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Welcome to EOI. We use new tools for building the middle class. The Economic Opportunity Institute, based in Seattle, Washington, defines and details new public policies that address the bread-and-butter issues faced every day by middle- and low-income families. We build a bridge to economic security through research, policy, and media work.

Board of Trustees 2001 Report Shows Long Term Strength of Social Security

By Marilyn Watkins, Ph.D.

The Trustees of the Social Security Trust Fund issued their 2001 annual report on March 19, 2001 showing a system that is fundamentally healthy, and confirming that fears of a "Social Security crisis" are unfounded. The trustees project program costs and income a full 75 years into the future based on numerous assumptions about population trends and the economy. Under a pessimistic scenario of slow economic growth, the trustees project that with no program changes Social Security revenues will fund full promised benefits until 2038 and about 70% of benefits thereafter. Under a slightly more optimistic but still cautious scenario, the trustees project the system fully able to pay all promised benefits through 2075 and beyond, with no program changes. For 65 years, Social Security has provided a sure foundation of economic security for America's working families. This new report confirms that Social Security is in good shape to face the retirement of the baby boomers and continue providing insurance of a secure future income to all retirees, workers, and their family members.

The Social Security Trustees and Their Annual Reports

There are six trustees: the Secretaries of the Treasury, Labor, and Health and Human Services, the Commissioner of Social Security, and two members appointed by the President and confirmed by the Senate. As required by law, the trustees make 75-year projections of Social Security finances based on economic growth, wages, inflation, unemployment, fertility, lengthening life expectancy, immigration, and other factors. Because as the trustees state, "any estimation of the future is uncertain," they use three different sets of demographic and economic assumptions, creating three alternative projections.

In their 2001 report, for the "low-cost" alternative the trustees project long term economic growth at a little under the long term historical level and moderately longer life expectancies. These assumptions result in a prediction of full funding for Social Security through the entire 75 year period. For the "high-cost" alternative which forecasts the trust fund being exhausted in 2030, the trustees assume extremely slow rates of economic growth and much longer life spans. The middle projection uses assumptions between these two. This middle scenario projects full funding for at least 37 years to

2038.

In 1997, the trustees' mid-range projection predicted Social Security running short of funds in 2029. That date has been pushed back in each report since then, largely because of the strong productivity gains and thriving economy of the past five years. The 2000 report projected 2037 as the probable date when the trust fund would be spent down and payroll taxes and would not cover full benefits. Throughout the 1990s, the trustees low cost projection always forecast full funding through the entire 75 year period.

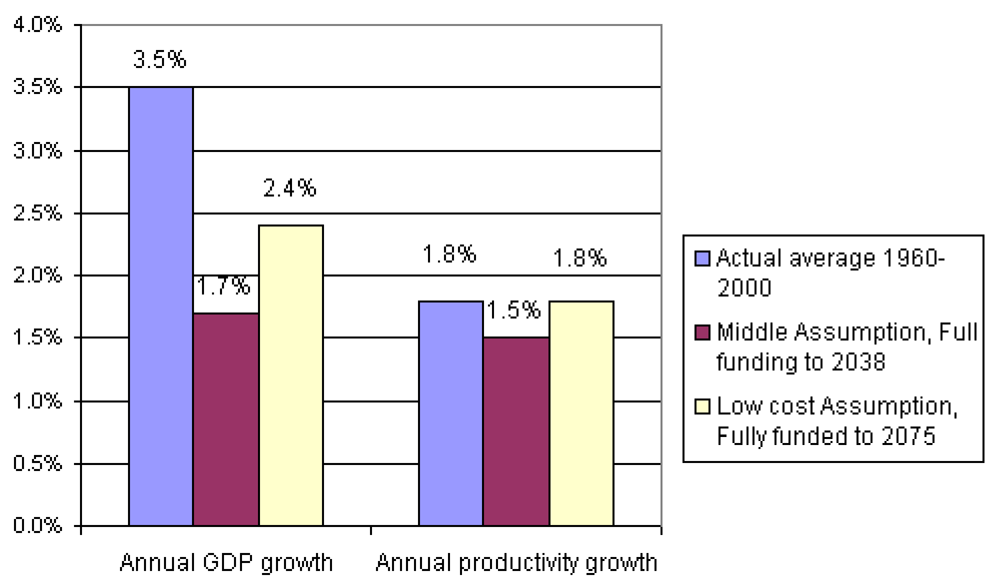
Changes Between the 2000 and 2001 Reports

The trustees have made a number of modest adjustments to their projections for the next ten years, based on the actual performance of the economy over the past year, but overall the assumptions in the 2000 and 2001 reports are very similar. In the long run for the mid-level projection, the trustees continue to predict that economic growth will fall sharply over the next decade and remain at 1.6% or 1.7% from 2020 through 2075, a lower rate of growth than our country has ever experienced for any prolonged period. Actual annual economic growth averaged over 3% during the entire 20th century, and in every decade since 1950.

Other economic assumptions remain largely unchanged between the two reports, with average annual productivity gains forecast to stabilize at 1.5% (the average for the past 5 years was 2.3%) and unemployment at 5.5% (currently at 4.2%). Demographic assumptions also stay pretty similar. In 2000, the trustees increased projected life expectancy for the year 2075 by about a full year over the 1999 report, to 81 years for men and 85.1 years for women. In 2001, the trustees scaled those life expectancies back by about one month, to 80.9 for men and 85 for women.

The low cost scenario, which shows Social Security fully funded indefinitely, assumes economic growth will average between 2.2% and 2.4% from 2020 through 2075, the same assumptions as in 2000. This scenario includes average annual productivity increases of 1.8% and unemployment at 4.5%, but somewhat shorter life expectancies, to age 77.4 for men and 81.7 for women in 2075. (Today's life expectancy is 73.8 years for men and 79.5 years for women.)

Key Economic Assumptions in the 2001 Social Security Trustees Report, and Actual Averages Since 1960



Although this year's report does raise slightly the projections for annual economic growth between

2001 and 2006, the trustees' forecast for the coming decade is still considerably below the growth level projected by the Congressional Budget Office (CBO). The trustees predict that annual growth will fall to 2% by 2006 and stay at about that level until 2015, when it will fall again. The CBO, on the other hand, whose projections are usually accepted by both political parties when setting the federal budget, projects annual growth at 3.1% between 2003 and 2011. If the trustees also accepted these shorter term forecasts, the financial health of Social Security would look even better.

What does the Trustees' report mean for the future of Social Security?

We can be confident in Social Security's future. Social Security is designed as a pay-as-you-go system, with today's workers paying current benefits. In 1983, Congress began preparing for the retirement of the baby boomers by raising payroll taxes a little higher than necessary for current benefits and building up the trust fund. The trust fund is invested in U.S. Treasury bonds, the safest investment in the world. In 2000 the trust fund earned 6.9% interest and contributed 11% of Social Security's income for the year. As the baby boomers retire, this large savings account will be spent down, but workers will continue to make new contributions each year.

The Social Security trustees have given us some possible scenarios of what Social Security finances might look like over the next 75 years, but as they point out, no one can predict the future. They suggest that economic growth will very likely slow over the long run, as fewer new workers enter the workforce. If future economic growth is half the rate of the past, then the trust fund will be depleted in 2038 and payroll taxes will only cover 73% of promised benefits. But even at that slow rate of growth the trustees also predict that because of productivity and wage growth, workers will actually earn 40% to 50% more after inflation in 2038 than they do today. Since Social Security benefits are based on earnings, benefits after inflation will also have increased substantially by then. That means that a retiree in 2039 who received only 73% of the predicted benefit would still get about 10% more in real income than the typical retiree does today.

If instead of slowing by half our economy only slows by one third, then even with the baby boomers all retired and everyone living longer, payroll taxes at the current 6.2% each for workers and employers will cover full anticipated benefits through the full 75 years.

Does Social Security need reforming?

Social Security is one of our country's most successful programs. Because of Social Security, poverty among our seniors has fallen to under 10%. While Social Security's retirement program gets the most attention, fully 30% of the programs beneficiaries are survivors of deceased workers, or disabled workers and their family members. All Social Security benefits are adjusted annually with inflation, and benefits for seniors continue as long as they live. Social Security is also administered extremely efficiently. In 2000, only 0.9% of expenditures went to administration, the rest to benefits.

As wonderful a program as Social Security is, there are modest reforms that would make it even better. Poverty and fear of poverty among seniors has fallen to the lowest level ever, but far too many still live in straightened circumstances. Adjusting benefit formulas to increase benefits for the lowest income earners and for elderly widows and widowers would be a significant improvement. Returning the retirement age to 65, rather than continuing the scheduled change to age 67, would also be a major relief for many workers, particularly those in physically demanding jobs. These changes could be easily funded by raising or completely eliminating the cap on taxable income. Currently, high income workers don't pay Social Security taxes on earnings over $80,400, meaning that the wealthiest Americans pay the least percentage of their income in Social Security taxes.

The 2001 report of the Social Security trustees confirms that the program as it exists is strong and healthy. There is no need for fundamental structural change. Any reforms we make to Social Security must recognize that it is a social insurance program. Everyone who works and contributes benefits and knows that they and their family are protected, whether they work for high wages or low wages, whether they are lucky or extraordinarily unlucky. We must retain these guarantees.

Note: The 2001 Annual Report of the Social Security Trustees, and annual reports from earlier years, can be viewed at the Social Security Administration web site, www.ssa.gov. Congressional Budget Office projections can be viewed at www.cbo.gov.

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