



Why Social Security Reform Is *Not* Like Enron

by David Hogberg

The *Cedar Rapids Gazette* recently printed my column promoting Social Security reform through personal accounts and warning of the folly of relying on the Social Security Trust Fund. On the same page, the *Gazette* printed *Fort Worth Star-Telegram* columnist Bob Ray Sander's piece arguing against reform as a counter to my column. Unfortunately, Sanders' column was so full of ignorance and distortions as to be almost useless except as a prime example of much that is wrong with arguments of Social Security reform opponents.

Sanders' argument can be summarized as follows: The recent failure of the Enron Corporation destroyed the retirement savings of many Enron employees. The example of Enron is typical of what can happen when retirement funds are invested in the stock market. The reason is that the stock market is a "risky gamble." Thus, Social Security should not be reformed with personal accounts invested in stocks, because these investments will put too many Americans at risk of losing their retirement funds.

Let's examine this argument one piece at a time.

1. Enron is typical of retirement investing in the stock market. Sanders plays fear of the Enron disaster to the hilt. He reports that "Tearful retirees told members of the Senate Commerce subcommittee how they had watched their nest eggs disappear. A 61-year-old Florida woman said her Enron stock holdings shrank from \$700,000 to \$20,418." He then urges the reader to imagine this on a mass scale: "Think of those who lost their life savings on one company's failure, and imagine what it would be like if millions of people in this country retired and realized that one-third, or half or any portion of their retirement money had disappeared."¹

This is certainly a scary scenario. It is also an exceptionally improbable one. The truth is that the Enron case is *atypical*. The employees at Enron had most of their retirement funds invested almost entirely in Enron's stock. This violates the number one rule of prudent investing, "diversify." The vast majority of retirement funds are diversified, that is they are composed of stocks from many different companies from many different sectors of the economy. Diversification reduces the risk to investors: if the stock they own in one company collapses, little damage is done to their overall investments. By putting all of their retirement eggs in one basket, the employees of Enron were engaging in risky strategy for retirement. Fortunately, most retirement funds do not follow such a strategy.

2. Reforming Social Security with personal accounts would put ordinary Americans at risk of losing their retirement funds. Sanders continues his scare tactics by linking Social Security reform to his scenario of millions of Americans losing retirement money: "That's the fear some people have if we move forward with privatizing any portion of Social Security. That's my fear. So, when the subject [of reform] comes up again, just remember: 'Enron.'"²

A Publication of:

Public Interest Institute at Iowa Wesleyan College

600 North Jackson Street

Mt. Pleasant, Iowa 52641-1328

Phone: 319-385-3462 Fax: 319-385-3799

E-Mail: public.interest.institute@limitedgovernment.org Web Site: www.limitedgovernment.org

If Sanders thinks that privatizing Social Security would look anything like the Enron fiasco, he clearly has not read the report by the President's Commission to Strengthen Social Security. The reform discussed by the Commission Report would allow personal accounts to be invested in stock funds. But as the Commission Report states, "The stock fund itself must... be very *diversified* and reflect the performance of many companies spanning all major commercial sectors" [italics added].³ Thus, personal accounts will be prudent investments, providing account holders protection against the collapse of any one company.

3. The stock market is a risky gamble. Sanders claims that personal accounts will reduce "the amount of dollars going into the Social Security Trust Fund while gambling on the risky stock market." He then warns "that precious retirement funds should not be used for gambling."⁴ Again, Sanders doesn't know what he is talking about. If the stock market is so risky, why do so many major retirement funds like TIAA-CREFF (for professors) and the Thrift Savings Plan (for Federal Employees) invest large amounts of assets in it? Are the people who run such funds imbeciles? Or do they know something that Mr. Sanders does not?

Mr. Sanders further displays his ignorance of the stock market by highlighting the market's dismal performance in 2001: "In the past year alone, we've seen how fickle the stock market can be, and how it can be manipulated by bad news."⁵ This is a classic example of the inability to see the forest for the trees. The stock market does have periods, like 2001, where it declines, but these periods are *short-term*. Had Mr. Sanders bothered to do any research, he would have discovered that the long-term trend in the stock market is one of positive growth. From 1926-1996, the average annual rate of return from the stock market was 7.56%. In fact, during the worst twenty-year period (1929-1948) the stock market still returned an average of 3.36% annually.⁶ In sum, betting on the stock market is about as risky as betting that the sun will come up tomorrow.

So don't let opponents of Social Security reform scare you with Enron scenarios. Personal accounts will look nothing like the Enron fiasco. Rather they will be invested in diverse portfolios in the stock market. So when the subject of reform comes up, don't think "Enron." Think "prudent investment."

ENDNOTES:

¹ Bob Ray Sanders, "No: Just say 'Enron' to Social Security fix," *Cedar Rapids Gazette*, January 6, 2002, Sec. A, p.5.

² Ibid.

³ *Strengthening Social Security and Creating Personal Wealth for All American: Report of the President's Commission*, President's Commission to Strengthen Social Security, December 21, 2001, p.47. The Commission report can be found at <http://www.csss.gov>.

⁴ Bob Ray Sanders, "No: Just say 'Enron' to Social Security fix," *Cedar Rapids Gazette*, January 6, 2002, Sec. A, p.5.

⁵ Ibid.

⁶ Melissa Hieger and William Shipman, "Common Objections to a Market-Based Social Security System: A Response," *The Cato Project on Social Security*, Cato Institute, July 22, 1997, p.7.

David Hogberg is a Research Analyst with Public Interest Institute.

Permission to reprint or copy in whole or part is granted, provided a version of this credit line is used: "Reprinted by permission from INSTITUTE BRIEF, a publication of Public Interest Institute." The views expressed in this publication are those of the author and not necessarily those of Public Interest Institute. They are brought to you in the interest of a better-informed citizenry.