

CATO INSTITUTE BOOK FORUM

NEW CENTURY, NEW DEAL:
HOW TO TURN YOUR WAGES INTO WEALTH
THROUGH SOCIAL SECURITY CHOICE

Monday, October 30, 2000

Featuring:

Wade Dokken, the Author

The Cato Institute
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P R O C E E D I N G S

MR. TANNER: I want to thank you for coming out today, especially on such short notice. We don't usually put things together quite so quickly here, but we thought this was an important topic, especially with the election so close and this being such a major issue in the election.

My name is Michael Tanner. I am the Director of Health and Welfare Studies here at the Cato Institute. I am also the Director of Cato's Project on Social Security Privatization.

As I mentioned, this is a key issue in the election. It is one of those bright-line differences between George W. Bush and Al Gore. And it appears to be an issue on which they are going to campaign during the final days of this election. We are seeing ads running on it and we are seeing telephone calls made, and we are seeing all sorts of issues dredged up on Social Security.

In fact, right now, I understand, in Florida, there is a telephone war between Ed Asner, who is telling people that George Bush's plan to partially privatize Social Security will leave old people eating cat food, and Norman Schwartzkopf, who is telling them not to worry, everything will be fine. I am tempted

to ask what either Ed Asner or Norman Schwartzkopf knows about Social Security, but I will leave that to others.

That said we are actually fortunate to have someone here today who does know something about Social Security. Wade Dokken is best known probably on Wall Street as President and CEO of American Scandia.

But he is also the author of this new book, "New Century, New Deal: How to Turn Your Wages into Wealth Through Security Choice," which I think is one of the best books at making the argument for Social Security privatization in a simple and readable way, and something I do urge all of you to read. We will have books available afterwards out there, and Wade will be happy to sign them for you.

Wade also comes to this from an interesting perspective of being a life-long Democrat, being a supporter of the Clinton administration. In fact, I can remember you telling me, Wade, about the picture you have of you and Hillary Clinton.

MR. DOKKEN: Would you like one?

(Laughter.)

MR. TANNER: Only for my dart board.

(Laughter.)

MR. TANNER: But at any rate, it makes for a very interesting perspective on such an issue that so divides the parties and has caused Wade to cross party lines on this issue.

We are really pleased to have him here. He is not only an author and an expert on the issue, he is a supporter of the Cato Project on Social Security Privatization and an advisor to that project, who has certainly been of great assistance to me. We are just thrilled to have you here today. Tell us a little bit about your book and yourself and the issue.

Wade Dokken.

(Applause.)

WADE DOKKEN, AUTHOR,

"NEW CENTURY, NEW DEAL:

HOW TO TURN YOUR WAGES INTO WEALTH

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MR. DOKKEN: Thank you, Michael.

For those of you who have been with Cato or followed this for some time, who would have thought here today you have on the front page of Investors Business Daily a major article arguing for the privatization of Social Security and, on the same day, in the Wall Street Journal, you have a series of articles communicating that the battle is pitched on this issue more than any other, and, at the same time, talking about how in all these other major countries around the world that this is becoming a

defining element of the public policy agenda? I mean, who would have thought that?

I bring a perspective to that. I represent a company, which is not a large brand name to anybody here, which is in many respects one of the leading providers of private pensions around the world. So, we witness this.

We are in Poland as they privatize. We are in Sweden as they privatize this very day. We are in Chile, with the first set of U.S. mutual funds to be sanctioned under Chilean law. And we are in France and Germany and every other country that is a headline, facing demographic shifts that the pay-as-you-go systems are causing.

But it is today that we are here. And, unfortunately, on this one issue, the United States is bringing up the rear. Having said that, the stage has been set. The stage has been set thanks to Cato, thanks to Steve Forbes, thanks to some people from my own party, Moynihan, Kerry, Breaux, Stenholm.

But the stage today and the debate today and the fact that it is at prominence, and the fact that somebody is going to win a mandate over this, to that, I think I and everybody here owes a debt of gratitude to Governor George Bush. There was a great deal of courage required back in May, when Governor Bush decided to endorse private accounts. That was step one.

But, fundamentally, the more important step he made was in the first debate. When he took this complex, fear-fraught issue and stated it as his gift, it is really a choice between less than 2 percent or 8 percent or 10 percent. Using some of the gift that Reagan first taught us, he showed the difference between fear and optimism.

I think that simple statement and that decision, which I don't believe that we had seen prior to that stage in the campaign, that decision on that day in that debate to make this a core of the remaining days of his campaign, in my opinion, it is going to be one of the core kernels of why he is likely to win this election. And that should not surprise us. He is not alone.

This country has been fundamentally reshaped since 1980. In the area of pensions and investments, the reshaping is at its core. Now, what is that reshaping? In 1980, three years before I entered the business of investments, only 10 percent of Americans owned mutual funds, a very small number. Slightly more than that was the percentage of American households' net worth in equities. And the foundation of people's pensions, outside of Social Security, was often a defined benefit plan paid for by a corporation.

Now the world has changed. The interest rates of those first few years really destroyed that corporate-defined benefit

plan. What sprang from that was defined contribution plans. Which is, in simple matter, companies putting small amounts of money every month in individual accounts, in 401(k)'s, 403(b)'s, and 457 plans. Plus, we have had over two decades in the growth of IRA's. So we find ourselves here, in the first election pitched on the issue of Social Security, probably since the 1982 or 1984 Congressional election, we find ourselves with a sea change in terms of the body politic. The body politic does not fear owning their own investments.

When you look at every way you can track this, the number of ads, the number of publications, the number of TV shows, in every way imaginable, this is a nation that has come to understand that individual responsibility and individual control over their investments is a part of their responsibility to themselves. This is what Social Security choice is all about. It is not something to fear. It is not something that people will end up destitute on.

They know that, because people are going to make wise decisions with their own money. Some may choose to stay within the Social Security system as it is today. Some may choose to go into bank systems that offer a 6 percent rate of return, which is a stark contrast to the pay-as-you-go returns that I just talked about.

That is why this is not gaining the traction, I believe, in the election. And that is why, as a Democrat, I feel extremely comfortable coming out against the nominee of our party, Vice President Gore, on this issue.

Sadly, sadly, I think this is electoral posturing. I think many of us would agree that, had things run their course two years ago, we might have had substantial movement on this issue toward private accounts, bipartisan movement. That bipartisan movement might have even involved the Vice President himself. Most believe it would have involved Senator Lieberman.

Private conversations I have had with several Democratic Senators who have not publicly come out for choice suggest that they are ready to come out for choice. This is no longer a scary issue. Every one of these people, as well as the people in this audience, has participated in the markets and they understand the power of the markets.

One of the most frequent conversations that comes up in the radio interviews and the conversations is this conflict between changing from a pay-as-you-go system to a funded system. This is also something not to fear.

We are a relatively wealthy country. We are a country who finds that wealth at an opportune time. And there is a chance for us to preserve the promises to people that have already been made, to fund those promises, and, more important,

to fulfill the aspirations of other generations of Americans, aspirations that these intelligent people know, intuitively and intellectually, cannot be fulfilled by the system we have today.

Now, as I stand here, I think this is an extraordinary moment. This is not a system -- and I defend Social Security -- one of the anecdotes I tell is, in 1956, my grandfather died at the age of 56. He had 13 children, five of whom were still under age seven. If it had not been for the various insurance provisions of Social Security, that would have been a very different life for my grandmother, my mother, my uncles and my aunts.

I think the income redistribution part of Social Security has been very healthy. I think it has been a big part of eradicating the poverty of old age. So, in that respect, I differ from some people. But, in that respect, I think is what gives my message credibility.

Democrats should not fear this. The wage earners and union members will be the biggest benefits beneficiaries of this. In the book I give one small little example, and I think it is worth repeating. A 25-year-old person today, given the chance to earn an average income of \$32,000, given the chance to put about two-thirds of their Social Security taxes in a private account and earning 6 percent, historically, a very low amount of money, that 6 percent would grow to be \$1.2 million. That would produce

a multiple of the benefits that they would receive under Social Security.

This is not something to fear. This is something the Democrats should embrace. Because it is exactly their constituencies, whether those are the constituencies of the labor unions, whether it is the constituencies of African-Americans, it is their constituencies who I believe will benefit more greatly than anybody else.

There is also something that we should talk about, which is the issue of government control. I believe choice, which was inevitably going to lead to privatization in some respect, is a very healthy thing for this country. I think the amount of capital formation that will occur real savings as opposed to the savings of the current Social Security system is one that will allow this country to grow at the rate that we have grown for the last two decades.

We do ultimately need to generate our own savings pool. We cannot forever be dependent upon the savings pools of other countries. I believe that is another very significant benefit of Social Security choice.

Now, my role in this debate is really to follow on the really extraordinary work of others. I see my role as a populizer. I see my role as somebody who takes one small idea and does my role in making this broadcast widely. We have

already sold over 30,000 books, which, relative to Social Security book-buying, is a pretty big number.

We work with every major brokerage firm in the United States and we work with most of the major money management companies in the United States. I suspect that the message in this book will be sent out in millions of statements to investors all around the United States in the next three to six months.

This is an idea whose time has come. This is an idea whose message bearer is there in Governor Bush. And I hope to add to this debate and I hope that my work and the work of Cato and the work of so many others can bring this to a successful conclusion in the next legislative session.

So, that is why I am here. I thank you for giving me the time. I feel privileged to speak on this subject at Cato. And I guess I will open up for some questions, Mike.

(Applause.)

MR. TANNER: We will take a couple of questions.

MS. PLANT: Hi. I am Christine Plante [sp] from the Cato Institute.

I was just wondering what your thoughts are on Senator Lieberman's apparent flip-flop on this issue.

MR. DOKKEN: The Vice President serves at the President's wish. This is not new. It is true in a corporation; it is true in our Federal system. This is not the first time a

vice presidential nominee has had to chew on some words and enjoy the taste the second time around. It is unfortunate, however. Again, I am a Democrat. And as a Wall Street Democrat, I have applauded the movement toward the center of the party. I have applauded the embracing of reducing deficits. I have applauded the constraints on government. I have applauded in particular free trade.

So, I hope Gore's movement to the left is not a movement of the party to the left. I hope this is not a throttling of the voices, like Breaux, Kerry and Lieberman, because that would be tragic for my party. And it would mean the exodus of many people. It would probably mean the exodus of myself and it would probably mean the exodus of a generation of people. So, from that perspective, I think it would be really sad.

MR. TANNER: Mr. Moore?

MR. MOORE: Congratulations on a terrific book. I read it last week and I just want to applaud you absolutely for it. When I talk to some of your friends in the financial industry, some of these millions of people that hopefully you will be getting the word out to, I hear more and more this concern that the market is at a high, that this is a bubble economy, and why would we want to put all this money into private accounts in the stock market now that it looks like the market is on a level or

maybe even will fall. And I am sure you have confronted that argument many times yourself. How do you deal with it as someone in that industry?

MR. DOKKEN: I think there are three very important points to make. First of all, making the statement, "Social Security choice," is not the same thing as making the statement that 100 percent of somebody's money has to go into equities. This is about choice.

People will choose bank accounts. People will choose money market accounts. They will choose bank CD's. They may choose U.S. Government bonds, and, yes, they make choose stocks, stock mutual funds. I don't believe that we will allow individual stocks, but I am not going to get down to that line. I think there are a couple of other more important points to make.

As you know, a pay-as-you-go system truly doesn't even have a rate of return. In a static population, static inflation, static longevity, you would have a dollar that you paid in today would be exactly one dollar 40 or 50 years from now. So a pay-as-you-go system truly doesn't have a rate of return. And that rate of return, if you would express it, would be precisely zero. Because of tax issues and other issues, it has been modestly above that.

But because it has been modestly above that, let's just take that rate of return. Today, this audience can expect a rate of return of a little bit less than 2 percent. Some members of the audience can expect a rate of return significantly less.

Dr. Jeremy Siegel, from Wharton, did a fantastic study. And I know Jeremy well and I have been privileged to be part of his research. In the last 200 years, take every 20-year period, and the worst 20-year period gives you a rate of return modestly above Social Security -- the worst 20-year period. So, if you chose to put all your money in stocks, which nobody is going to suggest, and you accidentally were in exactly the worst period, you would have exactly the same rate of return as Social Security. But, having said that, of course, people don't make 20-year decisions about retirement. Retirement for a 20-year-old is really 50, 60 or 70 years.

So, when you look at that rate of return, 60 or 70 years, you are talking about a rate of return that is about 6.6 percent after inflation. So it is going to compound at a profoundly higher rate of return than anything in Social Security.

And retirement is not a cliff. People don't reach retirement and take all their money out. That is just one more day in an investing cycle. So I don't think that the risk is

really in allowing people to participate in the equity markets. I think the real risk is in not allowing them to.

Thanks, Steve.

MR. TANNER: Anyone else? Andrew?

MR. BIGGS: I am Andrew Biggs, from the Cato Institute.

This is following on a little bit from your first answer. The recent ads run by Vice President Gore and the Democratic Party have essentially been saying that even a modest privatization plan like Governor Bush's would cut benefits for present retirees. Given the ratcheting up of the rhetoric on these types of ads, do you think it is going to be possible for Democratic members of Congress and the Senate to come around to something, to a modest privatization, after the election, or do you think that they have taken the rhetoric to such a level it is impossible for them to backtrack at this point?

MR. DOKKEN: Well, I have never seen a significant policy issue that a politician can't backtrack on.

(Laughter.)

MR. DOKKEN: So I have great confidence in their ability to reverse a trend. But let's just talk about that.

In the first debate, Gore made the statement that every dollar taken out would be a dollar out of somebody's pocket. That is an obvious lie. Now, the policy challenge we face is if we privatize we also have to fund the liability. That is an

honest policy issue. Gore receives zero points for this because his plan is really swapping debt for debt. So, he hasn't tackled this problem in any way.

Obviously, a commission is going to have to fund that. Private accounts address a long-term issue. The short-term issue is still something we are going to have to deal with. That is, after 2015, if we create private accounts, we exacerbate the cash flow issues. And we are going to have to address that. I don't know how we are going to address it.

Are we going to address it with the general account today? Are we going to do that? Are we going to have a temporary increase in the Social Security tax? I don't like that, but that is an option. Are we going to cut benefits? Another option I personally don't like.

We have to address these issues. But funding that future liability, that is a problem that is an indictment of Social Security as it has been created and as it has been managed. It is not an indictment to private accounts and it is not really related.

MR. TANNER: We have a couple more, one there and one in the back.

MS. BOKAR: Hi, I'm Kelly Bokar, ConservativeHQ.com.

Are there any other areas in which you disagree with Al Gore, and have you gotten any flack from your Democratic friends for releasing a book this close to a close election?

MR. DOKKEN: I don't know whether it is releasing the book, if it's the radio shows, the editorials, I don't know which part irritates my friends the most. But I do have this friend in Florida who calls and leaves these really long, nasty voice-mails.

Other issues? Let me take two sides of that. I am a hunter who favors gun control. I am an outdoorsman who favors a lot of Gore's positions on the environment. Having said that, I will admit, his rhetoric and his campaign makes me, and I am sure it makes a lot of people in my position, really uncomfortable.

What is the rhetoric I am talking about? It is back to the rhetoric of class warfare and fear. Optimism is a great thing. Clinton, for all his foibles, has followed in the optimistic tradition of Reagan. That is a lot easier to get around that flag and that is a lot easier to motivate people.

Unfortunately, Gore has, through some calculus of his own weaknesses or the election, has chosen to create this imagery, which really pits people against each other. If you saw -- and I don't know where I just read this -- union membership now is at the lowest point it has been since 1900. So

this is not a country that is going to be motivated by fear today.

This is a country that, I think, is going to be motivated by how do we create more opportunity, and the kind of opportunity that has been created relatively consistently since 1980. And I think he has made a big mistake, because the language is clearly the language of class warfare. It is the language of a significant increase in government. His 10-year plan doesn't speak to it, but his language does. And which one is the real Al Gore?

MR. TANNER: We have time for two more questions.

MR. CHILERAS: My name is Phil Chileras [sp].

I am a recent retiree, so I am facing some of the problems. One problem that I noticed is the problem of the number of options that you have for the payout of any kind of privatized plan. I am using a model like the TIAA-CREF, which university professors have. And my brother, who is recently thinking of retirement now, is a full professor at NYU, in mathematics, and he is looking at the number of options they have. It is like 30 different ways, a matrix of whether you go with inflation-adjusted payout or what you leave to your beneficiaries after five, 10 or 15 years, the percentage that could be left to your beneficiaries. It is a real bucket of worms.

Has your book dealt with this and the cost of having to deal with 280 million people, with that number of very difficult decisions in terms of payout?

MR. DOKKEN: Well, you really have two questions. I will try to briefly touch on both. The first question is choice and confusion and complexity. That is a difficult question to answer because, with opportunity, comes this responsibility. It is not free. Choice accounts are not going to remain a teaspoon from the bowl of Pablum to the mouth. That is the beautiful thing about it. And those choices are almost all in your benefit.

And in the particular choice that you are talking about, one of the things that just excites me is that in those choices will be a choice not only for a lifetime income, which you have under Social Security, but almost certainly a lifetime income with a property result for your heirs.

So, in some mix of mortality statistics, either your spouse or your children will have part of that inheritance, something that they don't get in Social Security today. So, yes, okay, there is some confusion with that. There will probably be a whole industry to help with that confusion.

And for the record, it may not be an industry that involves companies like mine. You will have different solutions. You may have something just like the Federal Thrift Savings Plan,

which is a matter of a few basis points. You may have something like TIAA-CREF, which is also a matter of a few basis points.

People will have the right to choose what level of service, what level of sophistication and what level of price. That is the world that I would imagine.

As it relates to your second question, which is a cost question, I think I will try to answer that in the same level of choice. There will probably be some very simple choices that will have very simple costs, and that will be great and people can freely choose those. It might look a lot like the stakeholders pension system that is in England today.

Alternatively, there will be more sophisticated solutions at a higher price than other people may want and desire, and people will have the right to choose that which is most appropriate to them.

MR. TANNER: Last question down here.

MR. ROSENBERG: I am Joel Rosenberg, November Communications.

You referenced two things that I wanted to briefly follow up. One is you talked about the sea change politically and the whole rise of the new investor class. I want you to talk a little bit more about the perceptions of Wall Street being what Main Street can look to for their financial future versus looking

to Washington and how that is changing and how that will affect this debate.

Also, you mentioned a little bit about what your company is doing in Social Security privatization in other countries and what kind of lessons we might be able to draw out of what you are seeing with your company in terms of what may be coming over the horizon for us.

MR. DOKKEN: Let me start with the second one first. It is actually somewhat humorous to see how agonizing this issue is here in capitalist United States whereas how little agony has gone into it in Poland or Sweden. I mean, it is really humorous. And even in Germany, Germany is going to have something. They have something that is partially there today. And they are going to have a major plan, clearly. But Sweden, my company's name is Scandia; we are the number one provider of a type of product called unit linked, which in the United States is called variable annuities. This is the largest private pension product of insurance companies, and we are the largest.

In every one of these markets we are either one, two, three, four, or five. And it really has come down to a whole series of choices. People are given, in many cases, a government option, and they almost all go to a private option. It is almost humorous how painful this debate is here when we have the money

and we have the sophistication and it should be the simplest conversation here. That is something I find interesting.

What was your first question?

MR. ROSENBERG: The investor class, and Main Street looking to Wall Street.

MR. DOKKEN: In my parents' generation, they were of a little different experience than so many people. Neither of my parents had a corporate pension. So, when IRA's came on, I can remember as a child how important it was, and they started investing in it, and it was all banks. Then I became a stockbroker. And at the point I became a stockbroker, my father wanted to move from banks to the markets. Over the last 20 years, I don't know how many times I have thought, you know what? It's a bear market, back to Steve's point, it is a bear market, this is a bear market.

My father never budged. He never budged. So, my father, with his very small savings, has seen those savings increase probably somewhere around -- let me think this through quickly -- around 10 times, because he came in at somewhere around 1,000, or a little bit over 1,000, in the Dow-Jones. So his savings have increased approximately 10 times.

Well, that history mirrors many, many other people in this country. And when that kind of wealth is created, because our economy is growing at the rate it is growing and profits are

growing at the rate they have grown, people aren't looking to Washington as a solution. They are looking to their own management of their own portfolios, and I think that we are going to see that in this election. This is not turning as clearly as Vice President Gore would have thought.

People are fundamentally more self-directed today than they were 20 years ago. I think that has profound implications, and that is a kind of good libertarian thing, don't you think?

MR. TANNER: Absolutely.

MR. DOKKEN: I think that is it, and I thank everybody. Thank you, Michael.

(Applause.)

MR. TANNER: Thank you, Wade. We very much appreciate it. I think what you have said today is an indication of how many thoughtful Democrats are coming to this issue, from my good friend Tim Penny, who has been working with the Cato Project for a long time, people like Pat Moynihan and Bob Kerry and Charlie Stenholm. We have identified somewhere around a dozen candidates for Congress who are Democrats who are running on a pro-privatization platform. So, certainly that is an issue now in some wings of the Democratic Party, and we certainly hope you will continue to speak out and push your party in that direction.

For everyone else, we have some copies of Wade's book here. If you would like to buy them, they are right outside. I am sure Wade would be happy to sign them for you.

Other than that, lunch is upstairs. Thank you all very much.

(Applause.)

(Whereupon, the Book Forum was concluded.)