Tea Leaf

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Your guide to understanding today's economy and financial markets

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And So It Begins!

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You may have heard the media buzz this week about Kathleen Casey-Kirschling, the retired teacher from New Jersey who is the first Baby Boomer to apply for Social Security retirement benefits. She is the first of an estimated 10,000 Boomers every day who will become eligible for benefits beginning in January. In light of this news, it seems like a good time to review the Social Security issue. The following discussion is taken, in part, from our latest book, ***econAmerica***.

One of President Bush's objectives during his second term has been to fix the Social Security "crisis." A key element of his proposed solution was to allow younger workers to withhold up to 25 percent of their FICA taxes and invest into individually owned retirement accounts. Younger people would then direct these funds over decades into stocks, bonds, mutual funds, and the like. This move would support his idea of an "ownership society."

I have not favored this solution. In a perfect world, it might make sense to have individual retirement accounts. It is not a perfect world.

Too Much Borrowing

One of the hard realities of the president's proposal was for the U.S. Treasury to borrow up to $2 trillion dollars over the next 10 years to "replace" tax revenue lost to the Social Security System with the creation of private accounts. These funds would no longer be available to pay current benefits. What you didn't hear about was the need for the U.S. Treasury to borrow an additional $3 trillion to offset the funding loss in the second 10-year period.

This is up to $5 trillion of additional borrowed money—additional debt. What this country doesn't need is $5 trillion in additional debt on top of the $9.5 trillion gross national debt already outstanding, especially when this suggestion does very little to fix Social Security.

The Social Security program is not broken. Pay-as-you-go funding will keep it in surplus for the next 10 to 15 years. The program can then tap into the "mythical" Social Security Trust Fund for the next 20 to 30 years. These projections are based on conservative assumptions about future U.S. economic growth and job creation. U.S. economic growth is likely to be stronger.

__econAmerica__ discusses four key factors, or Silver Bullets, that will combine to drive the American economy in coming years. Learn more at www.econAmerica.com.

Silver Bullet #2: NAP Time is Coming

This nation will reach a point in coming years when politicians are simply forced by the pressure of powerful financial markets and by constant media attention to set aside political rancor and work together to solve the entitlement funding and benefit issue. We refer to this as NAP (No Alternative Politics) time.

Neither party will be willing then or able to make such changes alone. Strong political leadership will see a bipartisan commission created, with required program changes debated in a civil environment. The full Congress will likely be asked to approve changes as proposed by the study group, with no ability to make modifications. Members of both major political parties will agree to avoid finger-pointing and accusations, recognizing that a cooperative effort is mandatory.

We have been at this point before and responded. We will do so again. We simply have no alternative. This issue is the second of four major developments, referred to as Silver Bullets, that drive my optimistic view of the American economy in coming years.

Tinkering Around the Edges

What the Social Security program requires is some "tinkering around the edges" to make the program financially viable for future generations when funding pressures are more painful. These changes will require bipartisan cooperation.

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$$ Adjustments

Nearly 50 million Social Security recipients, as well as more than seven million who receive Supplemental Security Income payments, will have a 2.3% cost-of-living adjustment in January, according to data released today by the Social Security Administration. The average benefit will rise to $1,079. Medicare premiums will rise 3.1% next year, the smallest increase in six years.

Nearly 12 million wage earners will pay higher Social Security taxes in 2008. The maximum amount of earnings subject to Social Security taxes will rise from $97,500 in 2007 to $102,000 in 2008. An estimated 164 million workers will pay Social Security taxes next year.

My parents both draw Social Security. I tell them they have nothing to worry about relative to Social Security viability in their lifetimes. As a Boomer, I will not draw full benefits until age 66. I tell my married kids that Social Security will be there for them, but not to plan on drawing it until they are 68, 69, or 70 years of age.

I favor proposals that stretch out the retirement age for younger people. This change reflects the reality that younger people will be able to work longer if they wish, will live longer and will, correspondingly, draw Social Security payments longer.

A minor change in the inflation calculation used to determine initial benefit payments for higher income earners is desirable. Such higher income workers would have their future payment schedule inflation-adjusted by the change in consumer prices. Lower income workers could continue to have initial payment levels inflation-adjusted by the average annual growth in wages, resulting in their getting a slightly better deal in the future than higher income workers.

I would suggest a slightly faster boost in wages subject to current taxation. For example, the annual adjustment to the wage cap might be the change in average wages plus an additional 1 percent each year during the next decade.

Providing greater incentives for people to save for retirement is advisable. Additional or expanded programs like the 401(k) would help minimize the role played by Social Security for millions of future retirees.

A Savings Incentive

I would favor other incentives to boost retirement savings of lower income families. If we are willing to go in debt another $5 trillion for the president's proposal, might we instead consider a two or three to one match for lower income people? For every $1,000 saved for retirement by lower income people, the government would match it with a $2,000 or $3,000 payment that would not be accessible until during retirement.

First of 78 Million

As noted, the first wave of 3.2 million Baby Boomers hits 62 in 2008, rendering them eligible to draw Social Security benefits. An estimated 51% of these Boomers will elect to draw benefits at age 62, allowing them to receive 75% of the benefits they would draw at their full-benefit age of 66.

An estimated 84 million people will draw Social Security in 2030, up from 50 million today. At that time, two workers will be paying into the system for each retiree. By comparison, that relationship today is three to one, and was 42 to one in 1945. The sooner modest changes can be implemented, the better.

Retirement and Benefits

Age at which workers can retire with full benefits for people born after 1943:

Year of birth	Full retirement age
1943-54	66
1955	66 and 2 months
1956	66 and 4 months
1957	66 and 6 months
1958	66 and 8 months
1959	66 and 10 months
1960 and later	67

Source: USA TODAY

Changes such as these are required to strengthen Social Security for generations to come. The inclusion of personal accounts would also make sense, but only as part of a comprehensive program.

"TEA"ser

People always feel optimistic after listening to me. They figure the next speaker can't possibly be as bad.

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