Research Brief

RAND NATIONAL DEFENSE RESEARCH INSTITUTE

Slowing the Increase in Military Pay

Key findings:

- It may be possible for the Department of Defense to save money on military pay while sustaining a high-quality force. This possibility is suggested by three facts:
  - Recruiting and retention have been robust.
  - Demand for personnel is decreasing.
  - Military compensation compares well with civilian opportunities.
- Potential savings from decreasing the rate of increase in basic pay range from approximately \$5 billion to \$17 billion over the next ten years, depending on the actions taken.

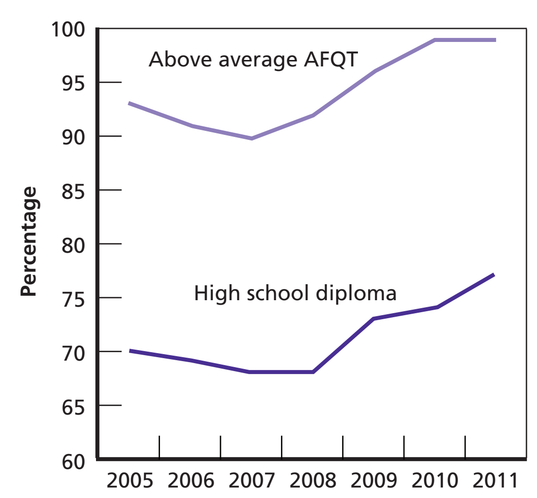
On February 14, 2012, in testimony before Congress, Secretary of Defense Leon Panetta revealed plans to "provide more limited pay raises beginning in 2015." This measure is one of many department-wide spending reductions driven by budgetary pressures to reduce the federal deficit. A key question is whether the Department of Defense (DoD) can realize savings in the military personnel budget without jeopardizing the nation's ability to sustain a high-quality all-volunteer force. Recent research by the RAND Corporation takes a step toward answering this question by considering the rate of growth in pay. (Other areas, such as controlling the cost growth of military health and retirement benefits, could also be examined but are beyond the scope of this work.)

Two Favorable Trends

Current defense manpower supply and the outlook for future manpower demand both suggest conditions favorable to a slower growth in military pay. Recruiting and retention are currently robust. The military services' active and reserve components have met or exceeded their numerical recruiting and retention targets since 2009, and have met and often exceeded quality targets for recruits set by the Office of the Secretary of Defense. These quality standards state that at least 90 percent of recruits should have a high school diploma, and at least 60 percent should score at or above average on the Armed Forces Qualification Test (AFQT). Indeed, overall recruit quality has steadily increased (see Figure 1).

Also, manpower requirements are anticipated to decrease in the coming years. The war in Iraq has ended, and the United States aims to reduce its presence in Afghanistan over the next two years. DoD plans to decrease the size of the active-component force by 72,000 soldiers and 20,000 Marines over the coming years. This will lower numerical recruiting and retention targets in the Army and Marine Corps. Thus, not only are the supply and inventory of quality personnel high by historic standards, but demand is also decreasing.

Figure 1
Percentages of Active-Component Enlisted Accessions in DoD That Are High Aptitude and Are High School Graduates



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Opportunities in the Civilian Sector

Another factor in judging whether conditions are suitable for a slower rate of increase in military pay is the economic opportunity in the civilian sector compared with that in the military. During the late 1990s, the private economy boomed and civilian pay grew faster than military pay. However, from fiscal years (FYs) 2000 to 2010, military pay increased faster than pay in the civilian economy. The RAND analysis examined this trend more closely.

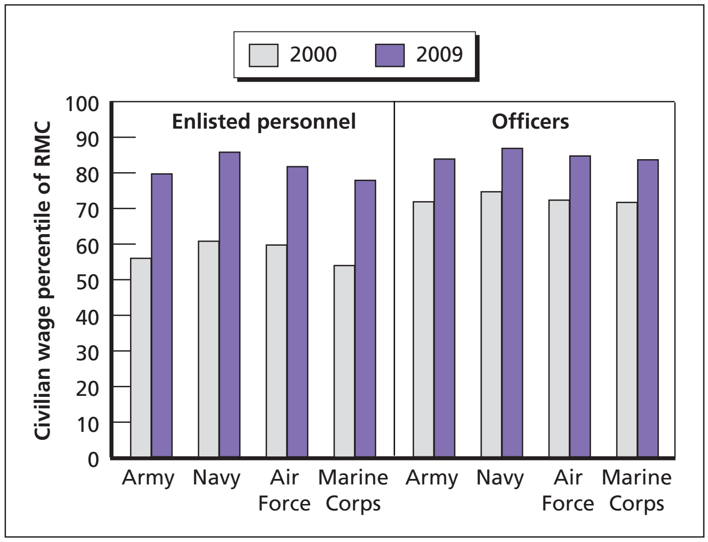
Military and civilian pay comparisons generally take two forms. One is to compare changes in basic pay to the Bureau of Labor Statistics' Employment Cost Index (ECI) for wages and salaries in the private sector. Another is to determine how military pay ranks in percentile terms against the distribution of civilian wages for workers who are comparable in terms of age and education to those in the military. For this latter comparison, regular military compensation (RMC) is used. RMC is a more expansive measure of pay that includes basic pay, subsistence and housing allowances, and the tax advantage that derives from the fact that allowances are not taxed. By either measure, military pay ranks well.

In FY 2000, Congress authorized an immediate 6.8 percent increase in basic pay along with a stream of annual basic pay increases equal to the percentage increase in the ECI plus half a percentage point (0.5) through FY 2006. This increase continued through 2010 in view of the burden on military personnel during a period of war. In addition to the higher-than-usual increases in basic pay, the housing allowance increased in the early part of the decade to cover the full, expected cost of off-base housing.

Together, these pay actions increase basic pay and RMC relative to civilian pay. Basic pay is up 45 percent since 2000, substantially more than the ECI (up 33 percent) and the Consumer Price Index (up 31 percent). For men and women in uniform, this means that basic pay buys a lot more than it used to.

As a further point of reference, the Ninth Quadrennial Review of Military Compensation proposed that RMC should reach at least the 70th percentile of comparable civilian earnings in order to sustain the size and quality force desired by the military departments. While military pay increased over the last decade, civilian pay (adjusted for inflation) did not—dropping 4 to 8 percent for most age and educational groups between 2000 and 2009. As a result, military pay is now well above the 70th percentile for civilian wages in most enlisted and officer age and education groups (see Figure 2). For instance, regular military compensation for enlisted personnel with a high school diploma at ages 23–27 grew from the 54th–61st percentile (depending on service) in 2000 to the 78th–86th percentile in 2009; for officers with a college degree at ages 28–32, regular military compensation increased from the 72nd–75th percentile to the 84th–87th percentile.

Figure 2
Regular Military Compensation as a Percentile of Civilian Wage, Officers and Enlisted Personnel, 2000 and 2009



Other factors also affect military-civilian pay comparisons. Perhaps the most important is the cost of health care. Active-duty service members receive health care at no cost, and the cost for their families is quite low. The fact that military members avoid the cost of health care premiums paid by civilian employees is highly valuable in an era of rapidly rising health care costs. Health care premiums increased approximately 150 percent from 2000 to 2010. In addition, the high rate of civilian unemployment (over 9 percent in 2011 and over 8 percent now) serves to decrease expected civilian wages. Together, these factors increase the differences in military and civilian pay in a way favorable to the military.

Options for Saving Money on Current Pay Growth While Sustaining a High-Quality Force

Rising recruit quality, falling manpower requirements, and high levels of military pay compared with those in the civilian sector suggest that conditions are now favorable to consider slowing the rate of increase in military pay, thereby saving money in the defense personnel budget. RAND reviewed several options:

1. Setting the basic pay increase at half a percentage point below the ECI for one year
2. Freezing basic pay for one year
3. Instituting a series of below-ECI increases, such as ECI minus half a percentage point for four years.

Choosing among these options requires balancing two effects of any rollback in pay, whether brief or prolonged. The first is the amount of money saved. The second is the level of concern that might be voiced in Congress, in the military, and in the public at large over what may be perceived as a devaluing of military service or a failure to appreciate the sacrifices of service members during a time of war. Thus, policymakers will need to weigh the advantages and disadvantages of each option before deciding on a course of action.

The first option is the most cautious, but it is perhaps the most acceptable to those concerned that service members not be shortchanged. It would realize savings of about $5 billion over the next decade. The second and third options produce more savings—about $17 billion over the next ten years—but are likely to be viewed more skeptically by those concerned that compensation be adequate. A further consideration comes into play when deciding between options 2 and 3. A multiyear strategy could lose momentum and support, particularly if the economy improves and recruiting and retention become more challenging. Furthermore, a lack of decisive action on pay reductions could create uncertainty for service members and affect recruiting and retention decisions.

Overall, conditions are currently favorable for DoD to be able to slow the growth in military pay, enabling savings in military personnel costs while achieving force management goals. ■

This research brief describes work done for the RAND National Defense Research Institute documented in *Should the Increase in Military Pay Be Slowed?* by James Hosek, Beth J. Asch, and Michael G. Mattock, TR-1185-OSD (available at http://www.rand.org/pubs/technical_reports/TR1185.html), 2012, 52 pp., $19.95, ISBN: 978-0-8330-7414-0. The RAND Corporation is a nonprofit institution that helps improve policy and decisionmaking through research and analysis. RAND's publications do not necessarily reflect the opinions of its research clients and sponsors. RAND® is a registered trademark.

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