

TESTIMONY OF

SCOTT WALLSTEN, PH.D.

**VICE PRESIDENT FOR RESEARCH AND SENIOR FELLOW,
IGROWTHGLOBAL**

**SENIOR FELLOW, GEORGETOWN CENTER FOR BUSINESS & PUBLIC
POLICY**

BEFORE THE

JOINT ECONOMIC COMMITTEE

FEBRUARY 28, 2008

Scott Wallsten, Ph.D.

Vice President for Research and Senior Fellow, iGrowthGlobal

Senior Fellow, Georgetown Center for Business & Public Policy

Mr. Chairman and members of the Committee, thank you for inviting me to testify today on the costs of the war.

I estimate that the expected net present value of the total direct costs of the war are approximately \$1 trillion to the U.S., and closer to \$2 trillion globally.

The real direct economic costs of the war include not only expenditures from the U.S. budget allocated for the war, but also injuries, lives lost, and lost productivity from reservists who cannot do their civilian jobs because they have been called up for service.

My coauthor, Katrina Kosec, and I began this project in 2005 and have updated our numbers periodically since then. (I submitted the original 2005 paper, which explains our methodology in detail, to the Committee). We have found that the total direct economic costs of the war at any given point in time tend to exceed budget appropriations by about 20-25 percent.

As wealthy as our nation is, our resources are limited and must be spent carefully. Other areas of policy attempt to explicitly take into consideration the full economic costs and benefits of government actions. President Ronald Reagan signed an executive order requiring certain agencies to conduct a cost-benefit analysis for any proposed major regulation and to adopt it “only upon a reasoned determination that the benefits of the regulation justify its costs.”

President Bill Clinton renewed this order, as did the current president.

And now cost-benefit analysis has become an important and accepted, though certainly not the only, tool for evaluating many proposed policies.

But this approach has yet to be explicitly incorporated into decisions regarding defense and security.

Admittedly, the current tools we have for evaluating costs and benefits are not perfectly suited for evaluating the costs of war since they were developed for use in a different setting. The tools are blunt and imprecise, meaning that the cost estimates all of us are presenting today are measured with a great deal of error. That's why Katrina and I included in our paper ranges of estimates and also built an online estimator that allows people to change underlying assumptions to see how those affect the costs.

Nevertheless, this type of analysis can provide valuable information to help inform policymakers as to the best course of action going forward.

In addition, we should apply these tools to other, related, areas, like homeland security. The Office of Management and Budget estimated last year that major homeland security regulations imposed a cost of \$2.2 to \$4.1 billion dollars a year on the economy.¹ But those rules were passed with no estimates of their expected benefits. Those costs may sound small compared to the costs of the war, but they are not. The net present value of those costs is close to \$100 billion.

Estimating the benefits of homeland security measures or of military operations is difficult because, as OMB acknowledges, they depend on the probability and severity of outcomes like terrorist attacks, which are difficult to quantify.

Just because expected costs and benefits are difficult to estimate doesn't mean they don't exist. And if you can't estimate the benefits, you should still follow through on a policy only if you have good reason to believe those benefits exceed the costs.

Professor William Nordhaus of Yale was the first to do this exercise for a war in Iraq, and he did it before the war when it could have helped inform policy.² He

¹ White House Office of Management and Budget. 2007. "Draft 2007 Report to Congress on the Costs and Benefits of Federal Regulations." Washington, DC.

² Nordhaus, William D. 2002. "The Economic Consequences of a War With Iraq." *NBER Working Paper*. Cambridge, MA.

acknowledged that there would be some benefits of a war. The world would be better off if Saddam Hussein were not in power. But Professor Nordhaus meticulously estimated ranges of the likely costs under different scenarios and concluded that a war in Iraq could cost between \$100 billion and \$2 trillion. And he further qualified the results by noting factors that he did not include, such as costs to other countries or, as he put it, “fallout that comes from worldwide reaction...against perceived American disregard for the lives and property of others.”

The point, aside from noting that Professor Nordhaus was far more insightful than any of us by doing this exercise in advance, is that even under tremendous uncertainty, these tools can provide us with useful information to help inform decisions. If Congress and the public had seriously considered Professor Nordhaus’s projected cost estimates, would we still have gone to war? Perhaps. Some might have still believed it was worthwhile. But perhaps not.

We can’t do anything about the costs we have already incurred. Those resources are gone. But we do have some control over what happens next. The lesson, I believe, is that policymakers can use the tools of cost benefit analysis to help evaluate whether proposals regarding what to do next in Iraq are likely to yield net benefits to us and to the world.

And hopefully that additional information will lead to better decisions.

Thank you.