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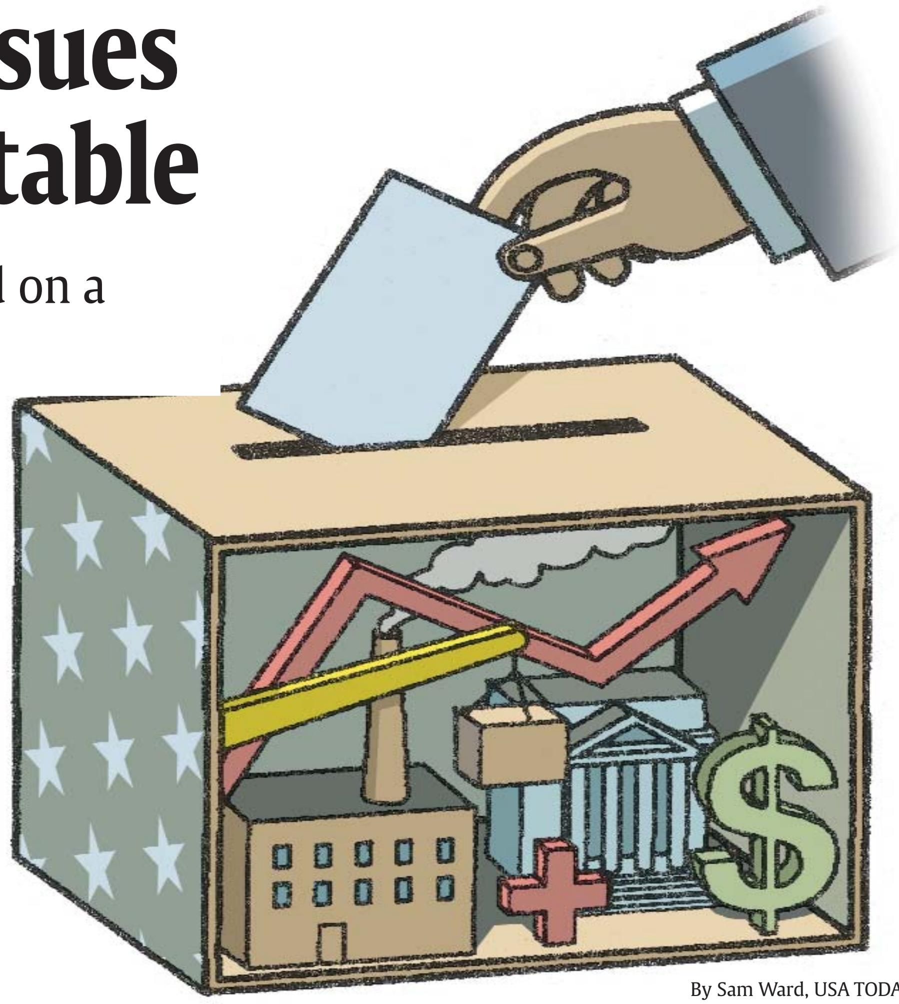
Economic issues on election table

Where Bush, Kerry stand on a number of fiscal points



By Sam Ward, USA TODAY

By Sue Kirchhoff
USA TODAY

WASHINGTON — This presidential election will affect the economy for a lot longer than the next four years.

For starters, it could determine whether Robert Rubin or Martin Feldstein will be a top candidate to replace Alan Greenspan, who is expected to retire as chairman of the Federal Reserve in 2006.

It will determine the stance of U.S. negotiators as they try to wrap up a new round of World Trade Organization (WTO) talks that could, among other things, make historic changes in agriculture policy. It will shape tax policy for both consumers and businesses.

And though Iraq, oil prices and short-term economic concerns are the focus of the campaign now, the next president could end up spending much of his time dealing with a looming issue that has been largely shunted aside: enormous future deficits, including Social Security and Medicare.

This election could also affect workers in direct ways, including how many qualify for overtime pay, what the minimum wage will be and how the nation deals with a looming pension fund shortfall.

President Bush and Democratic

presidential nominee Sen. John Kerry will likely face questions on these issues and more tonight at Arizona State University in Tempe in a debate that will focus on economic and domestic policy.

While some economists say the choice between Bush and Kerry could be a wash in terms of short-term growth and job creation, they generally agree the actions either one takes on longer-term issues, particularly Social Security, Medicare and the record trade deficit, will have lingering repercussions.

"Fiscal policy has become very important," says Jim Steiner, managing principal of Lowry Hill, a wealth management firm that handles $5 billion in assets for affluent clients. "I don't know that (the economy) can grow fast enough to fund all the commitments that we have made."

In general, Bush advocates continued tax cuts and open trade as the means to prosperity. While he has talked of creating private accounts under Social Security, he has not come out with a detailed plan. Kerry has taken a slightly tougher stance on budget issues, promising to reinstate rules that require offsetting cuts for new spending or tax reductions. Kerry would spend more on health care than Bush and eliminate some of the president's tax cuts.

Over the longer term, National Association for Business Economics (NABE) members at a recent conference said the next president would play a major role by appointing a new Fed chairman and grappling with budget issues.

Greenspan's successor:

How do you replace an icon?

Greenspan, who has been chairman of the Fed since August 1987, is expected to step down when his current 14-year term on the board expires in February 2006.

Nariman Behravesh, chief economist at Global Insight, says the departure of Greenspan, one of the most acclaimed chairmen in Fed history, could prompt the bond market to refocus on fiscal issues, possibly creating jitters about long-term federal deficits. So far, bond traders have kept interest rates low despite rising deficits.

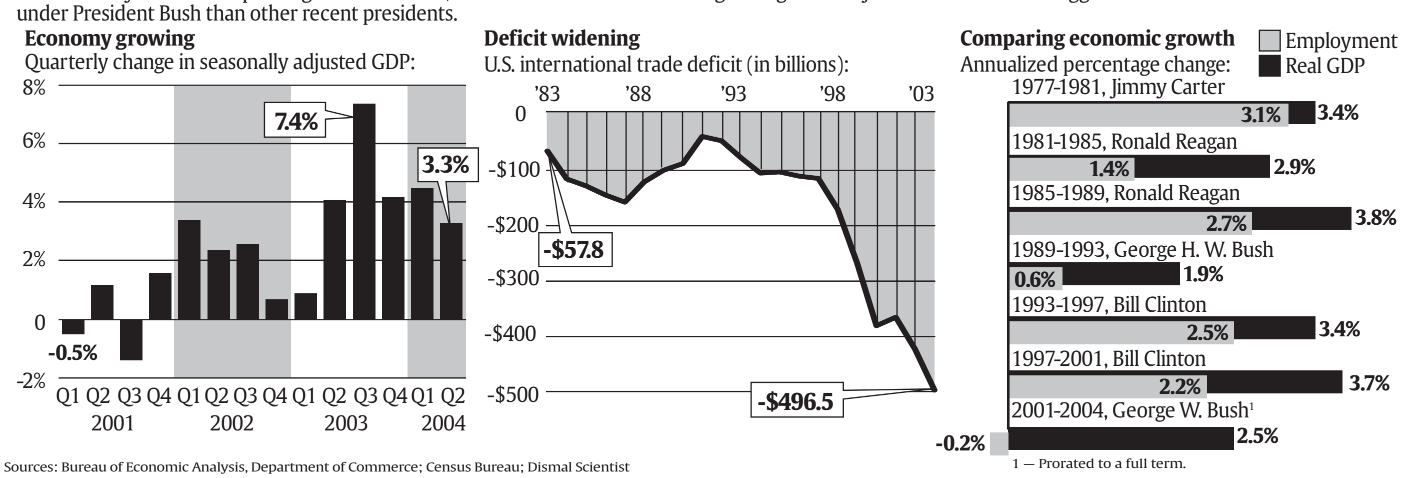
But partly because of changes Greenspan helped bring to the Fed, the central bank today is much more politically independent, Fed members are unified behind the goal of keeping inflation low, and the caliber of Fed governors and regional bank presidents is high.

"Short term, it's a huge deal. Long term, it's not much, because whoever replaces (Greenspan) is going to say, 'I think he was great, and we're going to do everything he did,' " says Milton Ezrati, chief economist at Lord Abbett, a mutual fund firm.

Economists are musing about possible replacements. If Bush wins, speculation centers on R. Glenn Hubbard, a former chairman of Bush's Council of Economic Advisers. Feldstein, a noted Harvard economist, is another oft-mentioned name, along with John Taylor, a Stanford professor and Bush Treasury official.

The election and the economy

The economy has been expanding since late 2001, but the trade deficit has been growing and the job market has been sluggish. Growth has been less robust under President Bush than other recent presidents.



Sources: Bureau of Economic Analysis, Department of Commerce; Census Bureau; Dismal Scientist

By Robert W. Ahrens, USA TODAY

If Kerry wins, early betting is on former Clinton Treasury secretary Rubin, now an executive at Citigroup. Lawrence Summers, another former Treasury secretary who is president of Harvard, has been mentioned, as have Fed governors Ben Bernanke and Donald Kohn.

Soaring deficits:

Red ink will be a defining issue in coming years.

When Bush took office, the Congressional Budget Office projected a 10-year $5.6 trillion surplus. CBO now predicts more than $2 trillion of red ink from 2005-2014. The deficit for fiscal 2004, which ended Sept. 30, was $415 billion.

Both Bush and Kerry have promised to cut the deficit in half within five years. But both have expensive plans that could make it hard to achieve that goal. Kerry wants to expand health insurance. Bush has vowed to make his tax cuts permanent and talked of creating private accounts under Social Security, which would involve huge upfront costs.

And there are other costs, including the war in Iraq and fixing the alternative minimum tax. The AMT was designed to ensure high-income households paid at least some income tax, but it is increasingly affecting other taxpayers.

Behravesh, in an analysis of the Bush and Kerry plans, predicts neither candidate will meet the goal of halving the deficit, with Kerry showing slightly more red ink. He expects economic and job growth under either man to be virtually the same, with the economy expanding at an average 2.9% annual pace and the number of U.S. jobs reaching an average of 146 million by 2014.

Some economists aren't overly worried about the short term. The CBO predicts the annual deficit will shrink to about $300 billion in 2009. But analysts warn that the economy cannot simply grow out of deficits as it did in the 1990s. The reason: The pending retirement of the baby boomers. Social Security and Medicare, now 7% of the economy, could rise to 12.1% by 2040. Greenspan has warned that without action the USA faces rising long-term interest rates and slower growth in living standards.

"If we want to live these years leading up to the boomers' retirement on credit cards, we can do it, and it won't lead to an immediate crisis," says Robert Bixby, director of the Concord Coalition, a budget watchdog group. But he calls it irresponsible.

"If we keep running big deficits like this, we could have serious problems sometime within the next 10 years, or even earlier, because we're borrowing so much from abroad," Bixby says.

Bob Doll, president and chief investment officer of Merrill Lynch Investment Managers, says a Kerry presidency would likely boost bonds, given that Kerry has proposed somewhat tougher budget rules, such as requiring that new tax cuts and spending programs be paid for by offsetting cuts. A Bush victory would be better for stocks, given Bush's record of cutting capital gains and dividend taxes.

Doll also says Bush would will have better luck getting his program through a closely divided Congress. Republicans are a majority in Congress, though Democrats say they could win the Senate in November.

Brian Wesbury, chief economist at Chicago investment banking firm Griffin Kubik Stephens & Thompson, is skeptical of such arguments. "Bush did not win the popular vote (in 2000) and yet still got two major tax cuts through."

Tom Welsh — CEO of Minneapolis-based Seelye Craftsmen, a 90-employee firm that fabricates stainless steel products — favors Bush's plan to extend his tax cuts, including permanent repeal of the estate tax. Richard Kogan, budget analyst for the Center on Budget and Policy Priorities, a liberal think tank, says Bush's plan is tilted toward tax cuts for the wealthy.

Trade:

Trade is once again center stage.

The United States is a central player in WTO talks aimed at a sweeping global trade pact. The fitful negotiations are intended to produce a deal that cuts tariffs, wipes out barriers to services such as banking and insurance and eliminates most farm subsidies. U.S. farmers, who get 18% of their income from government payments, are watching the talks nervously.

The negotiations are coming amid voter concerns about outsourcing jobs overseas and a record trade deficit.

The current account deficit, the broadest measure of trade including investment and goods, hit $550 billion in 2003 — equal to 5% of the overall economy. If foreign investors who are financing much of the deficit pull out, it could mean higher interest rates, a lower dollar and lower stock prics.

"The biggest thing I would worry about are the twin deficits (budget and trade) and trade policies, because they affect the economy so much," says Frank Riddick, CEO of Cincinnati-based Formica. Riddick sees the economy at a turning point, with U.S. firms pressured by global competition. He says there is a "fear and uncertainty factor" among business leaders because "a lot of the major issues that we have aren't being addressed adequately."

Over time, high trade deficits have been associated with efforts at protectionism that some economists warn could stifle capital flows, making the problem worse.

Kerry has promised to curtail tax incentives for moving jobs overseas, incorporate labor and environmental standards in new trade pacts and investigate labor practices in China, which has a record trade surplus with the USA.

The Bush campaign boasts that the president filed the first-ever WTO action against China regarding discrimination against U.S. high-tech exports. And the administration will send Congress a free trade deal with Central America.

Other issues:

Aside from shoring up Social Security, the next administration could have to spend some time bolstering the private pension system. The Pension Benefit Guaranty Corp., which insures traditional pensions, ran an $11.2 billion deficit last year and is expected to post a bigger shortfall this year. Bradley Belt, PBGC executive director, has said the agency is at long-term risk, especially if some of the airlines with under-funded pension plans go under.

A Kerry presidency means a push to increase the minimum wage from the current $5.15 to $7 an hour by 2007. Kerry has sharply criticized Bush administration regulations changing overtime rules. Labor unions say the changes stripped millions of workers of overtime protection. The White House says the change will help lower-income workers collect overtime pay.

The economy:

While their policies will affect the future of the economy, neither Bush nor Kerry can control the business cycle. There are mixed signals as to whether the next president will have the luxury of an accelerating economy or one that is starting to slow.

Business has been expanding since late 2001. Corporate profits have hit records. Overall inflation is running under 3%, though oil prices spiked to a record $53.64 a barrel Monday.

The unemployment rate has fallen to 5.4% from its recent peak of 6.3% in June 2003, but the number of people who have dropped out of the workforce is up. Job growth is below the pace of other recoveries, and consumer spending is starting to slow. Even employers who are optimistic, are cautious.

Seelye's Welsh calls the economy "a lot better off than gets reported. From our perspective, we're having a great year, as are many of our suppliers and vendors."

Welsh has been hiring. But his optimism, and that of business people he deals with, has its limits. "I could hire another 10 people. We have the work coming in to justify it. But the forecasts that I'm getting from our main customer base, everybody is sitting on their heels, (though) they're starting to stand up a little bit" as the economy expands, he says.

Even as the election nears, most of the market focus is on surging oil prices and the Fed, which has raised its target for short-term interest rates three times since late June, from 1% to 1.75%.

Goldman Sachs in a recent advisory to clients said it expects good performance in the short run, but slower growth in 2005. "Whoever wins the race for the presidency is likely to inherit a difficult economic environment," the firm says, citing the large trade deficit and low consumer saving rates.

Economic issues on election table

Objectives:

Students will:

- read and discuss the article, “Economic issues on election table.”
- develop a graphic organizer that compares Bush’s and Kerry’s fiscal plans. Decide which one they agree with and why.

Concepts:

- Social Security
- Deficits
- Tax cuts and Alternative Minimum Tax (AMT)
- Jobs and the economy
- Trade policy
- Pensions

Preparation:

- Give each student a copy of the article, “Economic issues on election table,” the discussion questions and graphic organizer.
- Divide students into small groups and ask them to discuss the questions.
- Have individuals complete the graphic organizer.

Activity at a glance:

- Grade level: 9-12
- Subjects: economics, personal finance, tax policy, Social Security
- Estimated time for this activity: 45-60 minutes

Materials:

- Reading: “Economic issues on election table”
- Copy of discussion questions and activity
- Graphic organizer
- Pencil and scratch paper

Economic issues on election table

Discussion:

Why does our Social Security system need to be reformed? What effect will putting Social Security taxes into private accounts have on the current system? How might a volatile stock market impact those participating in a privatized plan? Do you think most Americans are savvy enough to successfully play the stock market? Will those without financial know-how be able to afford professional advice?

In groups, read and discuss the article. Then, record detailed answers to the questions that follow. 1.) To what degree will each of these groups benefit from a privatized Social Security system: the rich, the middle class, the poor, your generation, the baby boomers and those currently in their 30s (Gen X)? 2.) Of the above groups, who has the most to lose if Social Security is privatized?

Activity:

Every time a worker in the U.S. is paid, a certain percentage of his or her earnings is deducted and placed in a Social Security fund. From this fund, retired workers receive monthly payments based on their lifetime earnings. Thus, the program is meant to provide a "secure" income for those who no longer work. Social Security operates on a pay-as-you-go system. Benefits to retirees come from the paycheck deductions of current workers, not from a large Social Security savings account. As the number of retiring baby boomers increases, and the number of current workers decreases, Social Security is in danger of going bankrupt.

Social Security is just one fiscal policy that the article addresses. After reading the story, create a graphic organizer that evaluates both Bush's and Kerry's economic plans. Which do you prefer? Why?

Additional resource:

- Goodpayer.com offers a handbook entitled "Learn Now or Pay Later" that helps young adults understand the basics of credit and debt. Visit www.goodpayer.com. You will see the booklet available in PDF format. The booklet also provides tips on choosing a checking account, writing a check, preventing identify theft, etc. To order a copy, call 800-756-4912.

Activity extensions:

- Determine the amount of income that is devoted to the Social Security "payroll tax." Then, calculate the amount of money you would pay in Social Security taxes if you had a beginning annual salary of $25,000 and worked for 42 years, with a 3% salary increase each year.

Economic Policy	Bush	Kerry
Social Security		
Tax cuts		
Deficit		
Trade		
Pensions		
Health care		

Additional Questions

What is the Social Security tax? How long has it been around? What benefits does Social Security provide other than retirement ones? If the current system for collecting and distributing Social Security monies remains at the status quo, how long will it be before the Social Security fund is exhausted?

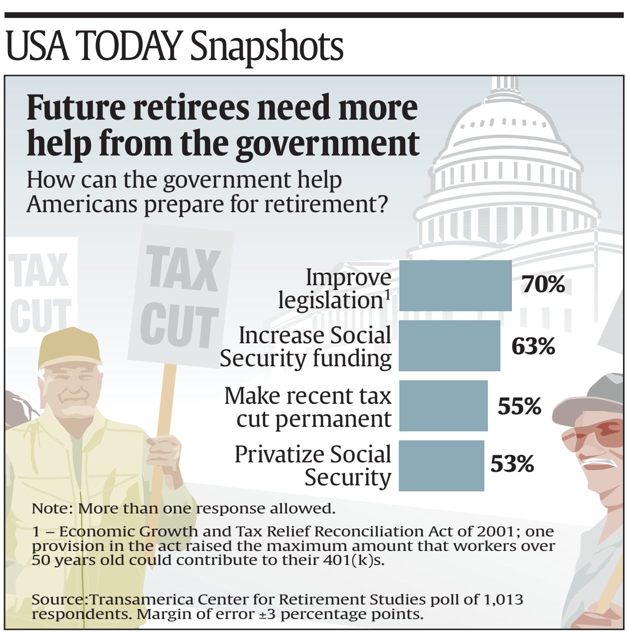
Why is the Pension Benefit Guaranty Corporation running a deficit for the first time in its history? Why is the deficit expected to increase this year?

Bush and Kerry have starkly different positions on trade. Explain the pros and cons of each man's stance.

What is the Alternative Minimum Tax?

Who will choose a successor for Federal Reserve Chairman Alan Greenspan? Why is the decision such an important one?

Snapshot



By Darryl Haralson and Dave Merrill, USA TODAY

What kind of legislation could help people prepare for retirement? How are individuals and the nation affected when older citizens cannot adequately support themselves?