

The State of the Union Address: What It Means to Government Contractors

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While the president newly embraced the concepts of American greatness and exceptionalism, he warned us that the world has changed and that the nation must be prepared to face unprecedented global challenges. Toward this end, Mr. Obama believes that we must invest in innovation, ease the path to job creation for businesses, make hard decisions about reducing the federal deficit, and streamlining and simplifying the way government does business.

HIGHLIGHTS

Innovation

The president's budget will include investments in information technology to spur productivity and clean energy technology to break our dependence on foreign oil. In education, he urged the Congress to continue funding for the 'Race-to-the-Top' program and expand tax credits to offset the expenses of a four-year college education. For infrastructure, he called for additional funding for transportation, but added the goal of expanding wireless coverage to 98 percent of Americans within the next five years.

Becoming More "Business Friendly"

Mr. Obama also called for reducing the burdens on business by simplifying the tax code, lowering corporate taxes, and eliminating unnecessary regulation. Other than plans in play to analyze the burden of regulations on small businesses, no specifics were offered. He also set forth the goal of doubling exports by 2014, and urged the Congress to approve the trade agreement with South Korea as well as other such pacts he plans to pursue in the coming years. And, in a bow to critics of Obamacare, he acknowledged that some flaws, like the bookkeeping reporting requirements for small businesses, need to be fixed while vigorously defending the healthcare overhaul.

Federal Deficit

Shifting his focus to America's debt, the president conceded that it is a mounting problem that needs to be addressed, but that he largely inherited it from his predecessor. In order to put America's fiscal house in order, he proposed a five-year freeze on discretionary spending and made it clear that he was willing to cut "excessive spending" wherever it may exist, but that he will not allow the budget to be balanced "on the backs" of the most unfortunate. He also indicated his support for Social Security reform provided it did not reduce coverage or benefits, and did not entail any degree of privatization. Again, in an effort to move beyond his base, he embraced the concept of medical malpractice reform in order to lower medical costs, but used the occasion to defend Obamacare as a means to balance the budget. Finally, he promised greater transparency in spending and the activities of lobbyists, vowed that he will veto any bill that contains earmarks, and reiterated his opposition to extending the Bush tax cuts for the wealthy beyond two years.

Federal Reorganization

Seeing competent and efficient government as essential to the task of a creating an America that can compete in a global economy, Mr. Obama will send to Capitol Hill a proposal to "merge, consolidate, and reorganize" the federal government. Of course, the devil is in the details yet to be released.

GovWin'S TAKE

The president used his recent political setbacks and the vigorous and heated state of our political discourse as a celebration of America's uniqueness and greatness--that it is symbolic of the strength of our system, not a weakness. By embracing the constitution and the 'American Dream' in his rhetoric, he tried to place himself within the American mainstream while implying that his agenda will enable us to remain great. However, while Mr. Obama hit many of the right notes, all will depend on the details. The biggest criticism is the dichotomy of 'investing' while reducing spending. Given America's fiscal condition and the stated position of Republicans in the Congress, that will be a major sticking point. As the president conceded, the current targets don't really address the main fiscal issues; deep cuts in spending are required to eliminate the deficit, much less pay off the accumulated debt. It remains to be seen if Republicans are serious about tackling profligate spending and are

willing to absorb the political body blows that are coming their way. If not, any cuts will be minimal.

Regardless, it seems likely that funding opportunities for government contractors will continue--one way or the other. However, contractors will undoubtedly be required to work harder for the win and withstand significant scrutiny of performance to justify costs. While a freeze on discretionary spending may have some impact, the level of current spending has expanded some 25 percent (excluding the stimulus bill) over just the past two years. This sets two very distinct tones within the budget debate: the president conceding the "need to freeze," yet at current spending levels that will provide some latitude for investments in innovation, technology, and infrastructure versus the Republican leadership citing FY2008 (and in some cases FY2006) spending levels as the target.

While the extent of the proposed cuts mentioned last night (which included those recently announced by Secretary of Defense Gates) won't be seen for a few weeks, Mr. Obama stated that he will consider any proposal to cut more and tough decisions needed to be made. The good news for contractors is that he sees investment in IT as essential to America's ability to compete and innovate so it isn't likely that he will propose major cuts in this area. IT investment will not only be important for global competitiveness but to support his proposal to consolidate and reorganize government, which will require considerable IT spending to the extent that it is embraced by the Congress. Accordingly, it seems unlikely that contracting opportunities will dry up significantly in the shorter-term; rather they will adapt to fit the House Republicans' agenda more so than the president's.