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WISCONSIN RAPIDS & MARSHFIELD 2004 ECONOMIC INDICATORS

**4th Quarter 2004
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Special Report: A Report on the Solvency of the Social Security Combined Trust Funds and the Demographic Factors Influencing Future Fund Balances.

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A Report on the Solvency of the Social Security Combined Trust Funds and the Demographic Factors Influencing Future Fund Balances.



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NATIONAL AND REGIONAL OUTLOOK

When compared to other states, Wisconsin's economic performance was very robust in 2004. Recently released figures from the U.S. Bureau of Labor Statistics indicate that Wisconsin came in ninth place in terms of jobs creations. Only eight other states exceeded the state in job creation. The government reports that Wisconsin added about 64,000 net new positions, a gain of approximately 2.3 percent. In contrast, the nation added about 1.7 percent to its payrolls.

What is particularly pleasing about this growth is that manufacturing employment is said to have rebounded by almost 16,000 jobs. This represents a healthy gain of over 3 percent. Given the state's high dependence on manufacturing employment, this indeed is welcomed news. Wisconsin ranks second among the states in terms of its dependence on manufacturing as a source of employment.

In addition, the Wisconsin Department of Revenue indicates that in 2004 Wisconsin experienced solid economic growth in employment and income. Moreover, the agency reports that this trend is likely to continue well into 2005. The Wisconsin Department of Revenue is forecasting that job growth will be approximately 1.8 percent during 2005, and wages and salaries are forecasted to grow by approximately 6 percent. Once again, if this forecast holds true, it would be welcomed news for the state.

Why has Wisconsin's and the nation's economy rebounded? Because of Wisconsin's dependence on manufacturing, the state benefits greatly when the national economy picks up steam. In other words, Wisconsin manufactures products that are much in demand at the beginning of an upturn in the national business cycle. In addition, the depreciation of the dollar helps Wisconsin's exporting activity by making its products less expensive to people living outside the country. The next question to be answered is why has the national economy gained economic momentum.

The reasons for this overall expansion in the national economy are many. A few of the more important reasons are as follows. The Federal Reserve reports that there has been a strong upward trend in spending by households and in their income levels. Moreover, business firms have definitely pulled out of their investment slump. It appears that business firms, in anticipation of profits, are once again investing in factories, plants, equipment and inventories. The economic slump in the early 2000s was predicated upon a retrenchment in business investment. The Federal Reserve also credits favorable monetary conditions for helping foster the improved climate. Interest rates are still relatively low, and credit availability remains abundant. Also, exceptionally strong productivity gains over the last four years have contributed to this expansion. On average, U.S. worker productivity has grown at over four percent since 2000. In the long-run, this translates into higher corporate profits and income growth for

workers. The technological revolution in computer aided business procedures has played a key role in this development.

Another factor playing a key role in the favorable growth forecast is the prospect for low inflation in 2005. The Federal Reserve and most economic analysts see inflation being lower in 2005 than the 3.3 percent in 2004. Even though the dollar has declined by approximately 30 percent against a basket of major foreign currencies, which makes imports more expensive, other factors will mitigate this upward pressure on prices. For example, there is still a significant amount of capacity left in the U.S. economy. In other words, there remains a good deal of underutilized resources. Moreover, competition is so strong in most industries that importers are very reluctant to raise prices in fear of losing market share. Lastly, productivity growth, having been so strong for so long, allows for the dissipation of higher input prices. Simply stated, if workers are more productive, costs can be spread out over a greater number of units. Thus, firms can keep prices down and still cover the higher production costs. Thus, unless some unforeseen economic or political crisis occurs, the most likely economic prognosis for the state and nation appears to be solid economic growth in 2005.

**TABLE 1:
NATIONAL ECONOMIC STATISTICS**

	2003 Fourth Quarter	2004 Fourth Quarter	Percent Change
Nominal Gross Domestic Product (Billions)	\$11,270.9	\$11,967.0	+6.2
Real Gross Domestic Product (Billions of 2000 \$)	\$10,580.7	\$10,975.7	+3.7
Industrial Production (1997 = 100)	113.4	117.8	+3.9
Three Month U.S. Treasury Bill Rate	0.92%	2.23%	+141.8
Consumer Price Index (1982-84 = 100)	184.3	190.3	+3.3

CENTRAL WISCONSIN

A summary of the economic indicators for our region is as follows. The unemployment rates were significantly below those of a year ago. Total employment was higher in almost all the reporting areas, and the rates of employment change were very impressive. Nonfarm employment grew almost in all categories--the exception being manufacturing and government payrolls. Retail sales activity was mixed with some counties experiencing more sales growth than others. Lastly, the survey of regional business leaders suggests that the local economy will grow more rapidly in the months ahead when compared to a last year's performance.

Unemployment rates were significantly lower for all reporting areas (Table 2). The unemployment rates for Marathon, Portage, and Wood counties stood at 3.3, 4.0, and 4.9 percent respectively. The unemployment rate for the state was 4.2 percent and for the nation 5.1 percent. In both cases, the aforementioned rates represent significant declines from the previous year's marks. In sum, there has been a marked improvement in the unemployment situation which reflects an improving economic situation.

**TABLE 2
UNEMPLOYMENT IN CENTRAL WISCONSIN**

	Unemployment Rate December 2003	Unemployment Rate December 2004	Percent Change
Portage	4.1%	4.0%	-3.5
Marathon	3.9%	3.3%	-14.2
Wood	5.3%	4.9%	-7.8
Central Wisconsin	4.3%	3.9%	-9.3
Wisconsin	4.9%	4.2%	-15.1
United States	5.4%	5.1%	-5.2

Employment figures are given in Table 3. Portage and Marathon experienced good amounts of growth in their payrolls, 1.8 and 2.2 percent respectively. In contrast, Wood county payrolls were at about the same level as a year ago. Wisconsin and the United States employment figures climbed, 1.7 and 1.2 percent respectively when compared to last year. Finally, the number of people employed in Central Wisconsin expanded from 152.1 to 154.4 thousand, or about 1.5 percent from a year ago. Lastly, employment growth in most geographic areas appears to be accelerating.

**TABLE 3
EMPLOYMENT IN CENTRAL WISCONSIN**

	Total Employment December 2003 (Thousands)	Total Employment December 2004 (Thousands)	Percent Change
Portage	38.4	39.1	+1.8
Marathon	74.0	75.7	+2.2
Wood	39.7	39.6	-0.2
Central Wisconsin	152.1	154.4	+1.5
Wisconsin	2,915.3	2,963.8	+1.7
United States	138,556	140,278	+1.2

Employment figures based on a government survey of employers is given in Table 4. Total nonfarm employment is estimated to have risen from 149.0 to 151.0 thousand or about 1.3 percent from December 2003. Good news comes from the manufacturing sector where the decline in employment appears to have leveled off. The only other sector to register a decline was the government sector. All other sectors in Central Wisconsin were reported to have made nice gains in their payroll levels.

**TABLE 4
CENTRAL WISCONSIN EMPLOYMENT CHANGE BY SECTOR**

	Employment December 2003 (Thousands)	Employment December 2004 (Thousands)	Percent Change
Total Nonfarm	149.0	151.0	+1.3
Total Private	129.2	131.5	+1.8
Construction & Natural Resources	5.4	5.5	+1.9
Manufacturing	29.8	29.7	-0.3
Trade	28.0	28.4	+1.4
Transportation & Utilities	8.0	8.2	+2.5
Financial Activities	9.8	10.0	+2.0
Education & Health Services	21.6	22.0	+1.9
Leisure & Hospitality	10.7	11.0	+2.8
Information & Business Services	15.9	16.6	+4.4
Total Government	19.8	19.6	-1.0

County sales tax collections are a barometer or a gauge of economic activity (Table 5). Portage County's sales tax collections are estimated to have declined slightly from \$1.17 to \$1.13 million over the year or about 3.5 percent. In Marathon County, sales tax collection rose from \$2.58 to \$2.70 million or about 5 percent. Wood County had no sales tax in place as of fourth quarter 2003, thus no comparison can be made with the 2004 collection.

**TABLE 5
COUNTY SALES TAX DISTRIBUTION**

	2003 Sales Tax Fourth Quarter (Thousands)	2004 Sales Tax Fourth Quarter (Thousands)	Percent Change
Portage County	\$1,171.4	\$1,130.9	-3.5
Marathon County	\$2,575.5	\$2,704.7	+5.0
Wood County	NA	\$1,113.9	NA

The business confidence index in Table 6 shows that recent changes at the national and local level were judged in a positive light by the survey groups. It seems that they were particularly pleased with the recent changes at the national level. The survey group also felt that economic matters would improve locally and their particular industry should show a marked amount of sales growth in the quarters ahead. The response for the industry question was encouraging because it has strong implications for job and income growth in our area.

**TABLE 6
BUSINESS CONFIDENCE IN CENTRAL WISCONSIN**

	Index Value	
	September 2004	December 2004
Recent Change in National Economic Conditions	60	65
Recent Change in Local Economic Conditions	58	58
Expected Change in National Economic Conditions	65	60
Expected Change in Local Economic Conditions	57	58
Expected Change in Industry Conditions	60	62

WISCONSIN RAPIDS AREA

A summary of the economic variables for Wisconsin Rapids is as follows. The unemployment rate in Wood County declined from 5.3 to 4.9 percent over the past twelve months. Total employment in the county was virtually unchanged. Similarly the number of nonfarm jobs was for all intent and purposes unchanged from a year ago. Public assistance claims and unemployment claims are well below last year's marks. Lastly figures 1 through 6 show how the Wood County economy has fared over the 1990-2004 time frame.

Table 7 gives a detailed presentation of Wood County employment change by major industrial sector. This data is compiled by the government from a survey of business firm payroll data. Total nonfarm employment is estimated to have declined by 0.4 percent from last year. Declines in manufacturing employment continued to be a drag on the economy; it was down by 5.4 percent from last year. Also, trade has declined by an estimated 2.8 percent over the period. It is clear that problems associated with the paper industry in south Wood County are driving these results and are also influencing the trade numbers. However, the good news is that just about every other sector in Wood County experienced a decent amount of job expansion. For example, transportation and utilities, education and health services, leisure and hospitality, and information and business all posted job gains.

**TABLE 7
WOOD COUNTY EMPLOYMENT CHANGE BY SECTOR**

	Employment December 2003 (Thousand)	Employment December 2004 (Thousands)	Percent Change
Total Nonfarm	44.7	44.5	-0.4
Total Private	39.2	39.2	0
Construction & Natural Resources	1.7	1.7	0
Manufacturing	7.4	7.0	-5.4
Trade	7.1	6.9	-2.8
Transportation & Utilities	3.2	3.3	+3.1
Financial Activities	1.2	1.2	0
Education & Health Services	11.1	11.2	+0.9
Leisure & Hospitality	2.7	2.8	+3.7
Information & Business Services	4.8	5.0	+4.2
Total Government	5.5	5.4	-1.8

Figure 1 shows how paper manufacturing employment has trended over the past number of years. The high point in employment came around 1997 when almost 52,500 people were employed. At the beginning of 2005 the number of people employed contracted to around 38,000. The decline of about 15,000 positions reflects the difficult economic conditions facing the paper manufacturing industry in Wisconsin. Slumps in worldwide demand and cheap imports have played a key role in this situation.

FIGURE 1



The help wanted advertising index for the Wisconsin Rapids area is given in Table 8. In December the reading stood at 73. This means there was .73 of a position being advertised for every 1.00 position advertised in the base year. There was no number for the year 2003 because the CWERB commenced collecting data on advertising in 2004. The amount of advertising at the national level remains at a low level, at a mark of 36.

**TABLE 8
HELP WANTED ADVERTISING IN WISCONSIN RAPIDS**

	Index Value	
	2003	2004
Wisconsin Rapids (December) 1980 = 100	NA	73
U.S. (November) 1987 = 100	38	36

Table 9 presents some good news for the area in terms of a reduction in family financial distress. Public Assistance claims on a monthly average basis declined from 104 to 91 or about 12.5 percent in our year over comparison. More good news comes in table 10. Unemployment claims in Wood County are much lower than one year ago (Table 10). New claims on a weekly average fell from 359 to 279 for a percentage decrease of 22.3. Likewise total claims dropped sharply from 1,670 to 1,247 or by 25.3 percent. Perhaps these measures of local family distress signal a more robust economic situation in the near future.

**TABLE 9
PUBLIC ASSISTANCE CLAIMS IN WOOD COUNTY**

	2003 Fourth Quarter (Monthly Avg.)	2004 Fourth Quarter (Monthly Avg.)	Percent Change
New Applications	N/A	N/A	N/A
Total Caseload	104	91	-12.5

**TABLE 10
UNEMPLOYMENT CLAIMS IN WOOD COUNTY**

	2003 Fourth Quarter (Weekly Avg.)	2004 Fourth Quarter (Weekly Avg.)	Percent Change
New Claims	359	279	-22.3
Total Claims	1,670	1,247	-25.3

Figure 2 presents Wisconsin average weekly earnings in paper and allied products manufacturing. The latest figures available suggest a rebound has taken place in earnings. Earnings per week are now about \$825 per week. This represents an improvement from around \$800 per week from a couple of years ago. The chart also shows that from 1998 the level of weekly earnings has been fairly flat. This of course reflects the overall economic condition of the industry and the difficult times it has faced in recent years. Hopefully the rebound in the national and world economy will help to correct this situation.

FIGURE 2

Wisconsin: Average Weekly Earnings: Paper and Allied Products; NSA

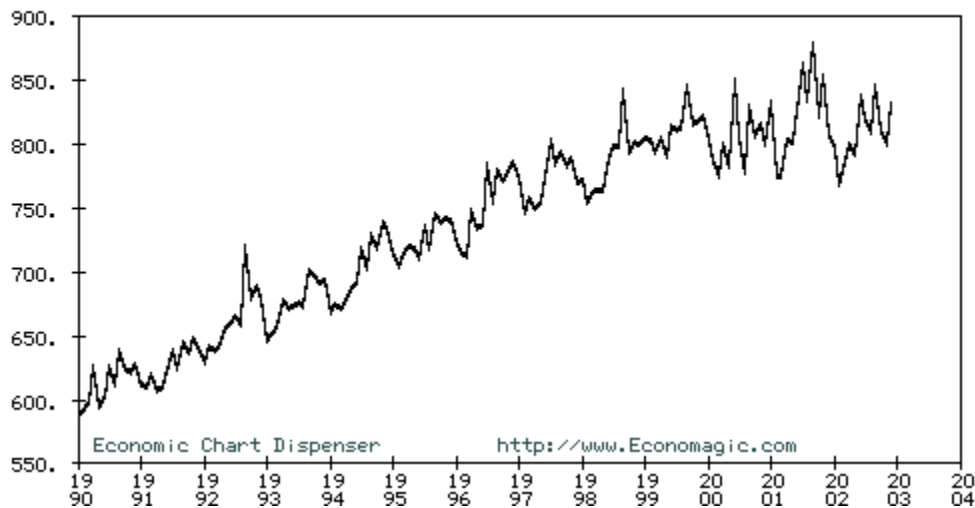


Figure 3 shows the historic trend for Wood County employment. In addition the employment level in Wood has been trending upward over the latter part of 2004. Figure 4 shows the seasonal fluctuations of unemployment in the county, and Figure 5 gives the unemployment rate movements since 1990. Currently the rate is below 5 percent. Lastly, Figure 6 shows that the labor force continues its upward trend in the county which should bode well for area employers in search of additional workers. All of these figures paint a comprehensive picture of the employment situation in Wood County from 1990 to the present.

FIGURE 3

Employment Level: Wood County, WI, Wisconsin; Thousands; NSA

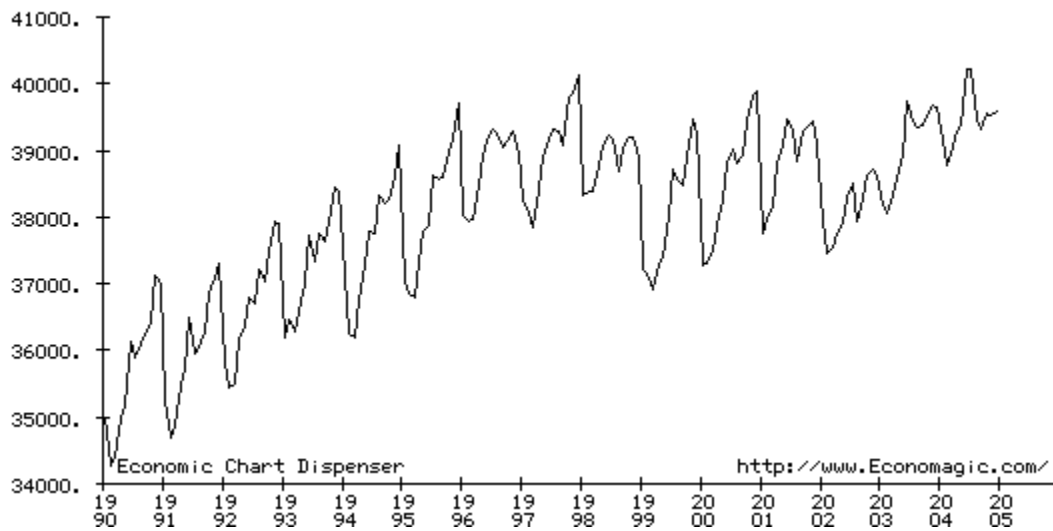


FIGURE 4

Unemployment Level: Wood County, WI, Wisconsin; Thousands; NSA

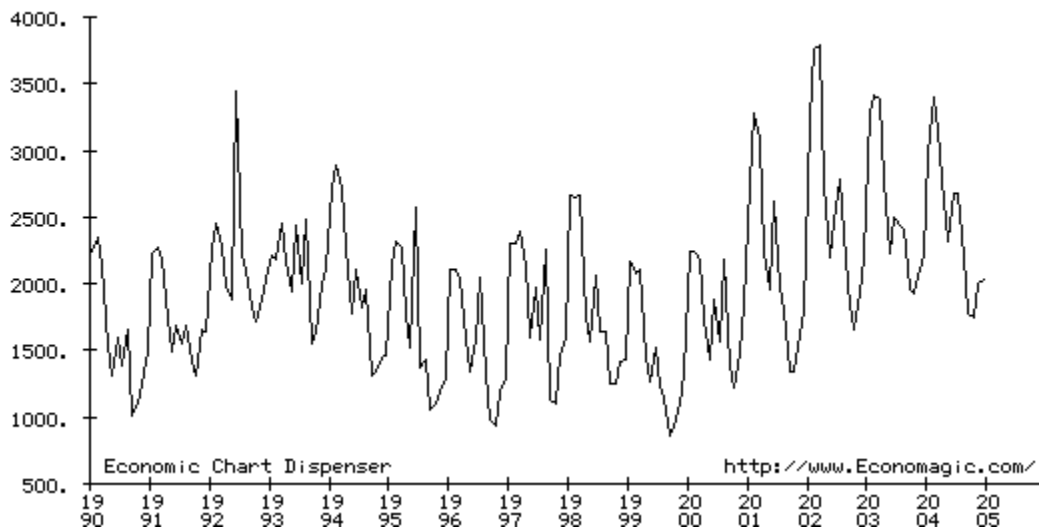


FIGURE 5

Unemployment Rate: Wood County, WI, Wisconsin; Percent; NSA

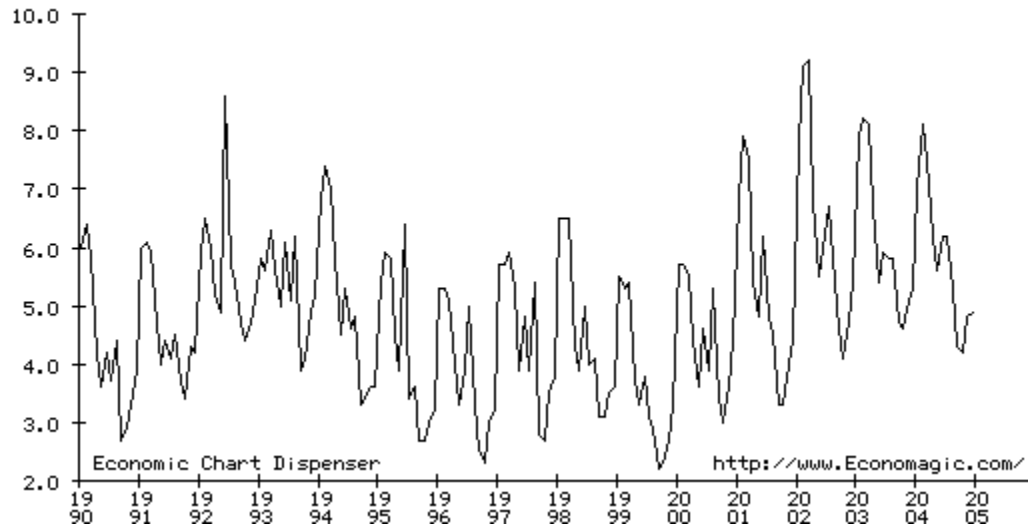
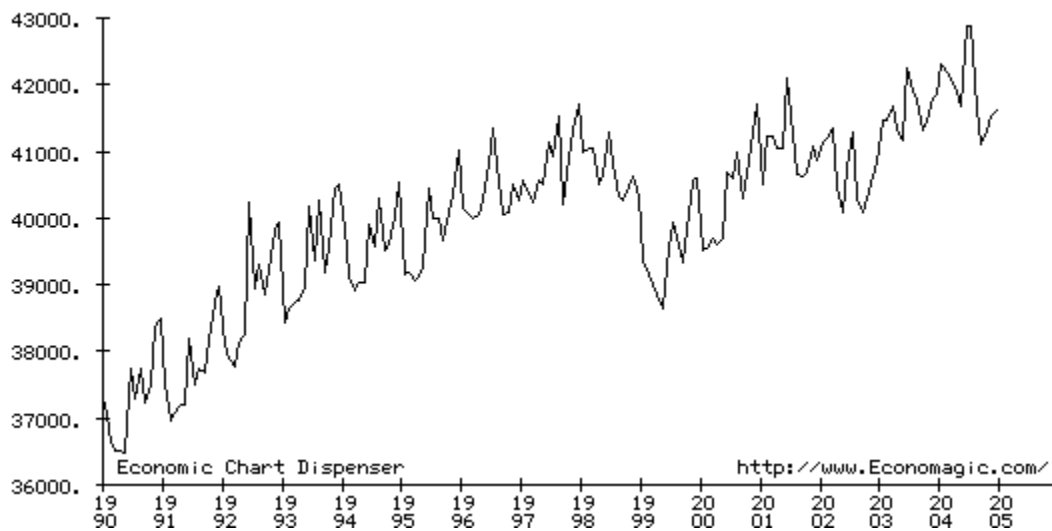


FIGURE 6

Labor Force: Wood County, WI, Wisconsin; Thousands; NSA



MARSHFIELD AREA

The results for the area are mixed this quarter. Some indicators of economic performance were very good. On the other hand, some were weaker than one would have hoped to see. However, with the state and national economies appearing to be picking up a lot of momentum this should bode well for the local economy.

Table 7 gives a detailed presentation of Wood County employment change by major industrial sector. This data is compiled by the government from a survey of business firm payroll data. Total nonfarm employment is estimated to have declined by 0.4 percent from last year. Declines in manufacturing employment continued to be a drag on the economy; it was down by 5.4 percent from last year. Also, trade has declined by an estimated 2.8 percent over the period. It is clear that problems associated with the paper industry in south Wood County are driving these results and are also influencing the trade numbers. However, the good news is that just about every other sector in Wood County experienced a decent amount of job expansion. For example, transportation and utilities, education and health services, leisure and hospitality, and information and business all posted job gains.

TABLE 7
WOOD COUNTY EMPLOYMENT CHANGE BY SECTOR

	Employment December 2003 (Thousands)	Employment December 2004 (Thousands)	Percent Change
Total Nonfarm	44.7	45.5	-0.4
Total Private	39.2	39.2	0
Construction & Natural Resources	1.7	1.7	0
Manufacturing	7.4	7.0	-5.4
Trade	7.1	6.9	-2.8
Transportation & Utilities	3.2	3.3	+3.1
Financial Activities	1.2	1.2	0
Education & Health Services	11.1	11.2	+0.9
Leisure & Hospitality	2.7	2.8	+3.7
Information & Business Services	4.8	5.0	+4.2
Total Government	5.5	5.4	-1.8

Retailer confidence in Marshfield is presented in Table 8. This panel believes that store sales were ahead of last year's pace but traffic was deemed to be lower. In contrast, this group was quite optimistic about future level of sales and store traffic. Given the importance of retail activity, it would bode well for the economy if their forecast materializes.

**TABLE 8
RETAILER CONFIDENCE IN MARSHFIELD***

	Index Value	
	September 2004	December 2004
Total Sales Compared to Previous Year	48	57
Store Traffic Compared to Previous Year	44	46
Expected Sales Three Months From Now	58	68
Expected Store Traffic Three Months From Now	58	64
100 = Substantially Better 50 = Same 0 = Substantially Worse *Data collected by UW Marshfield-Wood County		

Help wanted advertising is a good barometer of labor market conditions (Table 9). The index for the Marshfield area declined from 65 to 56 over the past twelve months while the national index remained virtually unchanged. The index for the Marshfield area indicates that the labor market was not as strong this year compared to last year. With the national and state economies forecasted to expand, improvement in the local labor market may be in the offing.

**TABLE 9
HELP WANTED ADVERTISING IN MARSHFIELD**

	Index Value	
	2003	2004
Marshfield (December) (1980 = 100)	65	56
U.S. (November) (1987 = 100)	38	36

Table 10 presents some good news for the area in terms of a reduction in family financial distress. Public Assistance claims on a monthly average basis declined from 104 to 91 or about 12.5 percent in our year over comparison. More good news comes in Table 11. Unemployment claims in Wood County are much lower than one year ago. New claims on a weekly average fell from 359 to 279 for a percentage decrease of 22.3. Likewise total claims dropped sharply from 1,670 to 1,247 or by 25.3 percent. Perhaps these measures of local family distress signal a more robust economic situation in the near future.

**TABLE 10
PUBLIC ASSISTANCE CLAIMS IN WOOD COUNTY**

	2003 Fourth Quarter (Monthly Avg.)	2004 Fourth Quarter (Monthly Avg.)	Percent Change
Total Caseload	104	91	-12.5

**TABLE 11
UNEMPLOYMENT CLAIMS IN WOOD COUNTY**

	2003 Fourth Quarter (Weekly Avg.)	2004 Fourth Quarter (Weekly Avg.)	Percent Change
New Claims	359	279	-22.3
Total Claims	1,670	1,247	-25.3

More good news is reported in Table 12. Residential construction in the area was significantly higher than last year at the same time. The number of new residential permits rose by 157 percent and the estimated value of the construction expanded by 205.9 percent. The number of housing units rose from 9 to 71 or by nearly 700 percent. Residential alteration permits issued, however, fell from 103 to 86 and the estimated value of this activity declined by 14.2 percent.

**TABLE 12
RESIDENTIAL CONSTRUCTION IN MARSHFIELD AREA***

	2003 Fourth Quarter	2004 Fourth Quarter	Percent Change
Residential Permits Issued	7	18	+157.1
Estimated Value of New Homes	\$1,325.0 (thousands)	\$4,053.2 (thousands)	+205.9
Number of Housing Units	9	71	+688.9
Residential Alteration Permits Issued	103	86	-16.5
Estimated Value of Alterations	\$614.3 (thousands)	\$527.0 (thousands)	-14.2
*Data collected by UW Marshfield-Wood County			

Table 13 lists nonresidential construction in the Marshfield area. Percentage changes are not given because of the volatile nature of this type of activity. The number of permits for new structures was 2 and their value was estimated at \$580 thousand. Business alteration permits reached 16 and the value associated with this activity was \$1.5 million.

**TABLE 13
NONRESIDENTIAL CONSTRUCTION IN MARSHFIELD AREA***

	2003 Fourth Quarter	2004 Fourth Quarter
Number of Permits Issued	5	2
Estimated Value of New Structures	\$2,947.3 (thousands)	\$580.0 (thousands)
Number of Business Alteration Permits	10	16
Estimated Value of Business Alterations	\$1,584.0 (thousands)	\$1,051.6 (thousands)
*Data collected by UW Marshfield-Wood County		

Table 14 and 15 presents data on Clark County. The major points of significance in the tables are as follows. Total employment expanded by an estimated 3 percent over the past twelve months. All business sectors expanded to some degree. The only exception to this was educational and health services, government, financial activities, and construction and natural resources. In addition total employment based upon a household survey suggests that total employment expanded by 0.6 percent. Lastly, the unemployment rate declined to 6.9 percent and the total number of unemployed dropped from 1,080 to 1,007.

**TABLE 14
CLARK COUNTY EMPLOYMENT CHANGE BY SECTOR**

	Employment December 2003 (Thousands)	Employment December 2004 (Thousands)	Percent Change
Total Nonfarm	10.0	10.3	+3.0
Total Private	7.8	8.0	+2.6
Construction & Natural Resources	0.6	0.6	0
Manufacturing	2.7	2.8	+3.7
Trade	1.3	1.4	+7.7
Transportation & Utilities	0.4	0.5	+25.0
Financial Activities	0.3	0.3	0
Education & Health Services	1.0	0.9	-10.0
Leisure & Hospitality	0.7	0.8	+14.3
Information & Business Services	0.7	0.8	+14.3
Total Government	2.2	2.2	0

TABLE 15
CLARK COUNTY EMPLOYMENT STATISTICS

	December 2003	December 2004	Percent Change
Unemployment Rate	6.6%	6.1%	-6.9
Total Employed	15,274	15,373	+0.6
Total Unemployed	1,080	1,007	-6.8
Labor Force	16,354	16,380	+0.2

A Report on the Solvency of the Social Security Combined Trust Funds and the Demographic Factors Influencing Future Fund Balances

Bruce W. Schultz
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INTRODUCTION

When the Social Security program was signed into law on August 14, 1935 it carried a provision that created the first Social Security Trust Fund and set forth a Board of Directors to oversee its operation. The Trust funds were deemed necessary as a cushion to allow payments between the quarterly deposits of FICA payroll tax.

The Board is composed of six members, four of whom serve automatically by virtue of their positions in the Federal Government: the Secretary of the Treasury, who is the Managing Trustee, the Secretary of Labor, the Secretary of Health and Human Services, and the Commissioner of Social Security. The other two members are appointed by the President and confirmed by the Senate to serve as public representatives.

The Board of Trustees reports each year on the current and projected financial condition of the Social Security program, which is financed through two separate trust funds. The Old-Age and Survivors Insurance (OASI) Trust Fund pays monthly benefits to retired workers and their families and to survivors of deceased workers. The Disability Insurance (DI) Trust Fund pays monthly benefits to disabled workers and their families.

The report on the current financial status of the funds includes an accounting of the actual income and expenditures for the last year. The projections for future years reflect the Trustees' considered judgment about all the demographic, economic, and program factors that affect income and expenditures. Projections are presented separately for the next 10 years (the short range) and for the next 75 years (the long range). All projections are based on current Social Security law and do not anticipate any future changes that Congress might make.

Because any projection of future experience is uncertain, the Trustees use three alternative sets of assumptions to show a range of possible outcomes. The intermediate set of assumptions, designated as alternative II, reflects the Trustees' best estimate of the trust funds' future financial outlook; the low cost alternative I is more optimistic, and the high cost alternative III more pessimistic. This writing is based on the 2004 Trustees report and will focus on the most likely assumptions, alternative II.

For the 2004 report, moving the valuation date from 2003 to 2004 has increased the program's actuarial deficit and unfunded obligation. Demographic, economic, and programmatic factors have also been updated with the most recently available information. Compared to the results shown in last year's report, projected annual

balances for the Social Security program (income minus costs) are somewhat improved for years after about 2045. Overall, the projected financial status of the program shows little change.

OVERVIEW

HIGHLIGHTS

The report's major findings are summarized below.

In 2003

At the end of 2003, 47 million people were receiving benefits: 33 million retired workers and their dependents, 7 million survivors of deceased workers, and 8 million disabled workers and their dependents. During the year an estimated 154 million people had earnings covered by Social Security and paid payroll taxes. Total benefits paid in 2003 were \$471 billion. Income was \$632 billion, and assets held in special issue U.S. Treasury securities grew to \$1.5 trillion.

Short-Range Results

The OASI and DI Trust Funds, individually and combined, are adequately financed over the next 10 years under the intermediate assumptions. The combined assets of the OASI and DI Trust Funds are projected to increase from \$1,531 billion at the beginning of 2004, or 306 percent of annual expenditures, to \$3,584 billion at the beginning of 2013, or 442 percent of annual expenditures in that year. Combined assets were projected in last year's report to rise to 309 percent of annual expenditures at the beginning of 2004, and 461 percent at the beginning of 2013.

Long-Range Results

Under the intermediate assumptions the combined OASI and DI Trust Funds are projected to become exhausted in 2042. For the 75-year projection period, the actuarial deficit is 1.89 percent of taxable payroll, 0.03 percentage point smaller than in last year's report. The open group unfunded obligation for OASDI over the 75-year period is \$3.7 trillion in present value, \$0.2 trillion more than the obligation estimated a year ago.

Between about 2010 and 2030, OASDI cost will increase rapidly due to the retirement of the large baby-boom generation. After 2030, increases in life expectancy and relatively low fertility rates will continue to increase Social Security system costs, but more slowly. Annual cost will exceed tax income starting in 2018 at which time the annual gap will be covered with cash from redeeming special obligations of the Treasury, until these assets are exhausted in 2042. Separately, the DI fund is projected to be exhausted in 2029 and the OASI fund in 2044.

Solvency

The combined OASDI Trust Funds are projected to become insolvent (i.e., unable to pay scheduled benefits in full on a timely basis) when assets are exhausted in 2042 under the long-range intermediate assumptions. For the trust funds to remain solvent throughout the 75-year projection period, the combined payroll tax rate could be increased during the period in a manner equivalent to an immediate and permanent increase of 1.89 percentage points, benefits could be reduced during the period in a manner equivalent to an immediate and permanent reduction of 12.6 percent, general revenue transfers equivalent to \$3.7 trillion (in present value) could be made during the period, or some combination of approaches could be adopted. *Significantly larger changes* would be required to maintain solvency beyond 75 years.

TRUST FUND FINANCIAL OPERATIONS IN 2003

The table below shows the income, expenditures, and assets for the OASI, the DI and the combined OASDI Trust Funds in calendar year 2003.

	Table 1.--Summary of 2003 Trust Fund Financial Operations		
	Amounts (in billions)		
	OASI	DI	OASDI
Assets at the end of 2002	\$1,217.5	\$160.5	\$1,378.0
Total income in 2003	543.8	88.1	631.9
Net contributions	456.1	77.4	533.5
Taxation of benefits	12.5	.9	13.4
Interest	75.2	9.7	84.9
Total expenditures in 2003	406.0	73.1	479.1
Benefit payments	399.8	70.9	470.8
Railroad Retirement financial interchange	3.6	.2	3.7
Administrative expenses	2.6	2.0	4.6
Net increase in assets in 2003	137.8	15.0	152.8
Assets at the end of 2003	1,355.3	175.4	1,530.8

Note: Totals do not necessarily equal the sums of rounded components.

In 2003, net contributions accounted for 84 percent of total trust fund income. Net contributions consist of taxes paid by employees, employers and the self-employed on earnings covered by Social Security. These taxes were paid on covered earnings up to a specified maximum annual amount, which was \$87,000 in 2003 and is increased each year automatically (to \$87,900 in 2004) as the average wage increases. The tax rates scheduled under current law for 2003 and later are shown in table 2.

Table 2.--Tax Rates for 2003 and Later			
	OASI	DI	OASDI
Tax rate for employees and employers, each (in percent)	5.30	0.90	6.20
Tax rate for self-employed persons (in percent)	10.60	1.80	12.40

Two percent of OASDI Trust Fund income came from subjecting up to 50 percent of Social Security benefits above a certain level to Federal personal income taxation, and 13 percent of OASDI income came from interest earned on investment of OASDI Trust Fund reserves. Social Security's assets are invested in interest-bearing securities of the U.S. Government. In 2003 the combined trust fund assets earned interest at an effective annual rate of 6.0 percent. More than 98 percent of expenditures from the combined OASDI Trust Funds in 2003 went to pay retirement, survivor, and disability benefits totaling \$470.8 billion. The financial interchange with the Railroad Retirement program resulted in a payment of \$3.7 billion from the combined OASDI Trust Funds, or about 0.8 percent of total expenditures. The administrative expenses of the Social Security program were \$4.6 billion, or about 1.0 percent of total expenditures.

Assets of the trust funds provide a reserve to pay benefits whenever expenditures exceed income. Assets increased by \$152.8 billion in 2003 because income to each fund exceeded expenditures. At the end of 2003, the combined assets of the OASI and the DI Trust Funds were 306 percent of estimated expenditures for 2004.

ASSUMPTIONS ABOUT THE FUTURE

The actual future income and expenditures of the OASI and DI Trust Funds depend on many factors, including the size and characteristics of the population receiving benefits, the level of monthly benefit amounts, the size of the work force, and the level of workers' earnings. These factors will depend in turn upon future birth rates, death rates, immigration, marriage and divorce rates, retirement-age patterns, disability incidence and termination rates, productivity gains, wage increases, inflation, and many other demographic, economic, and program-specific factors.

Assumptions are reexamined each year in light of recent experience and new information. This careful review and updating of the assumptions on an annual basis helps ensure that they provide the Trustees' best estimate of future possibilities.

PROJECTIONS OF FUTURE FINANCIAL STATUS

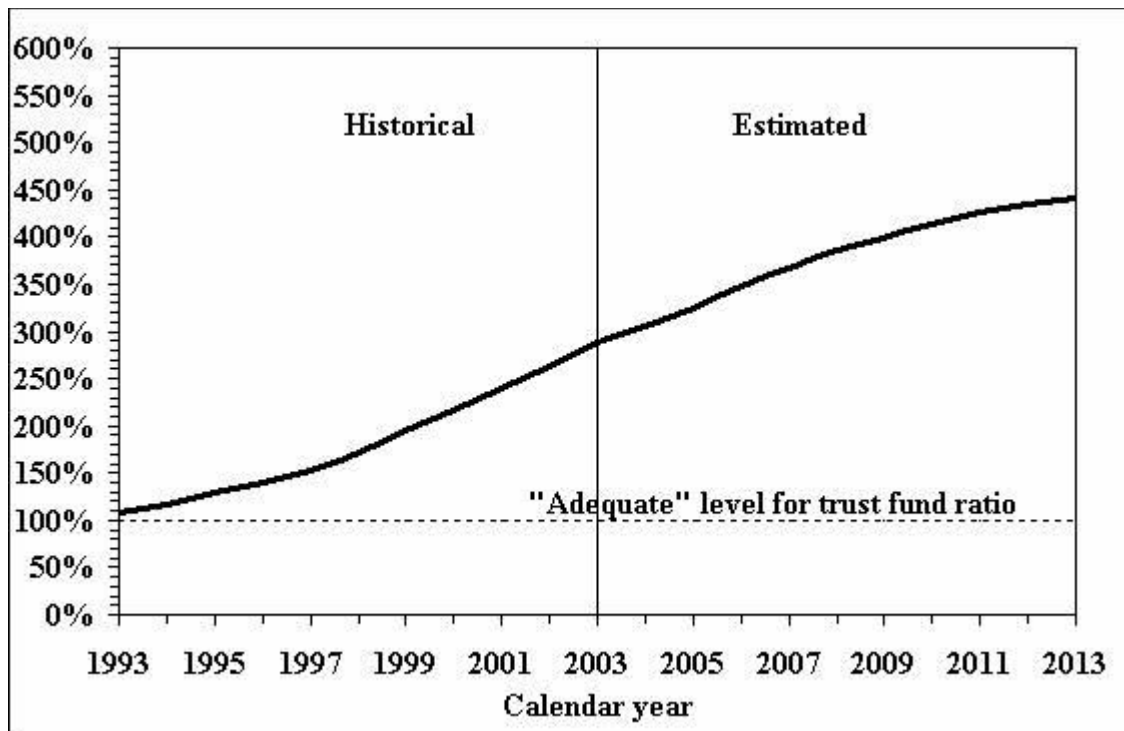
Short-Range Actuarial Estimates

For the short range (2004-2013), the Trustees measure trust fund adequacy by comparing assets at the beginning of each year to projected program cost for that year under the intermediate set of assumptions. Having a trust fund ratio of 100 percent or more--that is, assets at the beginning of each year at least equal to projected outgo during the year--is considered a good indication of a trust fund's ability to cover most short-term contingencies. Both the OASI and the DI trust fund ratios under the

intermediate assumptions exceed 100 percent throughout the short-range period and therefore satisfy the Trustees' short-term test for financial adequacy. Figure 3 below shows the trust fund ratios for the combined OASI and DI Trust Funds for the next 10 years.

Figure 3.--Short-Range OASDI Trust Fund Ratios

[Assets as a percentage of annual expenditures]



Long-Range Actuarial Estimates

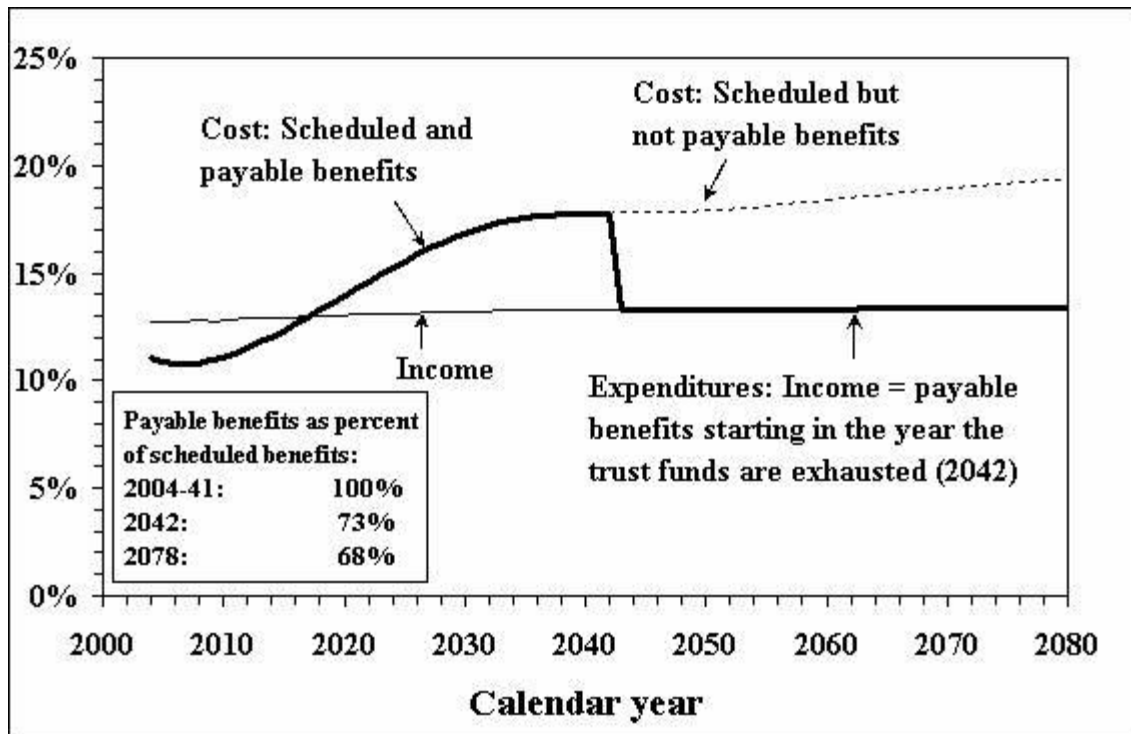
The financial status of the trust funds over the next 75 years is measured in terms of cost and income as a percentage of taxable payroll, trust fund ratios, the actuarial balance (also as a percentage of taxable payroll), and the open group unfunded obligation (expressed in present-value dollars).

The year-by-year relationship between income and cost rates shown in figure 4 illustrates the expected pattern of cash flow for the OASDI program over the full 75-year period. Under the intermediate assumptions, the OASDI cost rate is projected to decline slightly between 2004 and 2007 and then increase up to the current level within the next 3 years. It then begins to increase rapidly and first exceeds the income rate in 2018, producing cash-flow deficits thereafter. Despite these cash-flow deficits, beginning in 2018, redemption of trust fund assets will allow continuation of full benefit payments on a timely basis until 2042, when the trust funds will become exhausted. This redemption process will require a flow of cash from the General Fund of the Treasury. Pressures on the Federal Budget will thus emerge well before 2042. Even if a trust fund's assets are

exhausted, however, tax income will continue to flow into the fund. Present tax rates would be sufficient to pay 73 percent of scheduled benefits after trust fund exhaustion in 2042 and 68 percent of scheduled benefits in 2078.

Figure 4.--OASDI Income and Cost Rates Under Intermediate Assumptions

[As a percentage of taxable payroll]



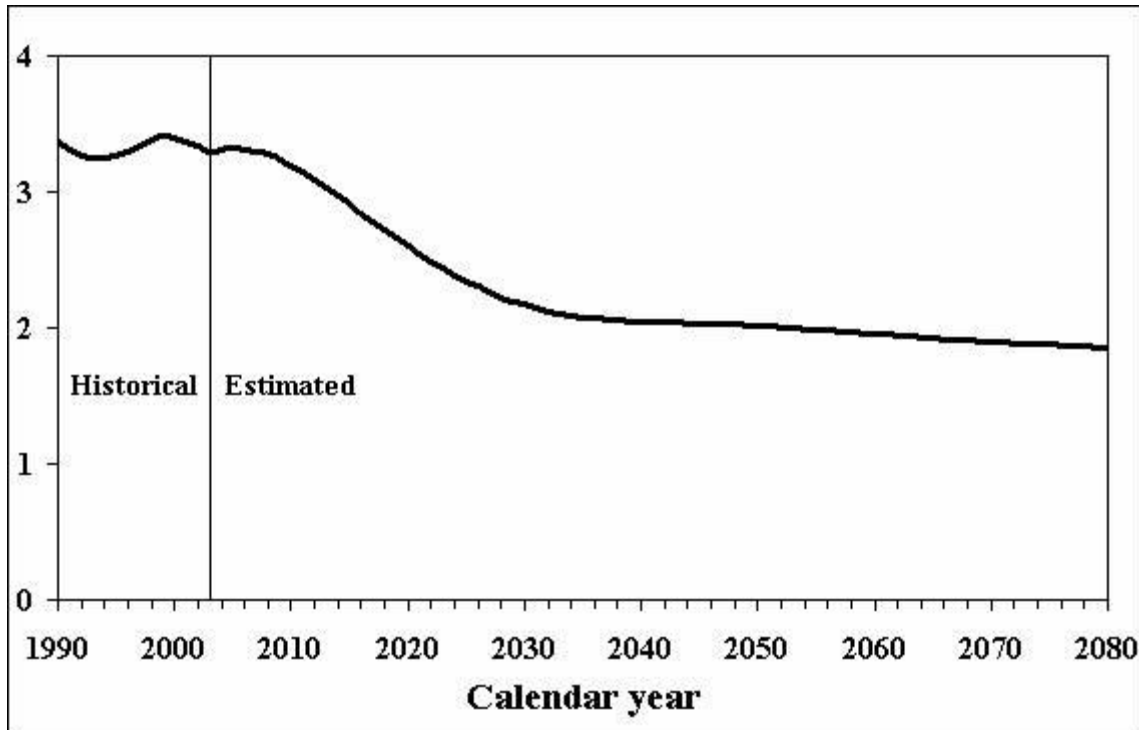
Social Security's cost rate generally will continue rising rapidly through about 2030 as the baby-boom generation reaches retirement age. Thereafter, the cost rate is estimated to rise at a slower rate for about 15 years as the baby boom ages and begins to decrease in size. Continued reductions in death rates and relatively low birth rates will cause a significant upward shift in the average age of the population and will push the cost rate above 19 percent of taxable payroll by 2078 under the intermediate assumptions.

In a pay-as-you-go system such as OASDI, this 19-percent cost rate means the combination of the payroll tax (scheduled to total 12.4 percent) and proceeds from income taxes on benefits (expected to be 1.0 percent of taxable payroll in 2078) would have to equal more than 19 percent of taxable payroll to pay all currently scheduled benefits. After 2078, the upward shift in the average age of the population is likely to continue and to increase the gap between OASDI costs and income.

The primary reason that the OASDI cost rate will increase rapidly between 2010 and 2030 is that, as the large baby-boom generation born in the years 1946 through 1964 retires, the number of beneficiaries will increase much more rapidly than the number of

workers. The estimated number of workers per beneficiary is shown in figure 5. In 2003, there were about 3.3 workers for every OASDI beneficiary. The baby-boom generation will have largely retired by 2030, and the projected ratio of workers to beneficiaries will be only 2.2 at that time. Thereafter, the number of workers per beneficiary will slowly decline, and the OASDI cost rate will continue to increase.

Figure 5.--Number of Covered Workers Per OASDI Beneficiary



The maximum projected trust fund ratios for the OASI, DI, and combined funds appear in table 6. The chart also contains the year in which the maximum projected trust fund ratio is attained and the years in which the assets are projected to be exhausted.

	OASI	DI	OASDI
Maximum trust fund ratio (percent)	500	226	448
Year attained	2015	2006	2015
Year of trust fund exhaustion	2044	2029	2042

The actuarial balance is a measure of the program's financial status for the 75-year valuation period as a whole. It is essentially the difference between income and cost of the program expressed as a percentage of taxable payrolls over the valuation period. This single number summarizes the adequacy of program financing for the period.

When the actuarial balance is negative, the actuarial deficit can be interpreted as the percentage that would have to be added to the current law income rate in each of the next 75 years, or subtracted from the cost rate in each year, to bring the funds into actuarial balance. In this report, the actuarial balance under the intermediate assumptions is a deficit of 1.89 percent of taxable payroll for the combined OASI and DI Trust Funds. The actuarial deficit was 1.92 percent in the 2003 report and has been in the range of 1.86 percent to 2.23 percent for the last ten reports.

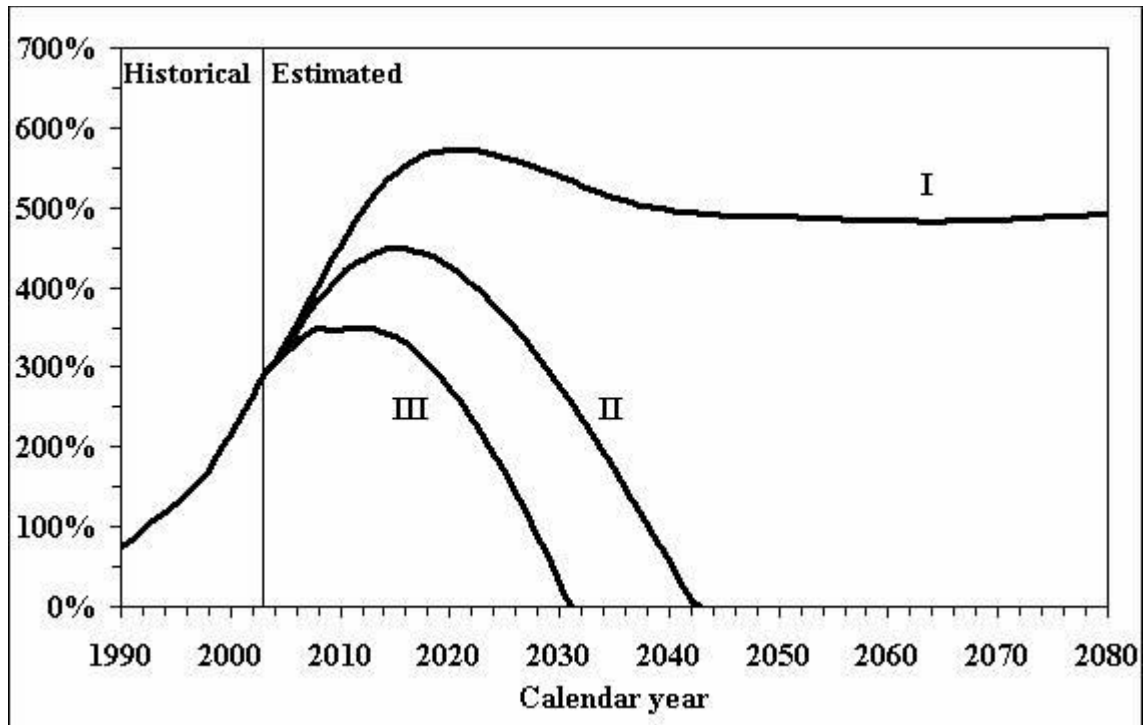
Even a 75-year period is not long enough to provide a complete picture of Social Security's financial condition. Overemphasis on summary measures for a 75-year period can lead to incorrect perceptions and to policy prescriptions that do not move toward a sustainable system. Thus, careful consideration of the trends in annual deficits and unfunded obligations toward the end of the 75-year period is important. In order to provide a more complete description of Social Security's very long-run financial condition, the Trustees Report also includes summary measures for a time period that extends to the infinite horizon. These calculations show that extending the horizon beyond 75 years continues to increase the unfunded obligation, indicating that much larger changes would be required to achieve solvency over the infinite future as compared to changes needed to balance 75-year period summary measures.

Uncertainty of the Projections

Significant uncertainty surrounds the intermediate assumptions. The Trustees have traditionally used low cost (alternative I) and high cost (alternative III) assumptions to indicate this uncertainty. Figure 7 shows the projected trust fund ratios for the combined OASI and DI Trust Funds under the intermediate, low cost, and high cost assumptions. The low cost alternative is characterized by assumptions that improve the financial condition of the trust funds, including a higher fertility rate, slower improvement in mortality, a higher real-wage differential, and lower unemployment. The high cost alternative, in contrast, features a lower fertility rate, more rapid declines in mortality, a lower real-wage differential, and higher unemployment.

Figure 7.--Long-Range OASDI Trust Fund Ratios Under Alternative Assumptions

[Assets as a percentage of annual cost]



These three alternatives have traditionally been constructed to provide a reasonable range of possible future experience. However, these alternatives do not address the probability that actual experience will be within or outside the range. As an additional way of illustrating uncertainty, the Trustees Report includes estimates from a model of the trust funds that provides a probability distribution of possible future outcomes. The results of this model suggest that outcomes better than the traditional low cost alternative and outcomes worse than the high cost alternative have very low probabilities of occurring.

CONCLUSION

Under current law the cost of Social Security will increase faster than the program's income, because of the aging of the baby-boom generation, expected continuing low fertility, and increasing life expectancy. Based on the Trustees' best estimate, program cost will exceed tax revenues starting in 2018 and throughout the remainder of the 75-year projection period. Social Security's combined trust funds are projected to allow full payment of benefits until they become exhausted in 2042. At that time annual tax income to the trust funds is projected to equal about 73 percent of program costs. Separately, the OASI and DI funds are projected to have sufficient funds to pay full benefits on time until 2044 and 2029, respectively. By 2078, however, annual tax income is projected to be only about two-thirds as large as the annual cost of the OASDI program.

Over the full 75-year projection period the actuarial deficit estimated for the combined trust funds is 1.89 percent of taxable payroll--slightly lower than the 1.92 percent deficit

projected in last year's report. This deficit indicates that financial adequacy of the program for the next 75 years could be restored if the Social Security payroll tax were immediately and permanently increased from its current level of 12.4 percent (for employees and employers combined) to 14.29 percent. Alternatively, all current and future benefits could be immediately reduced by about 13 percent. Other ways of reducing the deficit include making transfers from general revenues or adopting some combination of approaches.

- If no action were taken until the combined trust funds become exhausted in 2042, much larger changes would be required. For example, payroll taxes could be raised to finance scheduled benefits fully in every year starting in 2042. In this case, the payroll tax would be increased to 16.91 percent at the point of trust fund exhaustion in 2042 and continue rising to 18.31 percent in 2078.
- Similarly, benefits could be reduced to the level that is payable with scheduled tax rates in every year beginning in 2042. Under this scenario, benefits would be reduced 27 percent at the point of trust fund exhaustion in 2042, with reductions reaching 32 percent in 2078.

Changes of this magnitude would eliminate the actuarial deficit over the 75-year period through 2078. However, because of the increasing average age of the population, Social Security's annual cost will very likely continue to exceed tax revenues after 2078. As a result, ensuring the sustainability of the system beyond 2078 would require even larger changes than those needed to restore actuarial balance for the 75-year period.

The projected trust fund deficits should be addressed in a timely way to allow for a gradual phasing in of the necessary changes and to provide advance notice to workers. The sooner adjustments are made the smaller and less abrupt they will have to be. Social Security plays a critical role in the lives of over 47 million beneficiaries, and 156 million covered workers and their families. With informed discussion, creative thinking, and timely legislative action, we will ensure that Social Security continues to protect future generations.

For further information related to the contents of this report, see the following websites.

- www.socialsecurity.gov/OACT/TR/TR04/index.html
- www.cms.hhs.gov/publications/trusteesreport/
- www.treas.gov/offices/economic-policy/social_security.html