

Analysis

Long-Term Deficit Reduction: Less Pain, More Gain

By ROBERT M. SOLOW AND JON BARON, The Fiscal Times on Aug 12, 2010

Many policy officials and economists support immediate federal stimulus spending to spur economic recovery in the short term, but are also increasingly concerned about [chronic budget deficits](#) over the long term. It is widely believed that a day of reckoning will come, when painful spending cuts requiring hard choices will be needed to avert economic catastrophe.

That later process, however, need not be so painful. Largely overlooked are clear examples, from welfare and health care policy in the 1980s and 1990s, in which research studies identified program reforms that produced major budgetary savings without adverse effects. Similar cost-saving opportunities already exist in a few areas, and many more could likely be identified through rigorous research.

The welfare example is bipartisan. From the Reagan through the Clinton Administrations, federal officials funded rigorous evaluations of [state and local welfare](#) reforms, using the scientific “gold standard” method of randomly assigning individuals to a program or control group. These studies showed convincingly that certain reform models which emphasized moving participants quickly into the workforce through short-term job search assistance and training — as opposed to providing remedial education — produced large gains in employment and earnings, reductions in welfare, and net savings to the government of \$4,000 or more per participant. These results helped shape the 1996 welfare reform act, whose strong work requirements transformed U.S. welfare policy and helped bring about major reductions in welfare rolls and gains in employment among low-income Americans during that era.

Similarly, in health care policy, federal officials in 1995 launched a rigorous randomized evaluation to test prospective payment of Medicare home health agencies — i.e. paying such agencies an up-front lump sum per patient — against the usual cost-reimbursement approach. The evaluation found that [prospective payment](#) reduced costs to Medicare by 20 percent over three years, compared to cost reimbursement, with no adverse effects on patient health. This finding helped shape Medicare’s nationwide implementation of prospective payment for home health agencies in 2000, generating major cost savings in this \$15 billion program.

More recent rigorous studies have already identified several other cost-saving opportunities. In health care, a nurse-administered smoking cessation program for hospitalized smokers has been shown in definitive studies to produce a 30 percent increase in confirmed abstinence from smoking one year later, at a cost of \$150 per patient. Nationwide implementation of this program would likely produce sizable Medicare and Medicaid savings, since smoking is the leading preventable cause of disease in the United States, according to the Centers for Disease Control, accounting for approximately \$96 billion in annual health care spending.

In crime prevention, [Multidimensional Treatment Foster Care](#) — which places severely delinquent youth with foster families trained in behavioral management — has been shown in rigorous studies to produce a 50 percent reduction in criminal activity over two years, at a cost that is 30 to 50 percent less than the cost of typical community treatment (placement in a group residential care facility). Here, too, nationwide implementation could well produce budgetary savings, while reducing crime.

To identify enough of these cost-saving strategies to produce sizable long-term deficit reduction, many more rigorous evaluations that test a wide range of strategies are needed. In part, this is because

experience suggests that many of those tested will be found not to work. For example, the welfare evaluations — in addition to identifying a few reform strategies with large effects — showed that many strategies thought to be effective based on expert opinion or preliminary studies actually had little impact on welfare and employment.

Similarly, the federal government's ongoing [Medicare Coordinated Care Demonstration](#) has been rigorously evaluating 15 promising cost-saving strategies for Medicare patients with chronic conditions, designed to coordinate care among their many physicians. Now at the two-year mark, the study has found that none of these strategies is reducing Medicare costs enough to pay for itself.

Unfortunately, rigorous evaluations are still rare in most policy areas, falling far short of what is needed to identify a sizable number of effective strategies. The president's budget proposes an important, but modest, rigorous evaluation initiative. It could be expanded — perhaps even as part of short-term stimulus — to identify effective longer-term cost-saving strategies across the range of federal programs areas, such as defense procurement, health care, retirement savings, education, housing and foreign aid.

It is widely believed that austerity and hard choices are the only path to reducing long-term spending. Indeed, they may have their place. But there may also be another way, one that uses ingenuity and entrepreneurship to develop new cost-saving strategies, and scientifically rigorous studies to identify those that really work.

Robert M. Solow is a Nobel Prize winner in economics and professor emeritus at the Massachusetts Institute of Technology. Jon Baron is President of the Coalition for Evidence-Based Policy.