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Jose Pinera: Social Security in the U.S. to Face Deficit in 7 Years

By [editor](#)|Feb 22, 2010, 4:25 PM|[Author's Website](#)

FOX Business Network's Brian Sullivan speaks in this interview with famed economist and fmr. Chilean Labor and Social Security Minister Jose Pinera about the Social Security problem in the United States. According to Pinera, in seven years we will be facing a deficit in entitlement accounts.



Pinera on U.S. \$100T Debt Problem



Here is the interview's Transcript : *Courtesy of Fox Business Network*

BRIAN SULLIVAN, FBN ANCHOR: We are very honored to be joined by Jose Pinera. He is the founder of the International Center for Pension Reform. He is the former labor and social security minister of Chile and a distinguished senior fellow at the Cato Institute. Up from Santiago into D.C., which is where we are. Jose, it's a pleasure. Thank you very much.

JOSE PINERA, FOUNDER, INTERNATIONAL CENTER FOR PENSION REFORM: Good morning. Thank you very much, Brian.

SULLIVAN: Last week, we hit hard on the program the latest Pew Center study showing that states have about a trillion dollars gap in their — just state — pension plans. How do we solve that?

PINERA: Well, that is a very serious problem and I'm extremely worried about all the debt America has.

But you have a much bigger problem, Brian. You have a 100 trillion-dollar problem. Look, this is something published by the American government, saying that the present value of the obligations on health and Social Security amount to a 100 trillion dollars...

SULLIVAN: OK, wait a minute. We were talking about 3-point-something trillion, 1 trillion underfunded. You are saying we have 100 trillion dollars. Where is that number coming from? How do we get to 100 trillion?

PINERA: This comes from the government. This is not recognizing the public debate, but this is the real debt of America. This amounts to 700 percent of GDP. This is a gigantic liability that basically you are legislating and will be paid by your children and your grandchildren.

SULLIVAN: Let's walk through what that is, OK? Because these are new numbers. These are big numbers. These are coming from the CBO, correct?

PINERA: These are coming from government, from the U.S. government. These are net, liabilities of the health, Medicare and Social Security system. This is the present value of what Americans will have, one way or another, to pay, unless they default on their obligation to the citizens.

And that is the future. And I'm extremely worried because it is like you are passengers in the Titanic. The Titanic is going towards the iceberg of aging populations. The populations that feel entitled to all the huge benefits that the politicians have promised the people. But they have not funded the benefits for the future. So how are you going to pay them? That is the big issue. The big domestic problem facing America.

SULLIVAN: One of the big stories today is the president unveiling his own healthcare plan. On this piece of paper, again from the CBO, \$35 trillion in hospital insurance for current and future. \$34 trillion for Medicare Part B, about \$18 trillion for drug benefits and Social Security.

So, actually Social Security, which we're going to talk about later on — that is actually a big hole, but it's smaller than health care. How are we going to pay for this? How does the U.S. cover a 100 trillion dollars, Jose?

PINERA: Brian, the problem is what I call the entitlement state. The problem is that there is gigantic disconnect between what people want the government to pay them in the future, in health pensions, and what the people want to pay in tax. And because the entitlement state is based on promises for the future, you don't have to pay it today.

This is growing, because to win elections, politicians offer benefits to people that will be paid in the future. So, this big hole is not only a problem in America. It's exactly the same problem in Greece today, in southern Europe, eventually in France, in Germany. The West will go bankrupt until and unless you reform deeply the entitlement state. This was created by Prince Bismarck (ph) in the 19th century. You are all prisoners of Prince Bismarck (ph). Prisoners of a system...

SULLIVAN: Otto von Bismarck?

PINERA: Yes.

SULLIVAN: Because he created...

PINERA: He created the unfunded tax-and-expense system. You said, he simply said if you tax workers a little, we can pay the pensions. But then the unintended consequences has been with the aging of population and the extended life, you have been accumulating this huge liabilities that eventually be bankrupt the government. A huge fiscal crisis is coming to the West unless you face it and confront it directly by completely changing the entitlement estate. That's the root of the problem.

SULLIVAN: I want to get more on Social Security in just a bit. But for pensions — OK. State and federal pensions. The gap between retirement ages between private and public is growing wider. The gap between the amount of money being given in pensions is growing wider.

How do we just solve the pension crisis on government workers, federal and state? And is it unsustainable as it is?

PINERA: It is totally unsustainable. You either will have to raise taxes big-time in America, or you will have to cut benefits. But it's extremely difficult to do that in a system in which you have people entitled to all these things.

That's why what we did in Chile was to completely change the logic. In Chile, you save for old age. In Chile, we have sort of a Benjamin Franklin system, you see. You remember Benjamin Franklin, the thirteen virtues? You should save for the future, you should be self-reliant. We have instilled a culture of personal responsibility and saving.

Of course, we also have a safety net for the very poor. But 80, 85 percent of the population will finance their old age, health and pension with their own personal savings.

SULLIVAN: We are going to take a quick break, Jose. We will come back and talk about what you did in Chile, and what we might have to do here. Look at some of the pretty scary numbers around Social Security. And also what we can do about it.

Will the Chilean plan work here? How does it work? We are going to learn as we continue part two of our

exclusive interview with Jose Pinera, right after this.

(COMMERCIAL BREAK)

SULLIVAN: Welcome back. I'm Brian Sullivan in Washington, D.C. today, and I am here because we are being very privileged to speak to Jose Pinera. He's the architect of Chile's Social Security reform. He's the former labor and Social Security minister and the founder of the International Center for Pension Reform. It is an exclusive interview.

Jose, we're very happy to have you. Listen, although some of the numbers you are throwing around are pretty frightening, there have been — there's a lot of debate in this country about whether or not our Social Security plan, our system is going to be there for people that are in their 20s and 30s. There's a big debate about whether or not we will be solvent by 2040. Do you believe that the U.S. system as it is now can be solvent decades from now?

PINERA: Clearly not.

SULLIVAN: Clearly not.

PINERA: Clearly not. In only seven years, the Social Security system will begin to have a deficit. That is more money will have to be spent than money coming in.

And then you will face the very hard choices. You will probably have to increase the retirement age. You will probably have to increase payroll tax. You may have to cut benefits, unless you change the paradigm and you go to a system of personal accounts.

Personal accounts is very simple. You save for old age. And that saving gets accumulated rate of return, so you benefit from that extraordinary force of compound interest. When you reach 65, you are going to look whether the government is deficit or in surplus, you look at the balance of your account, and with that, you buy annuity for your life.

It is a system we had all over the world before Otto von Bismarck, a Prussian chancellor created this monster of the unfunded welfare state that is bankrupting Europe and eventually the U.S.

SULLIVAN: That's the problem with Social Security, right? Is that we are using money now. Instead of me saving for myself, the money that is taken out of my paycheck, out of everybody in this room's paycheck, is being paid to current beneficiaries. You have described that as a Ponzi scheme.

PINERA: That is a Ponzi scheme. You could even call it a Madoff scheme.

SULLIVAN: Hopefully, the money is real somewhere.

PINERA: No, there is no money being saved for the future. There is no funding. There's no trust fund. You are paying the money immediately to the retirees, and the problem is that with Baby Boom generation retiring, with the expectancy of life increasing every single year because of your great doctors and researchers, you will not be able to pay the promises.

So, the system will eventually default. Technically default in the sense that you will have to break the promises to the people, and that may create a lot of pain and a lot of anguish. That's why you have to look into the future, do the responsible thing and begin moving towards a system of personal accounts. It's the only long-term solution.

SULLIVAN: Seventy-one million people will be 65 in this country by 2030. 330 people turn 60 years old every hour right now. But they are expecting benefits. How would we implement a system like yours with everybody

already expecting the current system to be there for them?

PINERA: The first decision that I took as secretary of labor and Social Security of Chile was to guarantee the benefits of the elderly. I call it we are not going to take your grandmother check away. We will find a way to protect the elderly.

So, the system has to be changed for the young people, for the future that are coming into the labor force or are already in the first years of the labor force. And the moment you change the dynamic and people begin to know that if they save more, they work more, they will get a better pension out of their own saving, then the whole system begins to...

SULLIVAN: Here's the criticism will be that we are at 11-year flat line for the stock market. That if you have your money in the stock market for 11 years, you are basically flat. That's what people will say. That the stock market has proven that it is not a wealth creator. At least in the short-term.

PINERA: The stock market is today the Dow Jones is around 10,000.

SULLIVAN: 10,300.

PINERA: Do you know how much it was when we began our system in Chile 30 years ago?

SULLIVAN: Thirty years ago. 1980 — 2 grand. Dow 2000.

PINERA: 900. The Dow Jones was 900. So — if you had began your system at the same moment that Chile began, you would have benefited enormously from the stock market.

SULLIVAN: Tenfold gain.

PINERA: OK. And you don't have to put all the money in the stock market at all. We don't put it all. You can have a very diversified portfolio of corporate bonds, of mortgages, of government bills (ph), of stocks international — you have to be very prudent with long-term management. That's how we have been in Chile, and that's why we have been able to give workers a rate of return of 9 percent above inflation for 30 years compounded.

So, the system works because in the long run, you see your economy is so strong. I do believe in America. And you must believe that workers by saving for old age would be much better than the government promise.

SULLIVAN: Instead of the 12.4 percent tax that we pay, like in Chile, they take 10 percent out, automatically put that into a private account that's not for use for current beneficiaries it is our money; correct?

PINERA: Yes, correct. Your money is protected constitutionally. That money grows in your account exponentially compounded 45 years, so forget the...

SULLIVAN: Can the government tap into it?

PINERA: No, no...

SULLIVAN: If Chile if the government gets into — in Chile if the government gets into financial difficulty, can they go raid that money?

PINERA: No way. It is protected by property rights. This is your money, we have accumulated already seventy percent of GDP in that money. The capital markets in Chile have boomed, have increased. We are financing the new infrastructure, the new growth of the industrial, the forest, with this money.

Instead of Chile having a huge trillion-dollars debt, as you have, we have a huge funded system of retirement.

SULLIVAN: Jose Pinera, we are going to leave that here. But I know later on we will be speaking about European problems. Thank you very much for joining us, at least in this hour. And we're going to see you more in a couple of hours. Jose Pinera of Chile. Thank you, Jose

PINERA: Thank you very much, Brian.

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