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Social Security and Medicare Spending Growth: Is it Just More Seniors or More Per Senior?

- **Long-term federal budget forecasts show sizable increases in federal spending in the coming decades**
- **A large share of this increase in spending is due to Social Security and Medicare**
- **Some of this is due simply to the growth in the eligible population but is some due to growth in spending per beneficially**
- **Our finding show that each accounts for sizable shares of the growth. Thus, there is room to limit benefits without cutting them and still constrain spending growth**

Most long-term projections indicate a large increase in the size of the federal government. For example, the Congressional Budget Office (2018) projects that federal spending as a share of GDP will rise from 20.6% in 2018 to 26.9% by 2040. This is greatly concerning to many people who worry that the increased role of government in the economy – and the consequent reduction of the private sector – inevitably comes with diminished work and investment incentives, reduced productivity, limited economic growth, and lessened opportunities for individuals to improve their lives.

Over half of this projected increase in federal spending is due to increased spending on Social Security and Medicare. Thus, any discussion of limiting federal spending should address these two programs. This paper examines two aspects of the projected increase in Social Security and Medicare. One aspect is purely demographic. The baby boom generation has begun to retire and will do so in increasing numbers over the next two decades. This alone drives up spending. The other aspect is the generosity of the benefits paid by the two programs. If these are increasing as well, this adds to the growth in spending.

These two components have different implications regarding how spending can be limited. If all of the increase is due to growth in the senior population, limitations in spending are more difficult since it requires reducing benefits. However, if a good deal is due to benefit increases, limiting spending can be done by slowing the growth or capping benefits at current levels. As described below, the spending growth in these programs is due to both sources, so there is room for limiting this growth without actual cuts in benefits. Indeed, we find that capping real spending per beneficiary of Social Security and Medicare at their 2017 level has substantial effects on the expected path of future spending. Instead of rising to about 12% of GDP, it would rise to about 9% and fall thereafter to a share no larger than today's. However, the methods used to limit spending growth are important. Use of price controls on services and mandating limits on types of coverage generate shortages, non-price rationing, and political infighting over what is covered and who is served. These methods to limit spending growth are highly undesirable.

The rest of the paper is organized as follows. Section II gives more background and details on expected spending growth of these programs and on the magnitude of the issue. Section III describes how spending and spending growth on Social Security and Medicare can be broken into components. These components are the number of seniors – the primary beneficiaries of the spending – as a share of the population, spending per senior, and GDP per capita. Spending per senior is denoted as absolute generosity and spending per senior relative to GDP per capita is denoted as relative generosity. The latter indicates benefits per senior relative to per capita national income.

Section IV presents the data on the forecasted time path of these components. Seniors' share of the population will grow by about one-third by 2040. Additionally, real Social Security and Medicare benefits per senior are forecast to grow as well. However, real GDP per capita is expected to grow a little faster that real Social Security benefits per senior, but slower than real per senior Medicare benefits. Section V shows the results of exercises that simulate capping real Social Security and Medicare benefits per senior. Growth in simulated spending still rises for a while because of the growth in the senior population – but by much less than current projections - and spending as a share of GDP eventually declines. Section VI discusses issues regarding 3 limiting spending on these programs, as well as the pitfalls noted above of price controls and mandated limits on coverage.