Free Advice for Democrats

By N. Gregory Mankiw and Phillip Swagel

Over the past two years, we were paid to give economic advice to the president. Now that we are private citizens again, we offer Democrats some free advice on how to handle the issue that is now on the top of everyone's in-box: Social Security. So here is our easy, seven-step program for recovering obstructionists:

Take your heads out of the sand. Some members of your party want to deny that we need to fix Social Security. Let’s face it: When you do this, you look like idiots. President Clinton talked about the “crisis” in Social Security long before President Bush did. Sure, you can make a plausible argument that Social Security’s unfunded liabilities are not a “crisis” but only a “major problem.” But even if you win that argument, you lose. You look like you’re more interested in word games than good policy.

Eschew tax increases. Republicans enjoy nothing more than calling Democrats “tax-and-spend liberals.” If you want to avoid that label the next time you run for president, this is the perfect opportunity to change your stripes. Stand up and agree that we can fix Social Security without raising taxes.

Embrace personal accounts. By themselves, voluntary personal accounts are neither a panacea nor a threat to the social safety net. The key is how the system works. So stop objecting to the concept of personal accounts and focus on the details. Remember that most Americans trust their 401k plan more than they trust Congress.

Stop railing about the budget impact. The introduction of personal accounts will involve some transition financing, but this increase in the budget deficit won’t place a new burden on future generations. These deficits are just an acknowledgement of promises that were made long ago. And if you think that complaining about budget deficits will advance your career, just ask President Mondale.

Protect people from Wall Street sharks. No one on Wall Street thinks they will get rich managing personal accounts for Social Security. But as Eliot Spitzer has demonstrated so brilliantly, demonizing the financial community can be good politics. Take his lead by insisting that management fees for personal accounts be kept at rock bottom. Insist on low-cost index funds.

Protect people from themselves. Personal accounts give people the option of accepting some investment risk to earn higher expected return. But it is a legitimate worry that some people will take on too much risk at the wrong time. You can insist that as workers near retirement, they limit their exposure to risky equities to, say, 50% of their account balances.
Protect the poor. As President Bush has made clear, Social Security reform will require slowing the growth of benefits for future generations. Pay close attention to how this is done. Changing indexing rules will have a roughly proportionate impact on rich and poor. So would raising the eligibility age (which, by the way, is our preferred solution). But, as Democrats, you should insist that workers with high lifetime earnings bear the brunt of the cuts. Insist that the benefit formula be reformed with minimal changes at the bottom and maximal changes at the top of the earnings scale.

Follow these steps and everyone’s a winner. The president can claim to have given personal accounts to young workers, and you Democrats can claim to have defended the social safety net from the clutches of greedy financiers, excessive risk-takers, and heartless Republicans (like us). Best of all, the American people will have a Social Security system that will work not only for them but also for their children and grandchildren.

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