

Are the Trustees Assumptions Too Conservative?

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Projections Driven by Assumptions

- Chuck—Excellent presentation of projections made over about the past 20 years.
- In the relative near term---projections driven by economic assumptions.
- Mortality, fertility, and even immigration do not contribute much in first 10-20 years.

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Near Term Economic Assumptions

- Slow growth in employment and real earnings reduce payroll and taxes immediately, lowering benefits only with a delay.
- In fact a poor economy will if anything induce retirement.
- Thus, slowed economic growth hurts financial status for Social Security in the near term.

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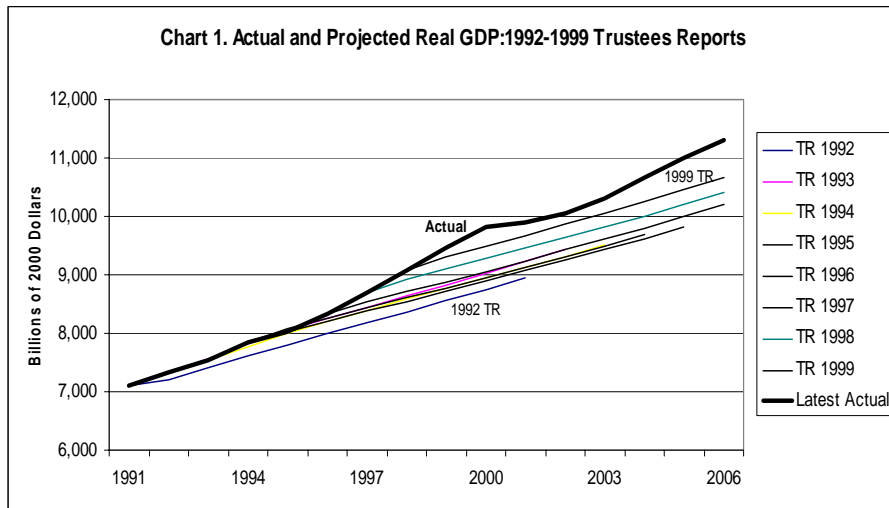
Trustees Assumptions Conservative?

- If the Trustees have been Conservative in the near term, they must have been underestimating real economic growth.
- Is this the case?

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1992 through 1999 Trustees Reports all under-projected Real GDP



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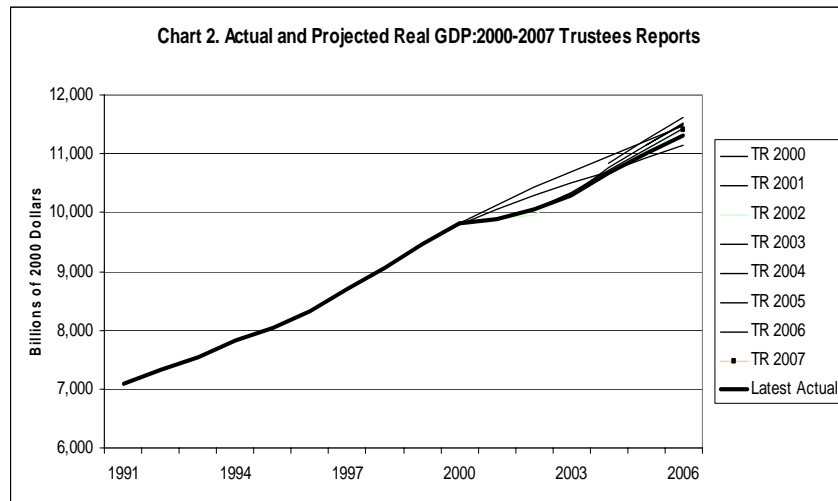
What Happened?

- The Trustees just missed the rapid acceleration in the “new economy” of 1995-2000.
- Projections gradually rose, accepting as permanent level shifts the unexpected growth each year.

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But since 1999, Trustees Reports have overestimated real GDP



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What happened this time?

- The Trustees assumed a little too much persistence of the “new economy”.
- Real GDP grew at 4% per year from 1995 to 2000.
- But grew at 0.8% in 2001 and 1.6% in 2002.
- Average growth around 3% per year since 2002.

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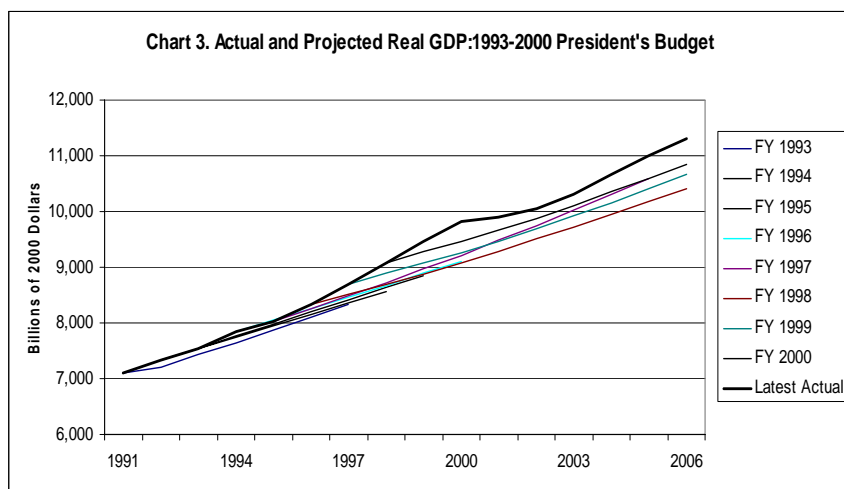
How have others done?

- GDP projections are also made for the President's Budget. And by the Congressional Budget Office.
- Did they err similarly?

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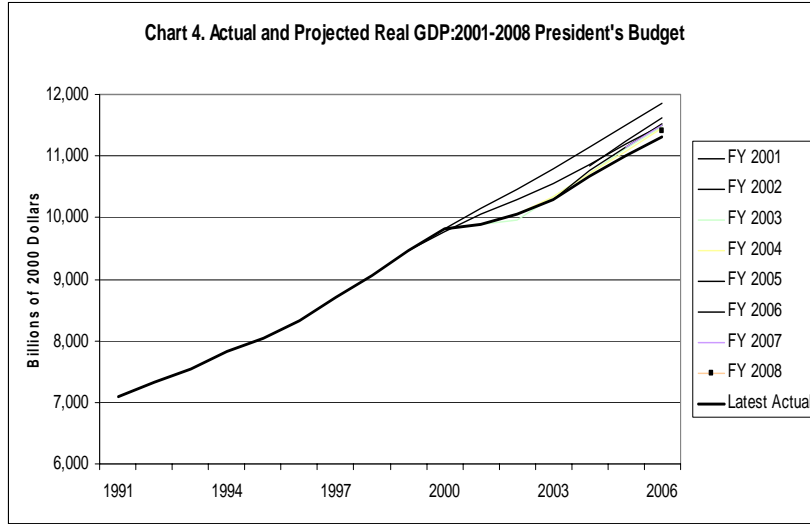
FY 1993 through FY 2000 Budgets also missed the 1995-2000 upturn



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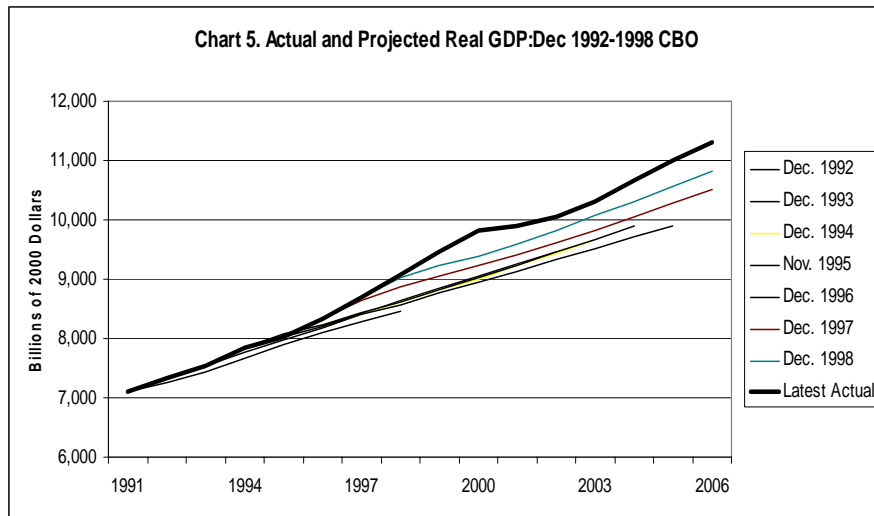
And have also overestimated since 2000



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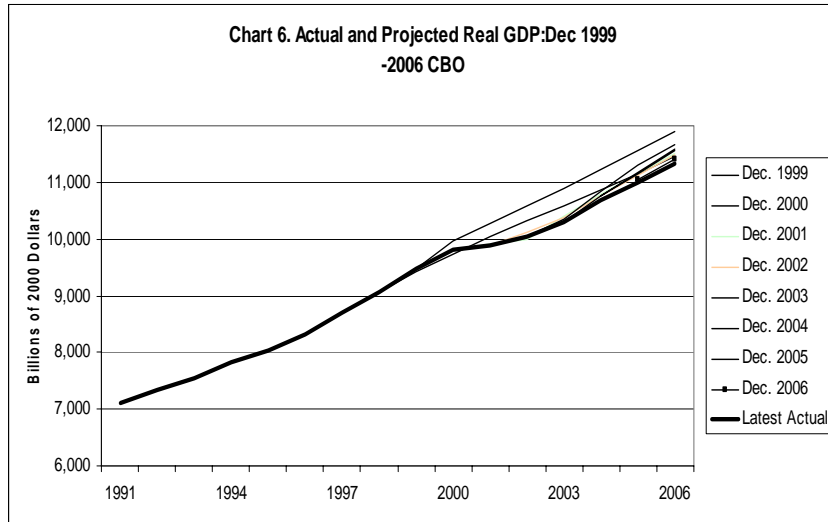
Likewise, CBO under-estimated in the early years of the new economy



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And like the Trustees and the Budget, CBO has overestimated since



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So are the Trustees Conservative in Near Term Projections?

- The record suggests no.
- Like others, the Trustees have proven to be unable to predict the timing of economic cycles.
- In fact there is no attempt to do so.
- Thus when a cycle slows the Trustees appear optimistic.
- And vice versa.

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How About in the Long Term?

- In the long term demographic assumptions are the dominant factor for financial status.
- Many suggest assumed mortality improvement is too slow.
- Some suggest birth rates are too high.
- If these assertions are valid then the Trustees are potentially underestimating future cost.

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How About in the Long Term?

- Long-term economic assumptions are debatable.
- The Trustees assume labor productivity will improve at an average 1.7 percent rate, as in the past.
- And that labor force participation rates will increase at middle and older ages as people live healthier and longer.

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