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Social Security for the Young

Scott Burn's Interview with Laurence Kotlikoff

Nearly five years ago MIT Press published "The Coming Generational Storm," a book I co-authored with economist Laurence J. Kotlikoff. We shared a deep foreboding about the implicit debt of our government and the burden it put on the young. We thought tough times were coming.

And they have.

But there is a silver lining--- if we are daring enough. Listen to this recent interview with professor Kotlikoff.

Kotlikoff: Our fears have been confirmed. The country has entered a great depression. Fortunately, the depression is mental, not economic. So far the nation has lost its mind, not its wealth.

What do you mean, the nation hasn't lost its wealth? House prices have fallen by one-fifth. The stock market is down two-fifths since last October!

Kotlikoff: Look around. You'll see the same equipment, factories, and office buildings we had a year ago. You'll also see the same people with the same skills available to work with these tools.

But the stock market drop has wiped out the savings of millions of Americans.

Kotlikoff: Yes, and that's horrible. But the economy's real wealth hasn't changed.

If total wealth hasn't changed and tens of millions are poorer, who's richer?

Kotlikoff: Current and prospective buyers of houses and stocks can now buy up these assets at deep discounts.

But this isn't fair-- the sellers are old and the buyers are young.

Kotlikoff: Nothing is fair in love or money. A generational storm was inevitable. Uncle Sam has spent decades transferring ever larger sums from the young to the old via Social Security, Medicare, and Medicaid. He's also been cutting taxes on wealth holders, who tend to be old, and raising them on workers, who tend to be young. Take dividend and payroll taxes. In 1950, the tax rate on dividends was 84 percent, while the FICA tax rate (employer plus employee) was 3 percent. Today, dividends are taxed at 15 percent, and the FICA rate is 15.3 percent.

So this financial crisis has leveled the generational playing field?

Kotlikoff: Right. The young still face huge tax bills to pay the boomers' retirement and health-care benefits. But the current financial mess has a silver lining. It will help the young face the coming fiscal mess.

But that's only if the young can earn and save enough money to buy up these low-priced assets.

Kotlikoff: Precisely. That's why the irrational pessimism, which has gripped the nation and much of the world, is so scary. It may lead to massive job layoffs. This would prevent our young from benefiting from this market-generated intergenerational transfer.

I see what you mean. But if the old are selling and the young can't buy, who gains?

Kotlikoff: The Chinese, Saudis, Russians, you name it. Cash is king. Anyone with a paycheck, a liquid bank account or, like China, \$1.9 trillion in foreign reserves can purchase America's homes and businesses at bargain-basement prices.

How can we ensure that our young obtain ownership?

Kotlikoff: No card-carrying economist is allowed to say this, but Uncle Sam should borrow the money that America's oldsters are too scared to keep in equities. Uncle Sam should invest it in the stock market on behalf of youngsters. If Roosevelt were alive, he'd call this Social Security for the Young.

Should Uncle Sam gamble in stocks?

Kotlikoff: He already owns 80 percent of AIG and some bank stocks. If the market continues to tank, Uncle Sam should effectively buy stock in the top 5,000 U.S. companies. He can do that by purchasing futures contracts on the Wilshire 5000 index and rolling them over through time.

Why future contracts?

Kotlikoff: The contracts confer ownership rights without voting rights. We don't want Uncle Sam micro-managing major companies.

Isn't this unprecedented?

Kotlikoff: Only in scale. By the way, Uncle Sam also holds stock, indirectly, via his claim to corporate income tax revenue.

When would you intervene?

Kotlikoff: The S&P 500 is down 42 percent from its peak. If it falls 75 percent, I'd intervene.

Who would oversee this investment?

Kotlikoff: An independent board. The board would buy stocks of all 5,000 of our leading companies with the proportions determined by the companies' total stock market valuations.

What if the market falls after Uncle Sam invests?

Kotlikoff: The government should invest for the long term. One dollar invested at the bottom in 1932 was worth more than \$6, after inflation, 20 years later. Twenty years is when the boomers will be mid-retirement.

That's pretty gutsy.

Kotlikoff: Sure is. But this would be a *buy up*--- not a bailout. It would provide what the country and the world needs -- an unequivocal statement of confidence by America's leaders in the American economy.

On the web:

Columns about the Coming Generational Storm:

[http://assetbuilder.com/tags/Medicare+ 2600 amp 3B00 +Generational+Storm/default.aspx](http://assetbuilder.com/tags/Medicare+2600_amp_3B00_+Generational+Storm/default.aspx)

The Coming Generational Storm on Amazon.com:

<http://www.amazon.com/Coming-Generational-Storm-Americas-Economic/dp/0262112868>

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