2011, <http://www.defense.gov/speeches/speech.aspx?speechid=1570>.

¹⁷ Ibid.

capabilities) of the defense dollar. In a trenchant analysis of the FY2012 defense budget, Todd Harrison from the Center for Strategic and Budgetary Assessment (CSBA) characterized the post-9/11 doubling of the defense budget as one of "hollow growth":

Overall, nearly half of the growth in defense spending over the past decade is unrelated to the wars in Afghanistan and Iraq -- personnel costs grew while end strength remained relatively flat, the cost of peacetime operations grew while the pace of peacetime operations declined, and acquisition costs increased while the inventory of equipment grew smaller and older. The base budget now supports a force with essentially the same size, force structure, and capabilities as in FY2001 but at a 35 percent higher cost. The Department is spending more but not getting more.¹⁹

Although the current defense drawdown may not approach the depth of those after the Korean War (43 percent), the Vietnam War (33 percent), and the Cold War (36 percent) [See Figure 1 in Appendix B], the effect upon DoD's ability to meet the demand for military capabilities may be just as great because of the weaker purchasing power of defense dollars -- that is, as CSIS' preliminary analysis of cost inflation suggests, a nominal 20 percent defense drawdown may "feel" like a 30-35 percent cut to DoD managers struggling to provide military capabilities to meet the nation's needs.

On 1 July 2011, Leon Panetta took over as Secretary of Defense and promised in his introductory message that "there will be no hollow force on my watch" and that implementing the Obama drawdown would "require us all to be disciplined in how we manage taxpayer resources."²⁰ While he agreed with his predecessor that "tough budget choices will need to be made," he insisted that he did "not believe in the false choice between fiscal discipline and a strong national defense" and that both could be achieved. The bar of fiscal discipline soon became much higher for Panetta as the partisan standoff over raising the U.S. federal debt ceiling resulted in the early August passage of the Budget Control Act of 2011. This bipartisan legislation mandated, via "BCA caps" for FY2012-2021, defense spending cuts estimated at \$487B over 10 years. It also established a sequester mechanism that would impose approximately \$500B in additional defense budget reductions if the Joint Select Committee on Deficit Reduction (the "Super Committee") failed to agree (or Congress failed to pass an agreed plan from the committee) on a \$1.2-\$1.5T deficit reduction plan. As discussed in Appendix B, the BCA caps, like the president's 13 April plan, did not result in a real decline in defense

¹⁸ "Long-term Implications of the 2012 Future Years Defense Program," Congressional Budget Office, July 2011, http://www.cbo.gov/sites/default/files/cbofiles/ftpdocs/122xx/doc12264/06-30-11_fydp.pdf.

¹⁹ Todd Harrison, "Analysis of the FY2012 Defense Budget," *Center for Strategic and Budgetary Assessments*, July 15, 2011, <http://www.csbaonline.org/publications/2011/07/analysis-of-the-fy2012-defense-budget/>.

²⁰ Leon Panetta, "Message to the Department of Defense from Defense Secretary Leon Panetta," July 1, 2012, <http://www.defense.gov/releases/release.aspx?releaseid=14621>.

spending and was accepted with little resistance from senior DoD officials. Opposition to the sequester mechanism, variously described as a "mindless," "goofy meat axe," or "doomsday" approach, was adamant because of the "catastrophic," "devastating," and even "emasculating" effect it would have on the Department.²¹ As illustrated by Figure 2 in Appendix B, the sequester cuts will result in a real decrease of 9 percent over the FY2013 FYDP. The sequester cuts are relatively modest when compared to previous drawdowns, although the suddenness with which they are imposed would be wrenching for DoD. In addition, as discussed previously, their impact would be exacerbated because of the weaker purchasing power of the defense dollar due to internal cost inflation.

In keeping with repeated assertions by top administration officials (including President Obama, who went to the Pentagon for the unveiling of DoD's 2012 Strategic Guidance) that this defense drawdown would be "strategy driven," the processes that produced both the "new defense strategy" and the FY2013-2017 budget request ran in close parallel as decisions in both forums were likely iterated back and forth. In his 11 April 2012 talk at the CSIS Global Security Forum, Vice Chairman of the Joint Chiefs of Staff James Winnefeld noted that the new strategy was driven by three factors -- changing geopolitical realities, the changing nature of warfare, and the "new fiscal reality" -- and that while strategy "most definitely preceded and drove every major budget recommendation...[i]t's the first time any of us currently in the Pentagon can remember when a strategy was so closely coupled in time and in action with budget decisions."²² Since the principals in both strategy and budgeting forums are largely the same group of people, deciding whether the first round of BCA cuts was "strategy driven" or "budget driven" is something of a chicken-and-egg problem. Declining budgets should compel more strategic thinking and actions, because the most important priorities should be resourced first.

In an unusual move on 27 January 2012, the Department of Defense issued a white paper entitled *Defense Budget Priorities and Choices* to provide an extended rationale for the FY2013 budget request of \$525B and to detail Pentagon plans for implementing the BCA-mandated reduction of \$259B over FY2013-2017 (the first tranche of the \$487B over FY2013-2021).²³ To summarize briefly, the Department proposed the following:

²¹ See Leon Panetta, "DOD News Briefing with Secretary Panetta and Adm. Mullen from the Pentagon," September 20, 2011, <http://www.defense.gov/transcripts/transcript.aspx?transcriptid=4886>; Leon Panetta, "Remarks to the Association of the United States Army," October 12, 2011, <http://www.defense.gov/speeches/speech.aspx?speechid=1621>;

Leon Panetta, "Testimony before the House Armed Services Committee," October 13, 2011, <http://www.defense.gov/speeches/speech.aspx?speechid=1623>.

²² James Winnefeld, "Keynote Address at the Global Security Forum 2012," Center for Strategic and International Studies, April 11, 2012, http://csis.org/files/attachments/120412_Plenary_GSF_Transcript.pdf.

²³ Department of Defense, "Defense Budget Priorities and Choices," January 2012, http://www.defense.gov/news/Defense_Budget_Priorities.pdf.

- \$60B in "efficiencies and overhead savings" on top of the \$150B identified previously.²⁴
- \$75B in program delays and terminations:
 - Programs that "are experiencing schedule, cost, or performance issues" such as the Joint Strike Fighter and Army Ground Combat Vehicle;
 - Programs that "are augmenting capability that already exists but at a significantly higher cost" (Global Hawk Block 30 over U-2s);
 - Or programs that "are entering service before they are needed" (e.g., Army aviation) or "are deemed excess to requirements" (e.g., commercial satellite imagery).
- \$50B in force structure reductions in U.S. Army and Marine end-strength:
 - Since U.S. forces will no longer be sized for large, long-term stability operations, the size of the active Army will be reduced from a post-9/11 high of about 570,000 in 2010 to 490,000 and the active Marine Corps from about 202,000 to 182,000.
- \$30B in adjustments to pay and benefits:
 - The budget white paper notes that "military personnel costs have doubled since 2001, or about 40 percent above inflation, while the number of full-time military personnel, including activated reserves, increased by only 8 percent during the same period" (for the base budget, the comparable increase in personnel costs was nearly 90 percent or 30 percent above inflation while the number of military personnel had increased by only 3 percent).

For DoD, achieving the BCA-mandated savings was "hard, but manageable": "*hard* because we have to accept many changes and reductions in areas that previously were sacrosanct...*manageable* because the resulting joint force, while smaller and leaner, will remain agile, flexible, ready, innovative, and technologically advanced."²⁵

As discussed in Appendix A, the senior leadership of the Defense Department appears to have absorbed the lessons of previous defense drawdowns and incorporated them into a balanced, to use their term, strategically-informed approach that will not "sacrifice readiness in order to retain force structure" and will not result in a "hollow force" that is under-manned, poorly equipped, or inadequately trained.²⁶ If the current defense drawdown were limited to about

²⁴ The amount of savings sought from efficiency initiatives has always been something of a moving target. In August 2010, Secretary Gates sought \$102B in cost-reduction measures. However, on 6 January 2011, Gates claimed that DoD had found \$154B in savings over the FYDP that "if followed through to completion...[would] make it possible to protect the U.S. military's size, reach, and fighting strength despite a declining rate of growth -- and eventual flattening -- of the defense budget over the next five years."

²⁵ Department of Defense, "Defense Budget Priorities and Choices," January 2012, http://www.defense.gov/news/Defense_Budget_Priorities.pdf.

²⁶ Ibid.

\$500B off the topline (over 10 years) -- which constitutes about a 9 percent real decline that just fails to offset the effects of inflation -- the Gates-Panetta drawdown would be the poster child of best practices and a model for future secretaries. However, there is a big "but" -- what if the drawdown is much deeper? Instead of merely flattening, what if, much as it did after Korea, Vietnam, and the Cold War, the defense budget actually declines significantly? The rhetoric used by senior defense officials about the potential impact of the BCA sequester cuts has been colorful and hyperbolic, but leaves the impression that if further cuts are made, the Defense Department's ability to provide the military capabilities that the nation needs will fall off a cliff. The impression that any further cuts beyond the first tranche would be unacceptable is also conveyed in the more measured language of the defense budget white paper:

As a result of a thorough process that was guided by the strategy and that left no part of the budget unexamined, we have developed a well-rounded, balanced package. There is no room for modification if we are to preserve the force and capabilities that are needed to protect the country and fulfill the missions of the Department of Defense. A change in one area inevitably requires changes elsewhere, unbalancing the overall package.²⁷

It is worth noting that this statement was made to preempt any challenges to how DoD planned to execute a modest decline in defense budgets and seemingly ignores the strong possibility that this is only the first tranche in a much deeper decline in defense spending.

Although some are still in denial about the imposition of the bipartisan BCA cuts,²⁸ the post-9/11 drawdown will both be deeper and steeper than DoD (and its supporters) clearly hope. As discussed in Appendix B, the sequester cuts alone would reduce the defense budget by another 9 percent. Although gaming the post-November 2012 "Taxmageddon" scenario -- the end of CY2012 brings an end to the Bush tax cuts and the Obama payroll tax cut, in addition to triggering the budget deficit reduction sequester mechanism -- has become a cottage industry in Washington, the likelihood that DoD will escape further reductions seems quite small. Preventing the imposition of sequester or, more likely, lifting the sequester once it's triggered will require a "grand bargain" deal on deficit reduction that consists of entitlement cuts and tax increases (sometimes called revenue enhancements). The defense budget, which constitutes 54 percent of discretionary spending, will be part of the solution, given Democratic aversion to entitlement cuts and Republican antipathy to tax increases. Optimistic (from DoD's perspective) scenarios are for a total drawdown of \$800-900B, which would be a 15-17 percent

²⁷ Ibid.

²⁸ The House of Representatives has just passed a budget bill that envisions a \$3.7B increase over the President's \$525B FY2013 request, an amount that actually exceeds the BCA cap by almost \$8B. DoD also understated the actual costs of the base budget by \$6.1B by moving the Army and Marine end-strength that is slated for reductions (by the end of the FYDP) into the OCO account.

cut from the FY 2012 FYDP. Pessimistic (again from DoD's perspective) estimates run from a \$1.5T decrease (28 percent) and above. The author's best guess is that cuts will total \$1.2-1.5T (23-28 percent) depending on how Republicans and Democrats fare in the presidential and congressional races. If President Obama wins re-election, the Democrats retain control of the Senate, and the GOP loses strength in the House, DoD is likely to take a bigger hit (\$1.5T). If Republicans take the presidency and control both houses of Congress, they might prefer to exempt DoD altogether from the contraction in government spending (see footnote 28 and statements by candidate Mitt Romney), but Democratic strength in Senate (and their likely ability to prevent cloture by denying the GOP 60-vote margins) will, in the author's view, keep DoD at the drawdown table.

DoD needs to accept the likely reality that it will absorb a deeper reduction in defense spending and plan accordingly. DoD knows better than anyone that likely eventualities should be planned for. But there is another compelling reason -- DoD must deal with the impact of a weak defense dollar that "buys" less and less military capability each year because of internal cost inflation. DoD now claims to have identified \$210B in "efficiency savings" that it will use to offset topline budget reductions and pay for increased spending on key priorities. It is largely ignoring the fact that the defense budget is being hollowed out from within and that the reduced purchasing power (in terms of military capabilities) of the defense dollar is digging the hole even deeper. A 10 percent drawdown in the topline today will have a much more severe impact than it would have had 20 years ago because the costs of personnel, health, acquisition, and O&M accounts are increasing by as much as 7-10 percent per year. DoD needs to plan for a defense drawdown of a magnitude similar to that of previous drawdowns (about a third), both because its budget might actually go that low and even if it does not, because it needs to come to grips with the weak defense dollar.

CONCEPTUAL UNDERPINNINGS OF THE PROPOSED 7-STEP METHODOLOGICAL APPROACH

The underlying paradigm of the proposed methodological approach is supply and demand -- DoD supplies forces to meet the demand for military capabilities. Unlike the marketplace, where the cost of a product reflects the point at which supply meets demand, the demand for military capabilities (no nation ever is completely secure) always exceeds supply. How much a nation is willing to pay for defense -- that is, the defense budget -- determines how much of the demand for military capabilities it is willing to meet. During an era of declining budgets, the "gap" between demand and supply grows and puts a higher premium on price (see Cost as an Independent Variable or CAIV) in the effort to maximize the amount of capability that can be

purchased with a declining number of defense dollars, which themselves may be declining in purchasing power.

The focus of this supply-demand paradigm is on military capabilities and the ability to execute missions assigned to the military, not on meeting defense goals or national security objectives, which are both at a higher level of abstraction. Operationalizing a defense goal, such as "promoting regional stability" or "defending the homeland" is not straightforward, because so many analytic judgments are required to assess the extent to which a particular set of military capabilities achieves a higher-level defense goal. Moreover, most defense goals and all national security objectives are defined broadly enough that they can be at least partially achieved by non-defense means. This requires another set of judgments on which combination of the so-called "instruments of national power" -- diplomatic, military, intelligence, economic and, in some formulations, developmental, and informational -- will best achieve national objectives or defense goals. Since the task here is shaping and sizing the military instrument, the level of analysis will be at the operational level and focus on the ability of components of military capability to execute missions.

Any military capability represents a weapons system (equipment), the concept of operations (CONOPS) for how these systems should be employed to accomplish a mission, and the men and women who actually employ them, plus any required support infrastructure. While military analysts debate whether it is the U.S. military's technological advantage or its world class personnel that is the basis of U.S. military superiority, most would agree with Secretary Panetta when he said on 11 October 2011 that "we now have the most experienced, battle-hardened, all-volunteer force in our nation's history...They are quite simply our greatest strategic asset..."²⁹ The individual soldiers, sailors, airmen, and Marines who make up the operational force are not the only component of U.S. military capability, since they must be trained and equipped as well, but they are critical.³⁰

Before turning to specific programmatic "cuts" and "adds," it is necessary to define a portfolio of key capabilities³¹ that should reside in the 2024 Desired Force. However, each key capability

²⁹ Leon Panetta, "Lee H. Hamilton Lecture," October 11, 2011, <http://www.defense.gov/speeches/speech.aspx?speechid=1620>.

³⁰ Note the use of the term "operational force" rather than "fighting force." Today's military conducts many missions that are not "fighting" or combat missions. While correct in warning against "mission creep" and the use of the military in non-traditional missions, DoD must accept and plan for the political reality that presidents will often turn to the most well-resourced (by far) "instrument of national power" when confronted with a security challenge. The use of the term "warfighter" is much abused, since it implicitly confers legitimacy onto combat missions and illegitimacy onto non-combat missions (e.g., many stability operations missions). The real differentiation is between "operational personnel" (between those in DoD who actually execute missions assigned to them) and the "non-operational personnel" who support them.

³¹ We prefer the term "key capabilities" or "critical capabilities" to "core competencies," because of their external focus -- that is, they are the capabilities critical to meeting the security environment's demands or key to

(such as ISR or precision strike) is itself a portfolio of capabilities across domains, functions, and missions.³² The matrix-approach to assessing how well a capability executes across the domains of warfare (land, maritime, air, space, and cyberspace) or core missions (however defined) can lead to a proliferation of nested matrices, which can lead to a complex and cumbersome decision tool. However, making informed decisions about which capabilities to keep and which to cut depends, in the final analysis, on how well a particular capability (weapon/people/CONOPS) performs tasks in multiple mediums and contexts across many missions.³³

As the defense budget declines and the defense dollar continues to weaken, the need to establish priorities between capability portfolios and within each portfolio increases. Thus, managing a deep defense drawdown is not unlike triage in that the need to allocate increasingly scarce defense dollars forces one to separate capabilities into bins that the joint force commander (both today and in the future) identifies as must-have, nice-to-have, and not-needed. Establishing priorities on the supply side of the equation also requires prioritization on the demand side. For example, military missions could be grouped according to whether they are mandatory or discretionary.³⁴ The most important must-have capabilities are those essential for achieving mandatory missions. A nice-to-have capability for a mandatory mission is more important than it would be for a discretionary mission. It's a matter of judgment whether a must-have capability for a discretionary mission is of higher priority than a nice-to-have one for a mandatory mission. The importance of the mission does not matter if a

dominating a domain of warfare. The term "core competency" has an internal focus, because it emphasizes sustaining a capability that a firm, organization, or nation may have. Ideally, one wants to have a core competency that addresses the demand function, but all too often (see the U.S. Army and the horse cavalry after WWI and IBM and the mainframe computer at the beginning of the PC era) the internal focus of core competencies can lead an organization to focus on what it likes to do, not what it needs to do.

³² According to the 15 March 2012 edition of *Inside the Pentagon*, Secretary Panetta directed Deputy Secretary of Defense (DepSecDef) Ash Carter to begin conducting "strategic portfolio reviews" of service modernization programs to identify redundancies and capability gaps. Modeled after the Army's capability portfolio review process, this "portfolio of capabilities" replaces the "front-end assessments" used by former DepSecDef Bill Lynn and returns to the "capability portfolio management" process institutionalized by former DepSecDef Gordon England.

³³ Military capabilities are capable of performing multiple missions and are increasingly designed to be robust across many missions in different physical environments. While some missions, such as nuclear deterrence, can be performed by one capability, in this instance "safe, secure, and effective" nuclear forces, even those weapons can perform other missions (e.g., war termination in the case of World War II or "escalation suppression" in recent Russian doctrine). Despite the multi-mission nature of modern military capabilities, DoD follows the programmer's rule -- each weapon belongs to one "jar," otherwise known as a program element (PE). Not only does this make it difficult to weigh the total worth of a capability across multiple missions, rather than just the mission set tied to the PE, it also obscures the fact that, as DDWG member Jim Beale pointed out in a 11 May 2012 email, capabilities funded in a particular PE often require funding in other PEs, which may or may not be funded. Thus, what appears to be a fully-funded capability in one PE may actually be a "hollow capability" because the enabling capabilities are not funded (e.g., jam-resistant GPS signals without military-unique receiver equipment).

³⁴ DDWG member Todd Harrison made this excellent point.

capability is not needed, although this is a judgment defense managers are reluctant to make. Their willingness to make this call, however, should increase as their purchasing power declines.

The principal elements³⁵ of the demand for military capabilities are:

- *Threats* to Americans and American interests:
 - This includes an adversary, whether nation-state, non-state actor, or lone terrorist, which must be overcome in executing a military mission.
- The *physical environment* in which military missions are executed:
 - A shift in strategic emphasis from Europe to the Middle East and then to the Asia-Pacific will have significant effects upon the capabilities (and the capacity of those capabilities) needed (e.g., the intra-theater lift requirements of the Far East approximate the inter-theater requirements of CONUS-Europe).
- The *changing nature of warfare*:
 - The offense-defense competition has always ensured that warfare is not static but constantly evolves as potential adversaries seek to counter or negate the advantages of their opponents and to attack their potential opponents' weaknesses;
 - However, several factors have recently shaped the evolution of warfare in unpredictable ways:
 - The risk of near-instantaneous annihilation through nuclear warfare has both bounded warfare by suppressing high-level warfare between major powers (a phenomenon referred to as the "nuclear overhang") and increased the risks and potential costs of the proliferation of nuclear technology;
 - Rapid technological changes have added two domains of warfare in the 20th century (air and space) and a third one in the 21st (cyberspace) and may bring more (e.g. bio or nano);
 - The overwhelming conventional superiority of the U.S. military has made direct warfare with the United States prohibitively risky and led potential adversaries to focus on "asymmetric" strategies (once known as the "competitive strategies" approach) as an indirect, often less expensive, means to counter U.S. areas of military advantage.
- Changes in *U.S. national security strategy*:

³⁵ DDWG member Katherine Schinasi made many suggestions that improved this report's language, including the use of "elements" as the components of the demand for military capabilities, rather than the more active and inexact terms of "drivers" or "determinants."

- The capabilities needed for a neo-isolationist Fortress America are quite different (both qualitatively and quantitatively) from those needed for a Global Policeman who pro-actively provides security to allies and friends around the globe.
- For example, President Eisenhower's "New Look" strategy relied upon nuclear weapons as a cost-effective means of executing the U.S. grand strategy of containment, an important consideration given post-Korean War reductions in the defense budget; however, the declining credibility of the threat of "massive retaliation" led to the adoption of the "flexible response" strategy under President Kennedy.

BOUNDARY ASSUMPTIONS, DESIGN PRINCIPLES, & ANALYTIC BIAS

As discussed in Appendix A (see "Looking Forward"), the Obama administration has drawn upon the lessons of previous drawdowns in developing its approach to implementing defense cuts (first, with regard to the Gates efficiencies and then, to those imposed by the Budget Control Act). As Kelley Saylor observes and as is discussed above, senior DoD officials (to date) have, in effect, drawn a line in the sand against any further budget reductions because of their "catastrophic" or "disastrous" effect, a political stance that is likely to impede the "serious thinking" about the sequester cuts that is supposed to begin in the summer of 2012. Moreover, DoD does not appear to be addressing (also discussed earlier) the additional challenge of coping with a weakening defense dollar. In an effort to sharpen the focus of our contribution, which is admittedly unimpeded by current political realities or responsibilities, the CSIS study team adopted a set of boundary assumptions and design principles for its methodological approach for a deeper defense drawdown that need to be explicitly defined.

BOUNDARY ASSUMPTIONS

Military personnel costs, which have risen approximately 40 percent above inflation³⁶ since 9/11, are indeed, as Secretary Panetta has said often, unsustainable. As illustrated in Figure 4 in Appendix B, if the defense budget is held constant in real terms and the current trendline in escalating personnel costs (pay, health, housing, retirement, etc.) continues, the entire defense budget will be consumed by the personnel accounts in the 2038-40 timeframe.³⁷ In an effort to preserve a tradespace for military capabilities, our first boundary assumption caps growth in per unit personnel costs:

³⁶ Department of Defense, "Defense Budget Priorities and Choices," January 2012, http://www.defense.gov/news/Defense_Budget_Priorities.pdf.

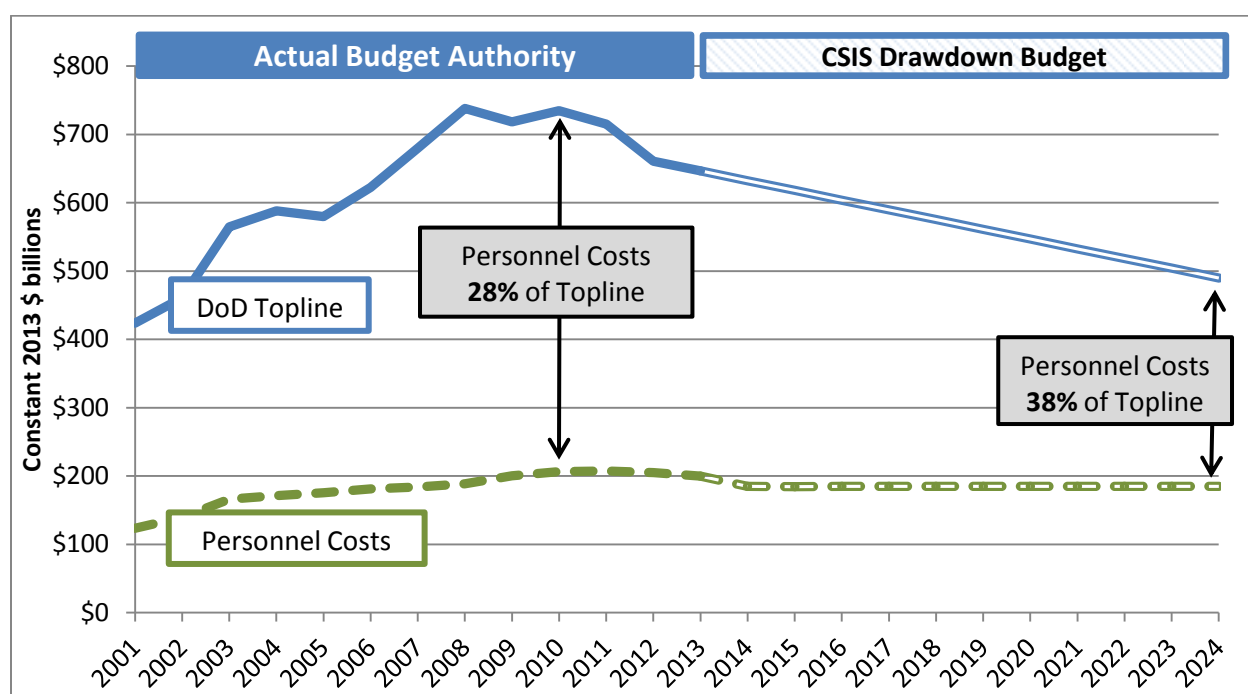
³⁷ Todd Harrison, "Strategy in a Year of Fiscal Uncertainty," *Center for Strategic and Budgetary Assessments*, February 2012, <http://www.csbaonline.org/publications/2012/02/trategy-in-a-year-of-fiscal-uncertainty/>.

- *Personnel compensation (pay and benefits per individual) are stabilized in the next 2-3 years and then maintained at constant levels in real terms until FY2024.*

In Part II of this report, scheduled for release next December, we intend to take DDWG member Andy Hoehn's advice that we do some excursions that relax this assumption. We suspect that it will add specificity to the losses in capability caused by the declining purchasing power of the defense dollar and underscore the necessity of making good on the oft-stated injunction that "DoD must change the way it does business." Figure 1 below illustrates the constraining effect of personnel costs, even if simply held constant.

Figure 1: The Constraining Effect of Personnel Costs

DoD Budget Authority, Constant 2013 \$ billions, 2001-2024



Note: "Personnel Costs" were calculated by summing the Military Personnel account, the Defense Health Program and Medicare-Eligible Retired Healthcare Fund.

Sources: Office of the Under Secretary of Defense (Comptroller), *Fiscal Year 2013 Budget Request Overview*, February 2012; Office of the Under Secretary of Defense (Comptroller), *National Defense Budget Estimates for 2013 (Green Book)*, March 2012, FY 2000-2012 Defense Health Program Justification Books; analysis by CSIS International Security Program

The impact of a deeper drawdown than the current \$487B drawdown, which flattens the defense budget but does not cause a real decline over the next 10 years, will be quite severe without being exacerbated by an arbitrarily rapid or uneven rate of decline in the defense budget. As portrayed in Figure 2 in Appendix B, the sequester cuts begin with a very sudden drop of \$55B imposed after the first quarter of FY2013. This makes the sequester mechanism even more draconian in its potential impact on the U.S. government, but so far has failed in its intended purpose of putting sufficient pressure on both Democrats and Republicans to reach a

PLANNING FOR A DEEP DEFENSE DRAWDOWN

"grand bargain" on taxes and expenditures. As noted earlier, we expect that a "grand bargain" will be reached, although not likely before the sequester mechanism is triggered, and that a less steep but much deeper drawdown will be agreed to. As a consequence, our second boundary assumption is:

- *The defense drawdown will be phased and steady over the ten years.*

DoD has identified (prior to 5 Jan 2012) more than \$150B in savings over five years due to efficiency initiatives³⁸ and (on 5 Jan 2012) claimed another \$60B in new projected savings over FY13-17. Ensuring that these efficiency savings are actually realized (and not "achieved" through budget gimmicks such as moving costs from personnel above the FY2017 ceilings into OCO) is imperative, because a failure to do so will result in then-year budgets that cannot be executed because of short-falls in funds. The sum of unfunded, but still necessary, activities at the outset of an execution year is known as "broken glass." So our final boundary assumption is:

- *No further savings for increased efficiency are likely.*

This does not mean that further savings from increased efficiency are impossible. However, DoD has a relatively poor record of making good on "the negative funding wedges" put into the FYDP to reflect cost-reduction action. Achieving the \$150B in claimed total efficiency savings prior to January 2012 is already a huge stretch goal for DoD and adding another wedge of savings seems injudicious. Further savings are, of course, desirable, since the real opportunity costs of inefficiency are not "wasted" dollars, which the media tends to focus on, but unacquired or lost capabilities that could have improved or maintained the security of the American people.

DESIGN PRINCIPLES

As the administration has, we have absorbed the lessons learned from previous defense drawdowns (see Appendix A) and embraced the following design principles for a deep defense drawdown:

- *Adjust strategy to deep budget cuts by aligning ends to means and shedding missions:*
 - The pursuit of ambitious goals with inadequate means is a recipe for disaster.
- *Preserve the quality of the All-Volunteer Force (AVF):*

³⁸ See Office of the Under Secretary of Defense (Comptroller), "Department of Defense Efficiency Initiatives FY2012 Budget Estimates," February 2011, http://comptroller.defense.gov/defbudget/fy2012/FY2012_Efficiency_Justification_Book.pdf, 1.

- The bias should be towards funding readiness (despite the difficulty of determining the relationship between dollars spent and readiness levels) at the expense of force structure.
- Any system of "tiered readiness," which includes the different level of readiness maintained by Active and Reserve forces, should be driven by the demand for military capabilities and DoD's strategy for meeting the demand.
- *Protect "balanced" procurement at the expense of force structure and end-strength:*
 - As portrayed in Figure 6 in Appendix B, the plans for the current \$487B drawdown take 38 percent of the budget cuts from the procurement accounts, although they only account for 20 percent of the defense budget. This may be "balanced" within the procurement account, but is not "balanced" across procurement, readiness, and personnel accounts;
 - The most critical tradeoff in procurement is temporal -- between how much capability to buy to meet current demand versus how much to invest in preparing for future threats and challenges.
- *Hedge by retaining the ability to mobilize and surge in selected areas (e.g. major combat operations, stability operations, etc.):*
 - Risk should be managed by retaining the ability to respond quickly to lower-probability events and strategic surprises (this is known currently as "reversibility").

ANALYTIC BIAS

The analytic bias of the CSIS methodological approach is towards a smaller force that is robustly manned, equipped, and trained. The imperative to avoid a "hollow force" or "hollow capabilities" translates into cuts that sacrifice force structure in order to preserve readiness and modernization. Unit manning and readiness are protected at the expense of mission coverage and capacity. This does not rule out "tiered readiness" options, but the tiers are defined by strategy (e.g., do not prepare for large-scale, long-duration stability operations) and the ability to mobilize upon strategic warning. It's a smaller force, to be sure, but its component elements are fully modernized and ready.

While the author believes that this bias reflects the lessons learned from past defense drawdowns, DDWG member Steve Biddle suggested that alternative defense drawdown strategies could be developed and assessed. Much like President Eisenhower's Project Solarium at the grand strategy level, 3-5 analytic teams could be tasked to come up with different plans for cutting a third of the defense budget. Examples include: sacrificing force structure for readiness and modernization (the CSIS analytical bias); preserving force structure as the top priority; sacrificing modernization for force structure and readiness; and so on.

While this two-phase study effort will not attempt this "alternative drawdown" exercise, in part because the author believes they have been discredited by experience, Biddle is essentially correct -- the bias in the CSIS methodological approach leans toward making force structure cuts to meet budget reduction bogies.

THE 7-STEP METHODOLOGICAL APPROACH FOR A DEEP DEFENSE DRAWDOWN

Step 1: "Paint a picture" of the multi-dimensional demand for military capabilities that provides a framework and context for making the tough trade-off decisions needed to prioritize U.S. defense capabilities.

The judgment of senior-level decisionmakers (both civilian and military) will be critical in deciding which drivers are the most important elements of the demand function and which portfolio of key capabilities best meets that demand. Providing a holistic context that identifies what is known about the future security environment, as well as the endemic uncertainty of the "known unknowns" and the "unknown unknowns" (to use Secretary Rumsfeld's now-classic formulation) will help inform their judgment and better enable them to manage the risk associated with future-oriented, cost-constrained strategic choices.³⁹

While most decisionmakers (and the analysts advising them) understand the risks associated with the false certainty of "point predictions," most fail to embrace the inherent unpredictability of the bases on which defense planning decisions are made.⁴⁰ This is particularly true with threats and the political direction the U.S. military receives from its political masters. For example, then-candidate George W. Bush said that he would not authorize using the U.S. military for nation-building, but then proceeded as president to do precisely that in Iraq and Afghanistan.

Threats include nation-states, non-state actors, and individuals, many of which are empowered by IEDs, WMD, and cybertechnology and are aware of the American people's general unwillingness to accept the costs (particularly with respect to casualties) of U.S. actions to protect less-than-vital interests. Americans may be more willing to engage on nation-state "unfavorable order" issues (e.g., the rise of China) than on the "disorder" or chaos caused by state failure or brutal governance (e.g., Libya and Syria), but, on occasion, the convergence of nation-state and disorder concerns (e.g., state failure in nuclear-armed Pakistan) may "compel"

³⁹ In Part II of this report, more extensive treatment will be given to all the elements of the future security environment that drive demand -- geopolitical and strategic priorities, threats, causes of conflict, nature of war, and partnership capacity. This outline, however, expands only on threats for illustrative purposes.

⁴⁰ DDWG member George "Chip" Pickett first suggested that DoD needs to plan for the many sources of unpredictability.

U.S. intervention, despite the *2012 Strategic Guidance*'s statement that DoD would no longer plan for large-scale, long-duration stability operations.⁴¹

Although DoD officials routinely laud the virtues of *strategy*-driven capability or force development processes, the reality is that U.S. strategies, particularly when it comes to use-of-force decisions, change much more rapidly and frequently than the U.S. force structures that execute those strategies. U.S. military history is replete with instances (see the 1991 Persian Gulf war) in which military forces designed for one purpose (fighting the Central Front war in Europe) were used for another purpose (reversing Iraq's occupation of the desert kingdom of Kuwait) or were woefully unprepared (e.g., the Korean and Vietnam wars) for the war that the president decided to fight. This inherent lack of predictability about where, when, and against whom the U.S. military will be called upon to engage should both induce a sense of humility in U.S. senior-level officials⁴² and cause them to adopt risk-mitigation strategies to hedge against and bound strategy-induced uncertainties.

Since DoD provides military capabilities to execute the missions assigned to it by political authorities, DoD could propose for SecDef and presidential consideration of a comprehensive set of military missions that are grouped according to whether they are mandatory or discretionary.⁴³ This would provide more focused and specific guidance to DoD on which capabilities are "must-have," "nice to have" or simply "not needed." Having an authoritative list of mandatory and discretionary missions could also induce National Command Authorities to exercise greater prudence in making use-of-force decisions, in part because it counters the all-too-human tendency to characterize "wars of choice" as being "wars of necessity."

Although the United States is a global power with global interests, military operations are most often conducted on a regional basis, which means that U.S. capabilities should be tailored for regional conditions and for regional adversaries.⁴⁴ For example, the capabilities developed to counter the anti-access/area-denial (A2AD) of China are quite different (and more extensive) than those needed for Iran, although the challenge of keeping the Straits of Hormuz open is far from trivial.

⁴¹ Our colleague Nate Freier deserves credit for observing that while U.S. defense planners, in the wake of Iraq and Afghanistan, might want to ignore "disorder" issues and focus on "unfavorable order" ones, events often leave the U.S. no choice but to confront disorder challenges.

⁴² The 2001 *Quadrennial Defense Review (QDR) Report* was released in September 2001 and postulated a 1-4-2-1 force planning construct that said the U.S. would prepare to rapidly deploy forces to four "critical regions" of the globe. Not only did the 2001 QDR report require last-minute revisions to reflect the 9/11 terrorist attack, but also the U.S. military found itself fighting in Afghanistan -- Central Asia was decidedly not one of the four "critical regions" -- within six weeks of the report's publication.

⁴³ Todd Harrison suggested this formulation.

⁴⁴ A brief that John Milam and Bud Hay delivered to the DDWG included a "regional engagement orientation" matrix that specified, by theater, the types of capabilities needed by the U.S. and their respective domains.

Step 2: Identify today's high-leverage capabilities that will still be relevant to 2024 military operations and ensure that these capabilities will be sustained and defended against direct and indirect attacks.

Sustaining U.S. military superiority during an age of austerity will depend increasingly on DoD's ability to first identify and, as stated in the foreword to the 2001 QDR report, then maintain its areas of advantage. DoD must also deny efforts to counter or negate those capabilities, often through asymmetric or competitive strategies, to ensure their continuing advantage. Unlike preparing for direct counters to U.S. military advantages (e.g., increasing force protection for U.S. operational forces), preparing for asymmetric attacks often means building defenses against attacks in areas unrelated to those in which the U.S. military is engaged (e.g., against American citizens traveling abroad or against the American homeland).

Step 3: Based upon one's best understanding of the future demand for military capability (see Step 1), identify those military capabilities (additional to those identified in Step 2) that a joint force commander "must have" to cope with future challenges.

Developing new capabilities to address "critical future deficiencies," and then defending and sustaining them, completes the portfolio of critical military capabilities that comprises the 2024 Desired Force. At this point, since resource constraints have not yet been applied, the portfolio of capabilities should include both "must-have" and "nice-to-have" capabilities. "Not-needed" capabilities are, to put it bluntly, not needed and should be dropped from further consideration.

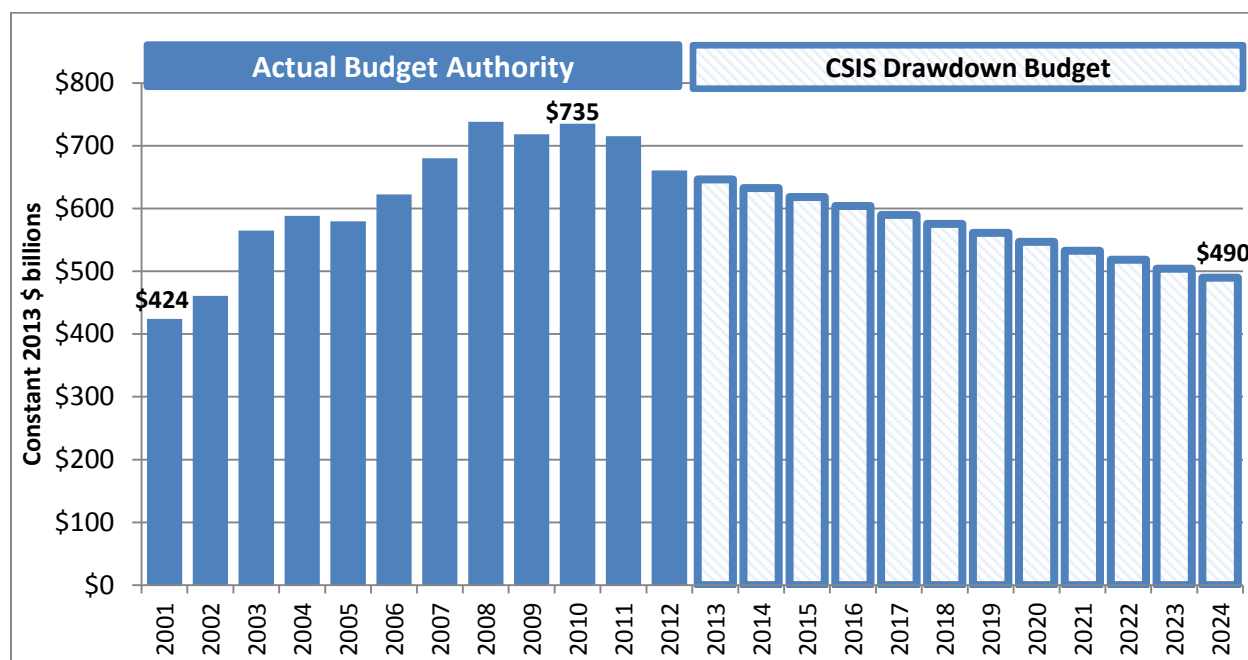
Step 4: The first step in sizing the 2024 force is to determine the targeted endpoint of a deeper defense drawdown force that costs about one-third less in real terms than the total cost (both base budget and "war funding") of the 2010 force, the point at which the post-9/11 buildup peaked.

As Ryan Crotty explains in Appendix B, baselining the post-9/11 defense buildup and the subsequent drawdown is complicated by DoD's use of accounts that funded operations in Afghanistan, Iraq and elsewhere. The "supplementals" and then the Overseas Contingency Operations (OCO) account have been used for procurement spending that was not operationally related (e.g., F-22s) and military personnel that were in the force but scheduled to leave by FY2017. While it might be optimal to come up with an "adjusted base budget" -- that is, a base budget that includes everything in the OCO account that should really be in the base budget -- this would require many fairly arbitrary analytical judgments. In addition, the likelihood that external observers such as the CSIS study team could penetrate budgetary gimmicks intended to fool congressional appropriation staffers is low. Thus, the CSIS study team uses the total defense budget topline as the basis for baselining the current defense

drawdown. Appendix B further defines a preliminary baseline of a one-third decline in the topline total budget, which is illustrated in Figure 2 below. This baseline will be refined in Part II of this report

Figure 2: Projecting a Path to 2024

Total DoD Budget Authority, Constant 2013 \$ billions, 2001-2024



Source: Department of Defense, *National Defense Budget Estimates for 2013 (Green Book)*, Office of the Under Secretary of Defense (Comptroller), March 2012; analysis by CSIS International Security Program

*Step 5: Build a template for the 2024 force that consists of at least the following components:*⁴⁵

- *Capability tradespace*: the percent (TBD) of Total Obligation Authority (TOA) that is available for acquiring equipment, personnel, and infrastructure and comprises the "operational force."
- *Innovation account*: the percent (TBD) which enables the U.S. to force the pace of military innovation, shape the evolution of warfare, and maintain its technological

⁴⁵ If it were politically doable, DoD should deliberately plan for uncertainty and set aside a portion (perhaps 2 percent) of its Total Obligation Authority in an "Unpredictability Reserve" that would provide resources that would hedge against uncertainty and enable the Pentagon to respond quickly to unforeseen developments and events. This would function much like the "management reserve" of acquisition programs in the private sector that are premised on the knowledge that any acquisition program will encounter unexpected cost, schedule, and performance difficulties. However, long-standing congressional hostility to contingency funds and their "undefinitized dollars" (that is, dollars not attached to specific purposes) makes this recommendation a non-starter.

superiority⁴⁶; creating “strategic surprise” by fielding capabilities developed in black programs (e.g., precision strike in the 1970s, stealth in the 1980s and, perhaps, directed energy in the 2020s) can be a game-changer.⁴⁷

- *Institutional force*: the percentage (perhaps 30 percent as a stretch goal) of TOA that supports (for the Title 10 responsibilities of the military services, policy development, and oversight functions of OSD and the Joint Staff, the Combatant Command structures, etc.) the operational force.

Further analysis may identify other essential components that should be added to the high-level template for a military organization.

Step 6: Build rough order of magnitude (ROM) cost estimates of the specific 2024 capabilities (to include weapons, force structure units, and associated infrastructure) in the capability portfolios.

Although costs are implicitly applied whenever cost-constrained tradeoff choices are made, this methodological approach requires a credible process for estimating the costs of future capabilities as an input to inform decisions by senior DoD officials on strategic capability choices. As Andy Hoehn commented, “good costing will be essential.” During the summer of 2012, the CSIS study team will either develop a credible process for future capability costing or, failing that, come up with an alternative way of informing these critical force development decisions. There is only one certainty, namely that these decisions will be made, either explicitly or implicitly. Our preference is for a deliberate planning process where the decisions are made explicitly in a transparent manner that invites debate.

Step 7: Using the 2024 capability portfolios developed in Steps 2 and 3 and the inventory of costing profiles built in Step 6, develop a roster of 4-5 alternative 2024 force mixes for the \$XX billion (TBD) available for capability tradeoffs (see Step 5), each representing different strategies and priorities for how DoD should spend its scarce operational capability dollars in 2024.

Each 2024 force mix alternative should indicate which specific weapon systems (and associated force structure elements and infrastructure) are being acquired and which are *not* being acquired. Understanding the specifics associated with making strategic choices about future capabilities is critical for senior-level decisionmakers who have the responsibility to make these big capability investment decisions and will be held responsible for them.

⁴⁶ Although one DDWG member correctly noted that more dollars do not necessarily equate to a faster rate of innovation, the U.S. has consistently outspent its potential rivals in RDT&E and procurement and has consistently maintained its high-tech advantage. For the U.S. military, weaponizing technology appears to be a core competence.

⁴⁷ Again, our thanks to Chip Pickett for this observation.

FINAL THOUGHTS

A former DoD comptroller once told the author with regard to the politics of defense budgeting: "Make no decision before its time." He was talking about the dilemmas caused by having to carry out several budgetary processes at the same time: executing the current budget (which may require reprogramming); defending next fiscal year's budget on the Hill; preparing the budget request for the year after that; and starting to think about the five-year defense plan that will start three years in the future. Clearly, the senior leadership in DoD faces a similar challenge now -- how do they oppose the sequester cuts mandated by the Budget Control Act of 2011 and, at the same time, prepare for the likely eventuality that the sequester mechanism will be triggered. Why has the Pentagon delayed "serious thinking" until summer? It's not because they are in denial or are confident the sequester cuts won't happen. Secretary Panetta, a well-traveled grandmaster at the game of budgetary politics, appears to be preparing for the endgame in late 2012 and early 2013. The very absence of big programmatic cuts (for example, 1-2 carriers, the Ohio-class submarine, the Next Generation Bomber, etc.) in the first tranche of the BCA cap cuts (totaling \$487B over 10 years) suggests to the author that Panetta is saving his biggest chips for the hard bargaining that lies ahead. This makes sense politically, but it may mean that the "serious thinking" that is supposed to begin this summer will not be very serious. And this would be a big mistake.

DoD faces two budgetary threats, not just one. It's not just fewer dollars for defense; it's also a weakening defense dollar. Whether it's caused by the BCA sequester mechanism or agreed to by a "grand bargain" over government spending and taxes, the defense budget faces another cut of similar (if not greater) proportion to the first \$487B.⁴⁸ In addition, the purchasing power of the defense budget has eroded badly over the past two decades and could continue to weaken if current trends continue. The effect of both budgetary threats on the ability of DoD to provide military capabilities is the same -- less capability to protect the nation and secure its interests. Political bargaining to deal with the threat of another wave of defense cuts may be necessary, but it's not the way to deal with the internal cost inflation that is hollowing out the defense dollar from within.

The purpose of this report was stated at the outset: "to provide a methodological and political approach for determining the key military capabilities that have to be retained (or developed) and sustained as the defense budget declines (in real terms) by approximately a third in 12-13 years, beginning in FY2011 when the total defense budget started to decline from its post-9/11 peak in FY2010." Our proposed 7-step methodology starts on the qualitative side of shaping and sizing the force for an age of austerity by identifying the must-have and nice-to-have

⁴⁸ Alternatively, as Chip Pickett observes, DoD may face years of annual uncertainty about its budget topline as the nation struggles to put its fiscal house back in order.

capabilities for the 2024 Desired Force. Knowing what really matters is key when you have fewer, weaker defense dollars. Our methodology is more mature for the "shaping" issue than it is for the "sizing" challenge. As discussed above, credible costing for future capabilities is essential because it is resource constraints, whether imposed from above or from within, that force the discipline necessary to make tough tradeoff decisions. Hopefully, the Pentagon will have enough purchasing power in 2024 to "buy" all the must-have capabilities the nation needs and the choices will be between nice-to-have capabilities for different missions. This is probably not the case, however.

Part I of this report is being released now in the hope that it will inform and help those in DoD who have the responsibility for these complex and difficult challenges. Over the summer, the CSIS study team will apply its 7-step methodology and present its preliminary results to the Defense Drawdown Working Group in the fall. After revising its report to reflect feedback from the DDWG, as well as a few very senior former DoD officials, the CSIS study team will release Part II of its report in December 2012.

APPENDIX A: LESSONS LEARNED FROM PAST DEFENSE DRAWDOWNS

Kelley Sayler

While the drawdowns following the Korean, Vietnam, and Cold Wars varied in both magnitude and rate of decline, each provides insight into the types of challenges that will be confronted in any future drawdown. For this reason, it will be necessary for defense planners to examine past drawdowns and to incorporate their lessons into a historically informed, strategically driven approach.

POST-KOREA

Following the conclusion of the Korean War, President Eisenhower significantly reduced both the defense budget, which declined as a percentage of gross domestic product from 13.1 percent in 1954 to 9.4 percent in 1961, and the size of the armed services, notably trimming the ranks of the Army by .5 million between 1953 and 1955.⁴⁹ These changes were reflective of the president's broader program of fiscal conservatism as well as his adherence to the doctrine of "sufficiency," which held that minimal gains in capabilities could not justify disproportionately high levels of defense spending. Thus, rather than continuing large-scale investments in weapons systems, Eisenhower sought to leverage existing capabilities to achieve offsetting advantages against the Soviet Union. This objective resulted in the adoption of the New Look national security policy with its emphasis on massive retaliation by nuclear weapons and other cost-saving tools including alliances, psychological warfare, covert action, and diplomatic negotiations.⁵⁰

In addition to pairing this substantial reduction in overall funding levels and military manpower with a change in strategy, Eisenhower shifted the content of defense spending to allow for sizable increases in funding for Research, Development, Test, and Evaluation (RDT&E) – expanding investments from \$19B in 1954 to \$41.7B in 1961.⁵¹ This adjustment was intended to provide a hedge against unforeseen Soviet technological advancement.⁵²

⁴⁹ John Lewis Gaddis. *Strategies of Containment: A Critical Appraisal of American National Security Policy during the Cold War*, Oxford (Oxford University Press, 2005), 162, 169.

⁵⁰ Ibid., 145.

⁵¹ Office of the Undersecretary of Defense, "National Defense Budget Estimates for FY2013," March 2012, http://comptroller.defense.gov/defbudget/fy2013/FY13_Green_Book.pdf.

⁵² Lawrence Korb, Laura Conley, and Alex Rothman, "A Historical Perspective on Defense Budgets," *Center for American Progress*, July 6, 2011, http://www.americanprogress.org/issues/2011/07/historical_defense_budget.html.

POST-VIETNAM

Although the post-Vietnam drawdown saw a less dramatic rate of decline in the overall defense budget compared to that of the post-Korea drawdown, it included a comparable reduction in active duty troop levels. In the post-Vietnam case, however, the impact of this reduction was magnified by the transition to the All-Volunteer Force (AVF) – which was heavily reliant upon pay and benefit incentives – and the failure of military salaries to keep pace with inflation. As a result, the military struggled to meet recruitment goals and maintain sufficient readiness levels. Indeed, the Congressional Research Service reports that “the Army signed up so many poor-quality soldiers during the late 1970s that 40% of new recruits were separated from the Army for disciplinary reasons or unsuitability prior to the completion of their first enlistment...and by 1979, 6 of 10 Army divisions stationed in the United States were assessed as ‘not combat-ready.’”⁵³

POST-COLD WAR

Following the Reagan build-up’s robust levels of procurement spending, “procurement declined to a low point [in 1997] of about half the peak in the mid-1980s.”⁵⁴ This resulted in the so-called “procurement holiday,” during which time the United States failed to adjust its procurement strategy to account for the post-Soviet threat environment. While this decline may have been initially warranted by the scale and success of modernization under Reagan, its duration “[led] to problems with mission availability rates for key equipment, most notably aircraft,” as weapons systems were retained far beyond their intended service lives.⁵⁵ This problem was compounded by the frequent use of military forces, which were mobilized throughout the 1990s for nation-building and stability operations (Haiti, Bosnia and Kosovo, Somalia, etc.).⁵⁶

In addition, the desire to claim the “peace dividend” of the post-Cold War era led to deep reductions in active duty forces as well as a shift to a smaller, but more agile, portfolio of high-technology capabilities. These capabilities, intended to counter a peer or near-peer competitor, were less effective in addressing the irregular conflict that ultimately developed in Iraq and Afghanistan following the strategic shock of 9/11.⁵⁷ Similarly, the revolution in military affairs and dawning paradigm of defense transformation - championed by head of the Office of Net Assessment Andrew Marshall and former Secretary of Defense Donald Rumsfeld,

⁵³ Andrew Feickert and Stephen Daggett, “A Historical Perspective on ‘Hollow Forces,’” *Congressional Research Service*, January 31, 2012, <http://www.fas.org/sgp/crs/natsec/R42334.pdf>.

⁵⁴ Ibid.

⁵⁵ Michael O’Hanlon, “Clinton’s Strong Defense Legacy,” *Foreign Affairs*, November/December 2003, <http://www.foreignaffairs.com/articles/59374/michael-ohanlon/clintons-strong-defense-legacy>.

⁵⁶ Feickert and Daggett.

⁵⁷ Ibid.

respectively - yielded a military that was ill suited to the counterinsurgency strategy that was subsequently employed in these theaters.

LOOKING FORWARD

In conjunction with the January 2012 release of the Strategic Guidance, which outlined the Obama administration's view of defense priorities in the coming decade, the administration conducted an independent review of lessons learned from past drawdowns. The conclusions of this review can be seen in the remarks of senior officials who have expressed, in particular, a commitment to keeping faith with the military, retaining high leverage capabilities, and maintaining readiness by preserving key organizational structures and ensuring sufficient training opportunities for personnel.⁵⁸

The administration has additionally drawn upon the lessons of previous drawdowns in developing its approach to implementing the cuts required by the 2011 Budget Control Act. As President Obama has emphasized, "We can't afford to repeat the mistakes that have been made in the past – after World War II, after Vietnam – when our military was left ill prepared for the future." For this reason, "...the size and the structure of our military and defense budgets have to be driven by a strategy, not the other way around."⁵⁹ This reading is reiterated in DoD's 2012 budget white paper, which explains that the administration's FY2013 budget request "endeavored to avoid the mistakes of previous drawdowns that attempted to maintain more force structure than the budget could afford. Readiness suffered as a result, leading to a hollow force, which took years of investment to reverse."⁶⁰ Furthermore, the administration has stressed that any future drawdown must be guided by the principles of reversibility and balance, thereby distributing risk across a range of national security challenges.⁶¹

While it does appear that senior officials in the Obama administration have absorbed the lessons of past drawdowns, many have thus far failed to consider how to prepare the public for deeper reductions in the defense budget. These officials have repeatedly characterized the consequences of such reductions in hyperbolic terms, an approach that, if continued unchecked, will constrain the administration's ability to effectively implement a drawdown by

⁵⁸ See Martin Dempsey, "Statement of General Martin E. Dempsey, USA Chairman Joint Chiefs of Staff before the House Armed Services Committee: FY13 Department of Defense Budget," February 15, 2012, http://armedservices.house.gov/index.cfm/files/serve?File_id=cd6a5684-65b5-4cae-9a1f-08548675fad1; Leon Panetta, "Major Budget Decisions Briefing from the Pentagon," January 26, 2012, <http://www.jcs.mil/speech.aspx?ID=1678>.

⁵⁹ Barack Obama, "Remarks by the President on the Defense Strategic Review," January 5, 2012, <http://www.whitehouse.gov/the-press-office/2012/01/05/remarks-president-defense-strategic-review>.

⁶⁰ Department of Defense, "Defense Budget Priorities and Choices," January 2012, http://www.defense.gov/news/Defense_Budget_Priorities.pdf.

⁶¹ See Ibid.; Michele Flournoy, "Defense Strategic Guidance Media Roundtable at the Pentagon," January 5, 2012, <http://www.defense.gov/transcripts/transcript.aspx?transcriptid=4954>.

narrowing the space in which decisions about missions and capabilities are made. Moving forward, it will be important for the administration to temper public statements regarding necessary tradeoffs and to refrain from exaggerating the impact of a reduction in defense spending on national security.⁶²

⁶² The author thanks Kim Wincup for this insight.

APPENDIX B: BASELINING THE CURRENT DEFENSE DRAWDOWN

Ryan A. Crotty

During a briefing on the FY2013 defense budget proposal at the Pentagon in February, Under Secretary of Defense (Comptroller) Bob Hale quipped that “there’s an old saying in the budget business: the out years never come.”⁶³ This platitude has become short hand for the uncertainty that plagues the budget. Unfortunately, it has also become a self-fulfilling prophecy in which budget planners have discounted the value of long-term budget planning for short-term political necessities. Indeed, this line reflects less on future uncertainty than it does on the Department’s refusal to plan for a likely future. In the same 17 February briefing, Mr. Hale fielded a question about the decreased pay raises for soldiers over the FYDP, reiterated his witticism, and stated that this sensitive issue would be revisited in “lighter weather.” In deflecting this politically difficult topic, the Under Secretary suggests that the “hard choices” made in the President’s budget were simply to get to down to the prescribed budget number until they can return to business as usual. This is exactly the kind of short term band-aiding that pervades the recent DoD budget process, implying that everything done today is only a bridge to a time in the near future when budgets can go back to growing and hard choices don’t have to be made.

Despite this kind of wishful thinking by the Department of Defense, historical experience and the current economic and fiscal environment suggest that a declining defense budget is a very real prospect. Therefore, the baseline in this Appendix seeks to present a path to a defense drawdown that is in line with historical precedents, and accounts for the internal budget dynamics that are weakening the defense dollar. This presumptive budget will serve as the baseline for framing the evaluation of tradeoffs and alternative scenarios in Part II of this report.

HISTORICAL BASIS FOR A DRAWDOWN

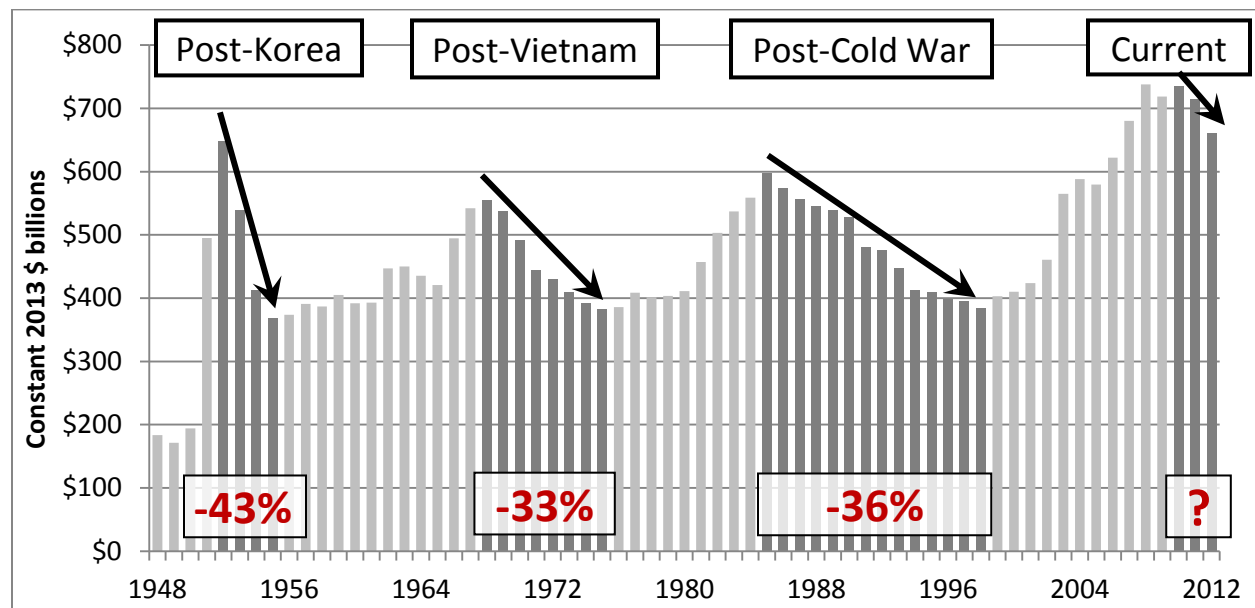
The first assumption for creating a baseline for the current drawdown is that this drawdown is not unique. History shows that the defense budget is cyclical, and that after periods of substantial growth, there is an inevitable return to earth where the budget contracts significantly. While every drawdown is influenced by factors particular to that time in history, they also share certain commonalities. Figure 1, below, demonstrates one of these

⁶³ Robert Hale and Larry Spencer, “DOD News Briefing by Under Secretary Hale and Lt. Gen. Spencer from the Pentagon on the Fiscal 2013 Budget Proposal,” February 13, 2012, <http://www.defense.gov/transcripts/transcript.aspx?transcriptid=4975>.

commonalities: the degree of reduction. In the years following the Korean War, the Vietnam War, and the Cold War, defense budgets declined at least one-third before starting to increase again. The Post-Korea drawdown saw the fastest and deepest budget reduction, declining by 43 percent (in inflation-adjusted dollars) in only three years. After Vietnam, the defense budget declined by 33 percent over seven years, the shallowest of the post-World War II drawdowns. The post-Cold War drawdown saw a 36 percent budget decline, despite the fact that there was no shooting war to come down from.

Figure 1: Defense Drawdowns Since World War II

Total DoD Budget Authority, Constant 2013 \$ billions, 1948-2013



Source: Department of Defense, *National Defense Budget Estimates for 2013 (Green Book)*, Office of the Under Secretary of Defense (Comptroller), March 2012; analysis by CSIS International Security Program

The attacks on 9/11 ushered in a new era of defense spending after the decline following the end of the Cold War. Between 2001 and 2010, the overall defense budget (including war costs) ballooned by almost 75 percent. This increase funded the wars in Iraq and Afghanistan and pumped money back into a department that had seen thirteen years of reductions after the peak of the Carter-Reagan Cold War buildup. The DoD budget flattened out in 2008 at the highest level of defense spending (in real dollars) since World War II.

DEFINING THE DEFENSE BUDGET

The defense budget comes in many forms and in order to maintain consistency, the budget used in this baseline needs to be clarified. The variation between Department of Defense spending and national security funding, budget authority and outlays, or base budget and supplemental appropriations, makes the defense budget an illusory and malleable instrument.

For the last decade, the budget has been divided into two segments: the base budget and the supplementals (later called Overseas Contingency Operations accounts, or OCO).

Supplementals are a mechanism through which to build up funding for emergency needs (like wars) outside of the budget process. In 1951, the first year of the Korean War, the supplemental comprised two-thirds of defense spending, but by 1952, all but a small fraction of war spending had been folded into the base budget. During Vietnam, there were large supplementals in 1966 and 1967, with smaller ones in surrounding years. Nonetheless, the buildup during the wars in Iraq and Afghanistan has seen the widest usage of supplementals over the longest period of time. FY2008 saw the largest supplemental appropriation of the period at \$187B, or almost 30% of the budget. From FY2001 through FY2012, over \$1.3T in war funding has been provided by the supplemental/OCO appropriations.

Ideally, we would separate out OCO funding from the base budget in our drawdown in order to focus on reductions independent of the build-down of forces in Afghanistan. Unfortunately, the OCO appropriations have frequently been used as slush funds for underfunded items for the services, whether or not they are intended for use in Iraq or Afghanistan. As pressure on spending has heated up, OCO has similarly been used to take on items that do not fit in the base budget. Because OCO is outside of the normal budget process, it does not count against deficit reduction packages, and similarly, it is politically easier to vote for war funding for the troops than it is for general discretionary spending. Due to this relatively free movement of monies between OCO and base budget, creating an adjusted base budget that incorporates all non-war funding is difficult, time consuming, and ultimately subjective. Therefore, to increase transparency, and maintain the comparison with previous drawdowns, our presumptive twelve-year budget will include all Department of Defense spending.

Beyond the OCO issue, the other defining characteristics of the baseline for this appendix are as follows: (1) the baseline will use “budget authority” (BA) accounting; (2) the baseline includes only DoD funding (budget function 051) and does not include other elements of national security funding that exist in budget function 050, like Department of Energy national security programs. The only caveat is that in the discussion of sequestration, there may be adjustments based on DoD as a percentage of function 050 because sequestration is based on caps to the entire 050 budget function.

THE CURRENT STATE OF THE DRAWDOWN

To date, defense budget planning has been an ad hoc exercise in which plans have changed substantially year-to-year. Long-term *planned* growth in the budget persisted through FY 2010, FY2011, and FY2012 Future Years Defense Programs (FYDPs), but was reined in by the combination of fiscal pressures from mounting deficits and the wind-down of the war in Iraq. Since FY2010, the total defense budget has been declining. While DoD now recognizes the pressure to trim its budget, so far this has only been done through cuts to growth, as opposed to real reductions. Therefore, preparing for a real decline in budget topline has been replaced by a scalpel approach that addresses near term necessities without addressing structural and strategy-level decisions.

In FY2011, the first year after the spending peak, the Department operated under a Continuing Resolution (CR), as Congress could not come to an agreement on a budget. This CR kept the base budget at FY2010 levels and OCO was reduced by over \$40B. Then, the FY2012 president's request implemented the first tranche of budget "cuts." These cuts represented a reduction in planned spending, but, as demonstrated in Figure 2, they were simply a slowing of the rate of growth of the defense budget.

During 2011, the furor over government inaction in confronting the growing debt and deficit crisis came to a head during congressional debate over raising the debt ceiling in August. In order to break the impasse and address this mounting problem, Congress passed the Budget Control Act (BCA) of 2011 which, first, imposed further pressure on budget growth, forcing growth down to near-inflation levels through discretionary spending caps. The BCA also created the Joint Committee on Deficit Reduction (the "Super Committee"), which was charged with finding an additional \$1.2-1.5T in deficit reduction. The failure of the Super Committee to come to a resolution brought the third mechanism of the BCA into play: sequestration.

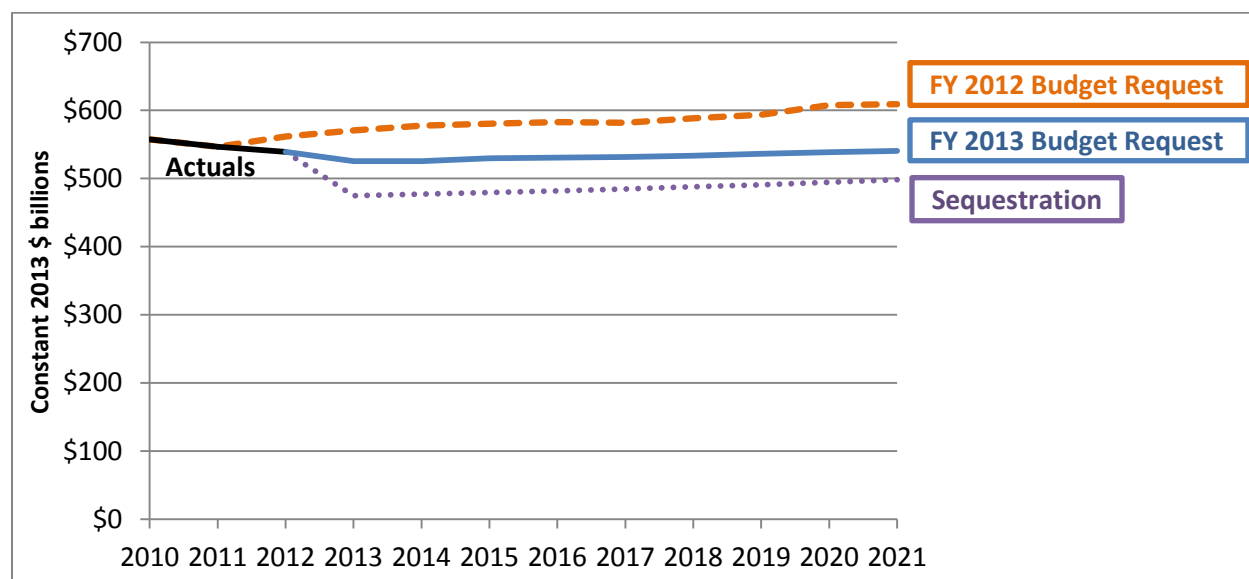
The President submitted his FY2013 budget request after the Super Committee's failure. This budget reflects the caps put in place by the BCA, cutting \$487B from the FY2012 FYDP (extended out to 2021). As can be seen in Figure 2, this \$487B represents a substantial decrease from earlier plans, but still grows slightly above inflation over the ten year period, after an initial \$5B cut from the 2012 enacted level.

The real potential for cuts to the defense budget currently comes from the sequester mechanism, mentioned above. If Congress cannot come to a debt reduction agreement by 2 January 2013, then the defense budget will be cut by almost \$55B on that day. This \$55B reduction applies to every year of the budget through FY2021. The \$55B would be achieved in FY2013 by slicing a percentage off the end of each program. This process takes away any measure of choice from DoD. While this method ensures that the level of deficit reduction

needed will actually occur, it does not allow leeway for DoD to prioritize and align cuts to strategy. Furthermore, sequestration inflicts the deepest cuts in 2013, which is the hardest year for the department to make cuts.

Figure 2: Defense Funding Levels, 2010-2021

DoD Base Budget Authority, Constant 2013 \$ billions



Note: Chart reflects a sequestration based on the FY 13 request baseline

Sources: Department of Defense, National Defense Budget Estimates for FY 2013 (*Green Book*), Office of the Under Secretary of Defense (Comptroller), March 2012; Department of Defense, National Defense Budget Estimates for FY 2012 (*Green Book*), Office of the Under Secretary of Defense (Comptroller), March 2011; Congressional Budget Office, "Final Sequestration Report for Fiscal Year 2012," January 12, 2012; Congressional Budget Office, "Long Term Implications of the FY 2012 Future Years Defense Program," June 2011.

INTERNAL "HOLLOWING" FACTORS

The goal of creating the baseline described in this appendix is to establish a quantitative framework through which to evaluate tradeoffs of systems, people, capabilities and strategies for the Desired Force of 2024. One step in this process is to determine a topline number to cap spending in each year of the drawdown and make cost-based decisions. This topline will be discussed later in the appendix. The other constraint on the tradespace available for capabilities is the internal pressure from the rising cost of doing business within the Department.

These internal constraints are generated by the inflation of costs within the defense budget over the past decade. The increasing costs of doing business that do not correspond to an increase in capability have led to a weakening defense dollar, where each dollar in the defense budget buys less than it did the year before. The cumulative effect of this weak defense dollar is a "hollowing out from within."

Similarly, cost growth in internal accounts, including personnel and operations and maintenance, is projected to continue in the future, and this will in turn crowd out other areas of discretionary spending.

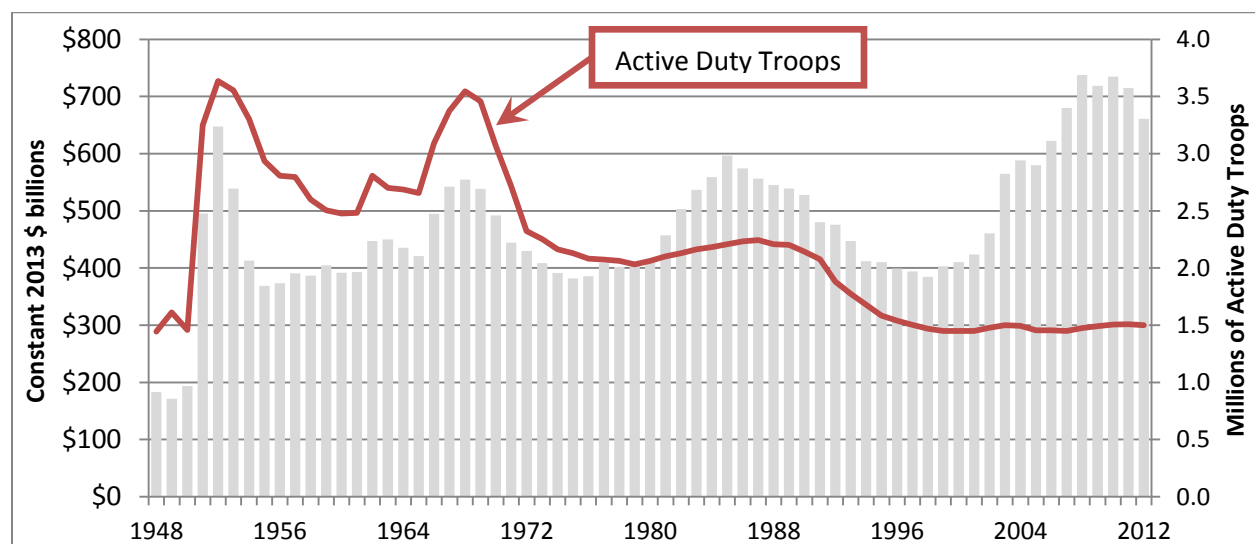
PERSONNEL

The most pressing of these “hollowing” forces is in the costs of military personnel. The problems caused by the personnel question during this drawdown are twofold.

The first issue is that of force size. As shown in Figure 3, budget buildups have historically been accompanied by troop buildups. This meant that during the subsequent drawdowns, these forces were reduced, providing a cushion for making budget reductions. But, during the wars in Iraq and Afghanistan, troop numbers saw a minimal increase. This means that in order to derive significant savings from troop reductions, force structure will have to be cut well below the size of the standing force from the last fifteen years.

Figure 3: Defense Budget and Active Duty Troop Levels, 1948-2012

Total DoD Budget Authority, Constant 2013 \$ billions, and Millions of Active Duty Troops



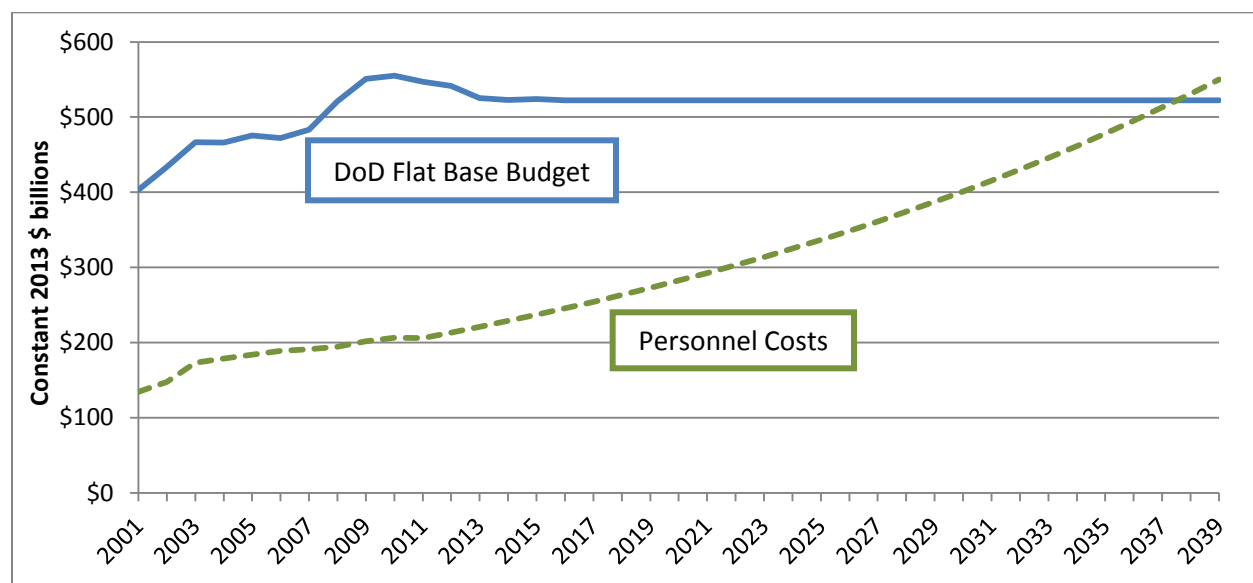
Source: Office of the Under Secretary of Defense (Comptroller), *National Defense Budget Estimates for 2013 (Green Book)*, March 2012; analysis by CSIS International Security Program

While force size has remained relatively the same over the buildup, the costs of those troops in pay and benefits expanded greatly. Thus, the second facet of the personnel budget is in the internal cost inflation caused by both external factors and conscious decisions by the government. While the generosity of the government in supporting combat troops is understandable, the broad increase of pay and benefits has created a crisis within the defense budget that mirrors that of the entitlement programs in the broader U.S. budget. Congress has repeatedly authorized above-inflation pay raises for the military and enacted new benefits,

including the \$11 billion per year TRICARE for Life (TFL) program.⁶⁴ The cost of these expanded benefits has been compounded by the inflation of healthcare costs and the fixed nature of military premiums. Due to these issues, military personnel costs have increased by at least 40 percent on since 2001. Much like Norm Augustine’s aphorism that the entire defense budget will eventually only buy one aircraft, the spiraling costs of personnel threaten to overwhelm the defense budget. As seen in Figure 4 below, if the budget were to remain flat and the price of pay and benefits were to continue to rise at the same rate of growth they have experienced since 2001, the entire defense budget would be consumed by personnel costs by 2039.⁶⁵

Figure 4: Augustine’s Law Applied to Military Personnel Costs

DoD Base Budget Authority, Constant 2013 \$ billions, 2001-2039



* Concept for chart courtesy of Todd Harrison

Note: The “Personnel Costs” line was calculated by summing the Military Personnel account, the Defense Health Program and Medicare-Eligible Retired Healthcare Fund. Beyond 2012, Personnel Costs were calculated at a growth rate equal to that from 2001-2012.

Sources: Office of the Under Secretary of Defense (Comptroller), *Fiscal Year 2013 Budget Request Overview*, February 2012; Office of the Under Secretary of Defense (Comptroller) *National Defense Budget Estimates for 2013 (Green Book)*, March 2012, FY 2000-2012 Defense Health Program Justification Books; analysis by CSIS International Security Program

On the positive side, DoD recognizes the threat that these ballooning costs pose to the budget and has begun to address them in the President’s FY2013 budget request. DoD plans to save \$16.5B over the FYDP by lowering pay raise rates after 2014. They also calculated savings of \$12.9B by increasing Tricare enrollment fees that have been static since 1995, adding a TFL

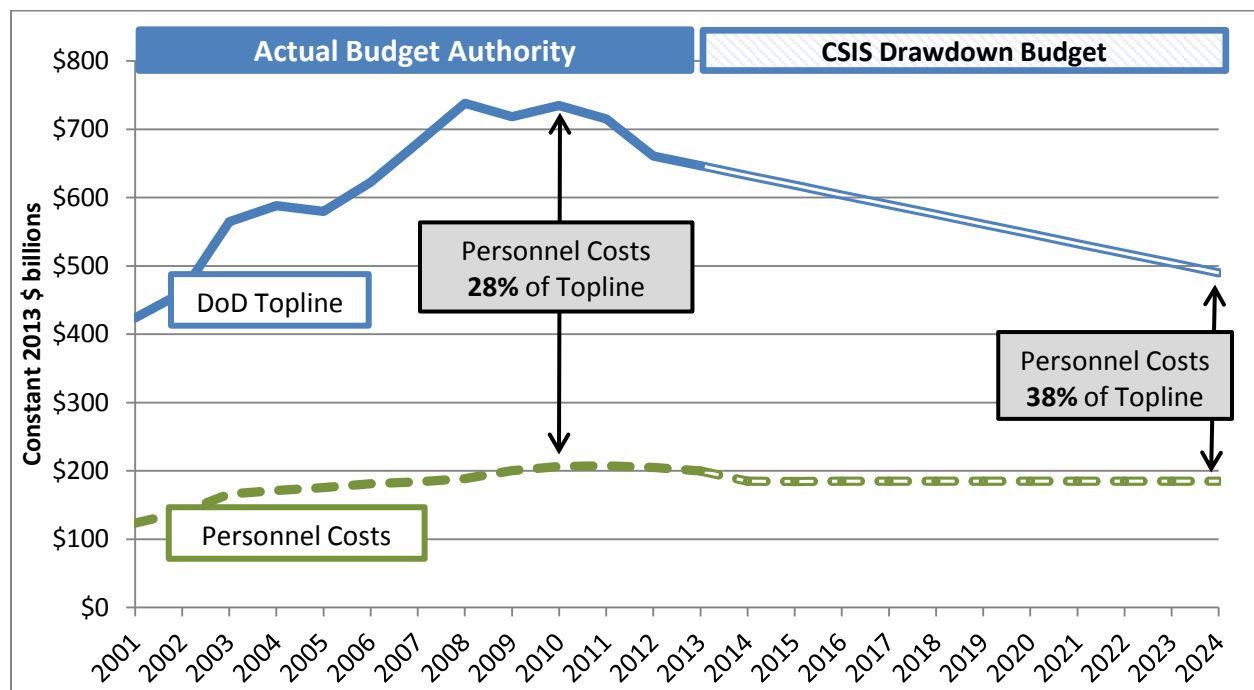
⁶⁴ Todd Harrison, “Strategy in a Year of Fiscal Uncertainty,” *Center for Strategic and Budgetary Assessments*, February 2012, <http://www.csbaonline.org/publications/2012/02/trategy-in-a-year-of-fiscal-uncertainty/>.

⁶⁵ Harrison, *Strategy in a Year of Fiscal Uncertainty*.

enrollment fee, and increasing pharmacy co-pays.⁶⁶ But, these savings are all contingent on the approval of Congress, which has been the guarantor of increasing pay and benefits over the last decade, despite DoD's efforts to contain these costs.

Part II plans to include an excursion addressing the pay and benefits crisis, but the baseline will assume that by FY2017, the end of the current FYDP, personnel costs will have been controlled and that these costs will remain flat (in real terms) out to the end of the period. As seen below, even with a flat personnel budget, these costs begin to consume a higher percentage of the budget as the topline budget comes down, thus constraining the tradespace available for modernization and capabilities. One caveat to this flat personnel budget is that, as the Working Group develops alternative force structures and postures, these personnel costs will be adjusted on a per capita basis to reflect the force size. With a flat personnel budget, personnel costs go from 28 percent of the budget in FY2010 to 38 percent of topline by FY 2024, and even the assumption of flat personnel costs presumes major policy changes by DoD that would have to make it through Congress.

Figure 5: The Constraining Effect of Personnel Costs
DoD Budget Authority, Constant 2013 \$ billions, 2001-2024



Note: "Personnel Costs" were calculated by summing the Military Personnel account, the Defense Health Program and Medicare-Eligible Retired Healthcare Fund.

⁶⁶ Office of the Under Secretary of Defense (Comptroller), "Fiscal Year 2013 Budget Request Budget Briefing," February 2012, http://comptroller.defense.gov/defbudget/fy2013/FY2013_Budget_Request.pdf.

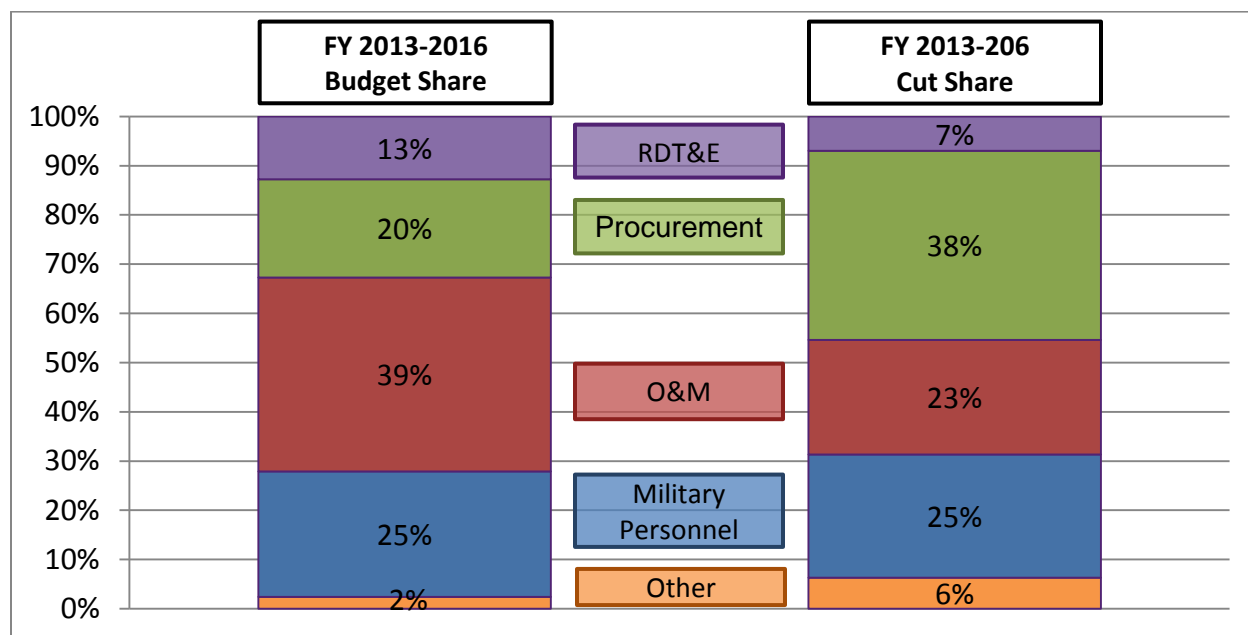
Sources: Office of the Under Secretary of Defense (Comptroller), *Fiscal Year 2013 Budget Request Overview*, February 2012; Office of the Under Secretary of Defense (Comptroller), *National Defense Budget Estimates for 2013 (Green Book)*, March 2012, FY 2000-2012 Defense Health Program Justification Books; analysis by CSIS International Security Program

OPERATIONS AND MAINTENANCE

Personnel costs are not the only constraint in dealing with a shrinking budget. Operations and Maintenance (O&M) costs have also experienced significant growth over the past decade. Due to the bottom-up nature of O&M spending, these costs can be very difficult to control. Furthermore, the rate of growth has increased dramatically. According to the Congressional Budget Office (CBO), O&M costs per active-duty soldier grew steadily from 1980 to 2001, doubling from \$55,000 per soldier to \$105,000.⁶⁷ But after 2001, the rate of increase leapt forward, doubling again in just nine years to \$211,000 per soldier. While per soldier costs are expected to decline with the wind-down of operations in Afghanistan, DoD still projects far higher per soldier costs than the historical rate of growth would suggest. Figure 6 illustrates how hard it is to reduce O&M: it consumes 39 percent of the President's FY2013 DoD budget request for the years 2013 to 2016, but only contributes to 23 percent of the cuts made to meet the BCA caps.

Figure 6: Allocation of Cuts to Get To the BCA

DoD Base Discretionary Budget, Constant 2013 \$ billions



Note: Base Discretionary Budget, does not include OCO. Numbers may not add due to rounding.

⁶⁷ Congressional Budget Office, *Long Term Implications of the FY 2012 Future Years Defense Program* (Washington, DC: U.S. Government Printing Office, June 2011).

Source: Office of the Under Secretary of Defense (Comptroller), *National Defense Budget Estimates for FY 2013 (Green Book)*, March 2012; Office of the Under Secretary of Defense (Comptroller), *National Defense Budget Estimates for FY 2012 (Green Book)*, March 2011.

PROCUREMENT

The procurement account, shown in green above, presents the other side of the coin. Because of the internal pressures of things like O&M that are difficult to cut, particularly in the short run, other items take the brunt of that burden. The procurement account pays for all of the major military equipment that is the hallmark of the modern U.S. military: tanks, planes, guns, and ships. As seen above, the procurement account makes up 20 percent of the FYDP budget, but absorbs 38 percent of the cut to reach the BCA caps.

Procurement is frequently the first segment of the budget to take a hit during a cut drill. Unlike cutting personnel, reforming pay and benefits, or trying to trim O&M, there is little lag time necessary to stop buying a piece of equipment.⁶⁸ During the drawdown following the Cold War, procurement absorbed the lion's share of spending cuts for years. This "procurement holiday" was mitigated by the fact that the Cold War buildup had completely modernized many major hardware programs, including tanks, planes, helicopters, submarines, and surface ships. Thus, a fleet of new cutting-edge platforms justified the reduction of procurement accounts in the near term. This is not the case today. While procurement spending over the last ten years has been relatively high, it has gone to specific war-fighting hardware tailored to the wars in Iraq and Afghanistan. At the same time, much of the fleet of major platforms has been neglected, and the average ages of almost every major piece of equipment is older than it was at the end of the last buildup. Also unlike the Cold War, many platforms have been in heavy service for over a decade, and much of the fleet, even if not modernized, needs to be recapitalized after the ravages of fighting in the Middle East.

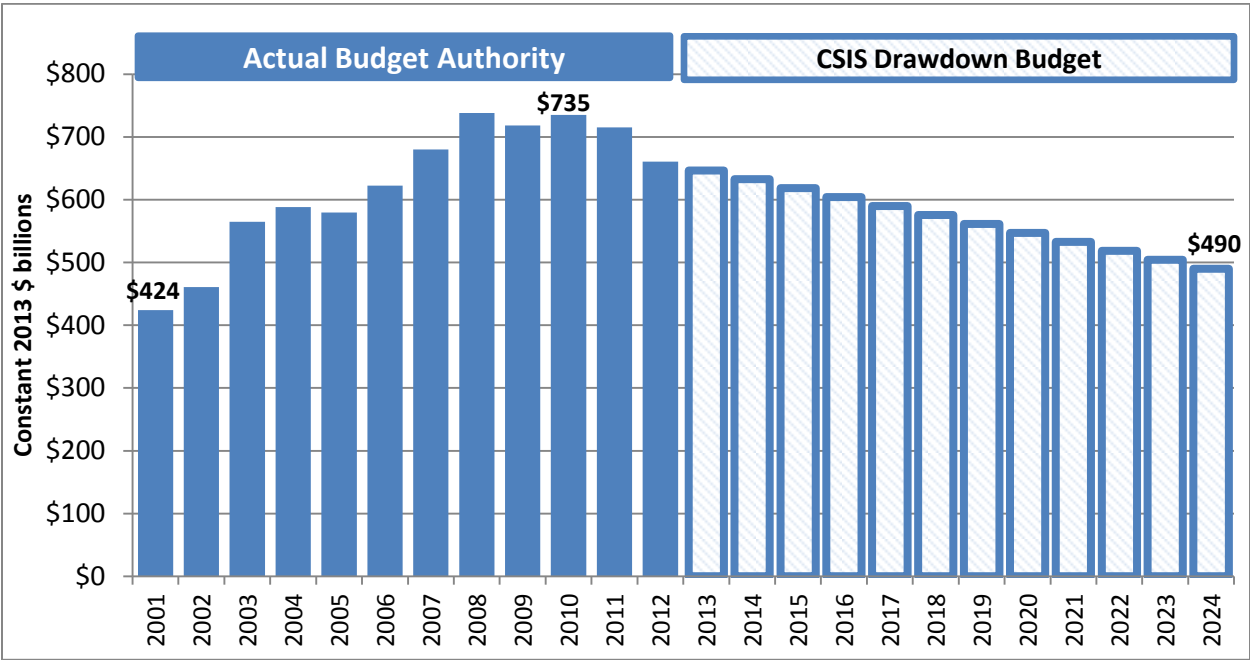
THE BASELINE FOR THE CSIS DRAWDOWN

The report will follow a drawdown from a starting point of FY2010, the high point of current-dollar spending, to a final year of 2024. As discussed above, historically, drawdowns have seen a decrease of one-third. So, in order to create a baseline from which to evaluate funding decisions, the final year of this effort, 2024, will have an inflation-adjusted budget of one-third of the FY2010 budget, or \$490 billion. Figure 7 below demonstrates an illustrative glide path from 2010-2024 which would result in a budget one-third below the peak year. This baseline assumes a reduction in the defense budget that follows a smooth glide path from FY2013 to FY2024 and avoids the steep drop-off seen in sequestration. By stretching the cuts out over a

⁶⁸ Although there can be longer-term cost problems created by early program terminations, as many contracts have large buyout costs in them to end the contract prior to completion.

smooth glide path, the approach of this report allows for conscious departmental decisions that address structural and strategic issues.

Figure 7: Projecting a Path to 2024
Total DoD Budget Authority, Constant 2013 \$ billions, 2001-2024



Source: Department of Defense, *National Defense Budget Estimates for 2013 (Green Book)*, Office of the Under Secretary of Defense (Comptroller), March 2012; analysis by CSIS International Security Program

The baseline described above will provide a framework over which to lay various force postures and structures that DoD could employ that fit within this realistic budget scenario for the next 12 years. While the authors reserve the right to alter this baseline over the course of the study, this broad framework will inform all of the costing and tradeoffs developed for the Part II.

APPENDIX C: DEFENSE DRAWDOWN WORKING GROUP SCHEDULE

Although the initial round of spending cuts mandated by the Budget Control Act of 2011 will not require a fundamental change in the nation's defense strategy, as articulated in the 2010 Quadrennial Defense Review, cuts substantially beyond this level will likely force DoD to examine the growing disconnect between strategy and resources. To help facilitate the long-range planning needed to address this misalignment, the Defense Drawdown Working Group, co-chaired by senior advisers Clark Murdock and Kim Wincup, convenes approximately 30 leading defense and budgeting analysts to provide feedback on charts, briefs, and draft text produced primarily by the CSIS study team.

Session 1: Overview of CSIS Approach & Assessment of DoD's Strategic Review

25 January, 0800-0930, Basement Conference Room C (B1C), CSIS

DDWG will provide feedback on the Murdock-Wincup brief and discuss the 5 January DoD rollout of its adjusted strategy.

Session 2: Best Practices for Managing the Defense Drawdown

7 March, 0830-1000, Basement Conference Room C (B1C), CSIS

DDWG will discuss a CSIS brief (lessons learned from past drawdowns & recommended design principles) and a commissioned brief on how DoD should address the management challenges facing them.

Session 3: Critical Factors Determining the Shape and Size of the Future Force

5 April, 0800-1000, Basement Conference Room C (B1C), CSIS

DDWG will provide feedback to a CSIS brief and a commissioned brief that first identifies, and then establishes priorities between, the principal determinants for both defining the qualitative nature and the relative quantities of the capabilities needed by the 2020+ U.S. military.

Session 4: Interim Report Methodology & Future Security Environment

9 May, 0800-1000, Fourth Floor Conference Room (4CR), CSIS

DDWG will provide feedback on the CSIS interim report draft outline on how the defense drawdown should be conducted, receive a short brief on baselining the current

drawdown and discuss (if time permits) a CSIS brief on the context in which future military missions are likely to be executed.

Session 5: Must-have Capabilities for the 2024 Force

18 July, 0800-1000, Fourth Floor Conference Room (4CR), CSIS

DDWG will discuss today's high-leverage capabilities and, based upon the future security environment and likely evolution of warfare, identify additional "must have" capabilities that will be required to cope with future challenges.

Session 6: Costing the 2024 Force

25 September, 0800-1000, Basement Conference Room C (B1C), CSIS

DDWG will discuss the capability trade space as well as CSIS' rough order of magnitude (ROM) cost estimates of the specific capabilities in the 2024 portfolio.

Session 7: Roster of Alternative 2024 Force Mixes

24 October, 0800-1000, Basement Conference Room C (B1C), CSIS

DDWG will discuss the CSIS roster of 4-5 alternative 2024 force mixes, each of which will represent a different strategy for how DoD should spend its operational capability dollars in 2024.

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