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Bush's Social Security Plan Assumes Much From Stocks

By *Jonathan Weisman and Ben White*

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To conclude that Social Security is careening toward a crisis in 2042, President Bush is relying on projections that an aging society will drag down economic growth. Yet his proposal to establish personal accounts is counting on strong investment gains in financial markets that would be coping with the same demographic head wind.

That seeming contradiction has become fodder for a heated debate among economists, who divide sharply between those who believe the stock market cannot meet the president's expectations and those who say investor demand from a faster-growing developing world will keep stock prices rising.

"If economic growth is slow enough that we've got a problem with Social Security, then we are also going to have problems with the stock market. It's as simple as that," said Douglas Fore, director of investment analytics for TIAA-CREF Investment Management Group. A spokeswoman said the company has not taken a position on the Social Security debate.

In the next two decades, as elderly populations swell throughout the developed world, retirees will begin withdrawing their savings, selling their financial holdings to raise cash and potentially glutting the world with stocks and bonds. Richard Jackson, director of the Center for Strategic and International Studies' global aging initiative, called it "the great depreciation scenario." Germany's Mannheim Research Institute for the Economics of Aging dubs it the "asset meltdown hypothesis."

That would not be an auspicious environment for young investors opening personal accounts to replace a portion of their traditional Social Security benefits.

"If there isn't an alternative source of demand for those assets, you're going to have a tremendous slowing of growth," said Jeremy J. Siegel, a University of Pennsylvania finance professor who just completed a book on the subject. "The only way to save the financial markets is very rapid growth in the developing world."

Compounding the problem of oversupply, economic growth -- predicted by the Social Security Administration to slow from a historical annual rate of 3.5 percent to a sluggish 1.9 percent -- would hit corporate profits and lower stock

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prices further, the theory goes. That would cause stock prices to drop, because they are priced as a multiple of a company's earnings.

The debate over future stock values has become so fierce that Bush's Council of Economic Advisers issued a statement to rebut its critics. It predicted that gains from the stock market, over the long term, will continue to be healthy.

"Although short-run movements in growth can affect stock market returns, there is no necessary connection between stock returns and economic growth in the long run," the White House said.

For workers choosing between private accounts and a traditional, defined Social Security benefit, the question would be important. Under Bush's proposal, for every dollar deposited in a personal account, a worker's traditional benefit -- delivered in a monthly Social Security check -- would be diminished by a dollar, plus the interest rate the money would have earned in Treasury bonds. To come out ahead of the traditional system, an account would have to realize returns on investment of at least 3 percent above the rate of inflation.

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Wednesday's Question:

What do the first three digits of a Social Security number stand for?

Place of Birth

Geographical Region

Date of Birth

Random Number

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