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Saving Social Security

By Valerie A. Ramey, Professor of Economics, UCSD



Professor Valerie Ramey

This year, politicians have found the courage to touch the “third rail” of American politics - Social Security. As anticipated, sparks are flying. Private accounts, re-indexing, raising retirement ages, and raising taxes are just some of the policies being discussed as ways to “save Social Security.” The details and conflicting forecasts are enough to confuse even the most informed citizen.

Historically, Social Security has worked as a pay-as-you-go system. Workers produced output, the government took a portion (by the payroll tax), and immediately gave it to the current retirees (in the form of Social Security benefit checks). Contrary to popular belief, the Social Security Administration did not “save” the worker’s income for his retirement.

Social Security worked well in the past because many workers supported each retiree. In 1946, 42 workers paid taxes to support one Social Security recipient. In 1960, there were nine workers for every retiree. By 2030, there will be only two workers supporting each Social Security recipient. Why is the ratio of workers to retirees declining so dramatically? First, people are living longer, so they are spending a greater fraction of their life being retired. Second, people are having fewer children, so the population of workers is growing more slowly. This fundamental demographic fact is the culprit behind the predictions that the Social Security Trust Fund will begin paying out more than it is taking in by 2017 and will be insolvent by 2041.

There are two parts to dealing with the problem. First, we can ensure that even with relatively fewer workers, living standards can be maintained. As long as labor productivity continues to grow at current rates, having fewer workers per retiree does not imply a decrease in the standard of living relative to today. One way to ensure that future workers are very productive is to invest in human and physical capital today. The second part to dealing with the decline in the worker-retiree ratio is to decide how goods will be divided fairly between workers and retirees. Relative to the current promises, either benefits must be cut or taxes must be raised.

With these issues in mind, it becomes easier to assess the fundamental effects of the various proposed policies, though the indirect effects are more complicated to assess.

Increase the retirement age. This directly addresses the problem of too few workers per retiree by decreasing the number of retirees at any point in time. This policy amounts to a decrease in promised benefits because it decreases the average number of years that retirees can collect benefits.

Change Social Security indexing. Currently, each generation of Social Security recipients receives benefits higher --- in purchasing power --- than the last, because their real (purchasing power) wages are higher. Their starting benefits adjust not only for inflation but also for increased labor productivity. Holding the purchasing power of benefits fixed at current levels --- indexing Social Security benefits to inflation only rather than to real wages --- would cut future retiree benefits enough so that taxes would not have to be raised.

Raise Social Security taxes. Since future workers are expected to be more productive, the government could simply make them share a greater amount of their income by raising their taxes. One disadvantage of this policy is that it might make people work less because their tax rates will be so high. Some economists believe that this policy could make the problem worse.

Privatize Social Security accounts. This proposal is very complicated and can have many subtle effects. At its core, though, it does not address the underlying problem of too few workers per retiree. It is very likely that this proposal would result in a decrease in benefits received by retirees relative to what is promised now. It is unlikely that private accounts would earn substantially higher returns than beneficiaries are implicitly receiving now. Currently retirees are earning two to five times what they contributed plus interest.

In any case, the sparks are sure to continue to fly as the nation debates needed reforms in one of its most beloved government programs.

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Chair's Corner



Professor Richard Carson

The Envelope, Please! Good News!

By Richard T. Carson,
Professor and Chair
UCSD Economics Department

In the annual *US News and World Report* 2005 ranking of US Economics graduate programs (now on the web, hard copy in 2006), UCSD Economics was named the **tenth** (10th) ranking economics PhD. program in the US. That's up from seventeenth in 2001, and second only to UC Berkeley in public universities. We even nosed out our sister campus, UCLA. UCSD is by decades the youngest of the top ten economics PhD programs.

There was special recognition of UCSD's leading role in econometrics (statistical analysis of economic data), ranking UCSD number 2 in that specialty, right after MIT. Additional specialties ranked were microeconomics (prices, markets, economic theory) 12th, public finance (taxation and government programs) 13th, macroeconomics (unemployment, inflation, business cycles) 16th, and international economics 16th.

The survey is based on questionnaires distributed to department chairs and graduate study directors at leading economics programs throughout the country.

US News and World Report Rankings: Economics

1. Massachusetts Institute of Technology
University of Chicago
3. Harvard University (MA)
Princeton University (NJ)
Stanford University (CA)
University of California, Berkeley
7. Yale University (CT)
8. Northwestern University (IL)
9. University of Pennsylvania
10. **University of California, San Diego**
11. Columbia University (NY)
University of California, Los Angeles
University of Michigan, Ann Arbor
University of Wisconsin, Madison
15. New York University
University of Minnesota, Twin Cities

Meanwhile, the June, 2005, Ph.D. graduates of UCSD Economics are spreading their knowledge of economics throughout the world. They are assuming faculty and research positions at: University of California Riverside, Rutgers University (the state University of New Jersey), *Instituto Tecnológico Autónoma de México* (ITAM, Mexico City), the Central Bank of Mexico, University of Technology (Sydney, Australia), The Bank of Mexico (Mexico City), State University of New York (SUNY, Albany), Central Bank of Venezuela. Recent graduates are moving to new positions including: Stanford University, University of North Carolina, Federal Reserve Bank of St. Louis.

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Melissa Famulari: Organizing Life and Career with Economics



Dr. Melissa Famulari, LPSOE

By Barry Jagoda
UCSD Communications

"I view life as a very long race, more like a marathon than a sprint. You want to be sure you are doing something you like and that you are good at: these tend to be related," is the way Economics Department Vice Chair for Undergraduate Education, Melissa Famulari expresses a central career lesson, one she has practiced and that she tries to communicate to undergraduates.

When she moved from a small Pennsylvania town near Valley Forge to attend Temple University in Philadelphia, Melissa started out as a communications major. "I used to read for the blind and everybody said I had a clear voice," she says. She still has a clear voice but it is now heard in the classrooms of UCSD, where, as "Lecturer With Potential Security of Employment" (which means tenure track), Melissa speaks the language of Intermediate Microeconomics and Health Economics, subjects of her specialty.

It was at Temple that Melissa discovered an interest and aptitude for tackling big problems. As an undergraduate she became deeply engaged by the problem of discrimination. As she explains, "I traveled in the summer to Europe and visited Austria where I realized there was discrimination against Arab workers. I had thought discrimination was only a problem in America. Since dislike of someone because of the way they look exists in many countries, it seemed to me that there must be an underlying model that could explain this phenomenon. When I got back to school I began to see that there might be answers in economics."

As a Phi Beta Kappa graduate of Temple, Melissa had numerous choices for graduate school but she chose The University of Washington, because she was attracted by the research of several professors. Although she remembers that first year as intensely rigorous, there was also time for some of her favorite outdoor hobbies, including rock climbing, kayaking and sailing.

Melissa decided to focus on labor economics and Washington had just hired Shelly Lundberg, a prominent labor economist, who became her thesis supervisor. She explains, "For my thesis I focused on discrimination against people with epilepsy. At that point there was legislation prohibiting discrimination against the disabled, but there was little study of the subject. I surveyed people with epilepsy about their job experiences and used their medical information to determine the individual's loss of productivity due to the illness. I also added a concentration in health economics, which was a new field at the University of Washington."

After graduate school Melissa had to select between academic jobs at Wellesley and Florida State or going to work in Washington for the U.S. Department of Labor's Bureau of Labor Statistics (BLS). The job at the BLS looked attractive particularly since she was offered a position that would permit her to work on her own research half-time and half-time on chores specifically designated by BLS. This choice resulted in five satisfying years and, most important, gave Melissa the chance to design a survey to collect information from business establishments about the people who work there. (Most data about individuals is collected from households.) This was a treasure-trove for a labor economist yielding studies and papers for Melissa on such topics as "employee and employer profitability and worker pay," "employer provided training," "wage-growth variations" and other subjects.

From the BLS, Melissa moved to the University of Texas where she lectured and continued her research on people with epilepsy with a grant from the Epilepsy Foundation of America to estimate the costs of epilepsy in the United States. She also had two children, Toni, now 7,

Nir Jaimovich: Focusing on Macroeconomics and the Real World



Professor Nir Jaimovich

By Barry Jagoda
UCSD Communications

Born and raised in Israel, of Argentinean parents who had immigrated in their early 20s, Assistant Professor of Economics Nir Jaimovich, remembers that early family discussions very often included questions about what makes national economies particularly those of developing countries grow and expand. "Growth is in my heart," he explained, but after undergraduate

work in economics, several years of graduate school leading to a master's degree and finally Ph.D work at Northwestern University, Nir joined UCSD as a macroeconomist specializing in the business cycle.

From a background in socialist-oriented Israel this new focus seemed puzzling to some who knew him well. "What is this business-cycle?" asked his mother, herself a professor of education at a leading Israeli University. Nir remembers being a bit sheepish answering her with, "Well, it helps to explain unemployment."

Now this highly regarded specialist not only has a lot to teach, but is himself deeply engaged with numerous compelling research projects. Nir says he came away from graduate school with the life-long professional lesson to "be focused and keep doing the things you know."

Thus, this winter Professor Jaimovich offered his first UCSD graduate class in macroeconomics on "Business Cycle Research," with 12 students. "We were focusing on the tools of the trade, how to think about developing theories and confront them with the data. I found it very satisfying and the students seemed to benefit," reflected Nir. And the syllabus outline from his undergraduate course on intermediate macroeconomics, points in the direction of his interests: Growth, Business Cycle, Unemployment, Inflation, Interest Rates, and more.... "I am trying to show my undergraduates that what they are studying is really related to the real world, to what is seen on the news and in our everyday lives," Nir explained.

Asked if he is finding promise in his research, Nir says, "I am very engaged with my field of macroeconomics and I'm glad to be working on business cycles and that is where I intend to stay focused."

In fact, after a year in economics graduate school at Hebrew University most of his professors said that if he was deeply interested in research he needed to go to the United States, where the best research was being done. Another looming factor was the continuing tension in Israel, the result of Middle East conflict. Though he clearly loves the land of his birth, it seems natural that, as Nir implies, work and productivity comes much easier in a more relaxed environment.

Upon matriculating at Northwestern he quickly realized there was a new world of economics to be discovered. Instead of focus upon the question of why some nations grow faster than others Nir's energies turned to "business cycle research." Within a short while he had become discouraged with the research possibilities on growth, explaining, "It was an area that had gotten a lot of attention in the 80s and 90s and I began to think there were serious concerns with the availability of reliable macro data."

Answers, Nir began to think, could be found by "deconstructing the 'black box' of business cycles and what drives them?" For example, he says, "One question I have worked on is "What is the impact of firms entering and leaving a particular segment of the market and how might this interaction help us better understand the business cycle phenomenon?" I have also worked on the questions of how "optimism" and "pessimism" among consumers gives rise to macroeconomic fluctuations."

Recently Nir has been thinking about one of the big questions in

macroeconomics: what causes recessions? "99% of economists would say, 'We are not exactly sure, we are still searching for an explanation,' but a colleague from Northwestern and I are speculating that a recession is just a natural consequence of not having the most precise information about the future. This suggests that there is a natural expectation of some result and, even if the business is successful, when an imagined target is not met this often causes a scaling back which, in the aggregate, can lead to recession."

He adds, "I'm also working on the relationship between monopolies and their impact on the adoption of new technologies in the market, and how this interaction might reduce productivity or growth." The list of questions goes on, and, tempered by training, Nir is content to go deeper and deeper into this and other macroeconomics issues.

Now 32 and settled into San Diego with a residence in North Pacific Beach Nir says, "I feel great here with a good-sized cohort of assistant professors who I enjoy and I'm working with senior colleagues from whom I'm learning a lot. I'm very pleased to have come to UCSD."

But, even before the passions and demands of economics reach a boiling point, a whole different personality emerges. There is the Nir Jaimovich who actually played soccer on a professional Israeli club team. The same Nir who took a year off after three years of required Israeli military duty (he was in the intelligence service) for traveling in Chile and Argentina. A hiker and trekker, Nir is a passionate basketball fan with personal web site links to four Israeli papers and four Argentine papers.

That other Nir knows that there is life beyond economics, but he is happy in his UCSD present. He's a modest guy but, in a recent interview, he let slip evidence of confidence derived from his heritage. Asked how his parents assess his current life Nir smiled and said, "Well, my Dad has a strong view. He told me, "As a soccer player you would have played in one of the best teams in the world. As an Economist, you didn't fall short...".

Famulari from page 2

and Matt, who is 6. She lived in Austin, Texas from 1992 until being recruited by UCSD in 2004.

Melissa is delighted to be at UCSD, "This is a great department and I'm proud to have my name on the door next to so many illustrious colleagues. I have also found most of the students to be excellent. This is a great time for my teaching and research, since both of the kids are now in school."

In her role as Vice Chair for Undergraduate Education, Melissa devotes a great deal of energy to the undergraduates. "We have a large department with many students. There has always been a faculty member in this job, and the Department feels strongly that it must be a faculty member's job to oversee the undergraduate economics program. I'm enjoying the work and feel that it is important."

When discussing research on her agenda, Melissa is very specific: "First, I have a wealth of data on people with epilepsy. I am examining whether people with epilepsy experience "job lock," which is when people remain on their jobs to keep their health insurance. I am also looking at the effect of the age of epilepsy onset on labor market performance.

Second, I am interested in the transition from not-for-profit hospitals to for-profit entities. Very specifically, I'm wondering how immigrant populations have affected this transition here in California and the Southwest. And there is other existing research."

Asked to sum up Melissa says, "I have found that economics is a great way for me to organize my thoughts. This field is very useful: it forces you to think about what questions you want to ask and how to go about finding supportable answers."

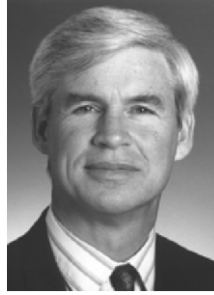
There we leave the story, on track and much of the long race to be run.

UCSD Economics Roundtable

"A Brief History of Time Series: What Makes UCSD Economics Great"



Professor Clive Granger



Professor Robert Engle

In 2003, UCSD professors Clive Granger and Robert Engle received Nobel Prizes in Economics for their pioneering work in Econometrics, statistical modeling of economic data. Granger and Engle are internationally known for their focus on "time-series econometrics," the analysis of data that accrues over time, such as interest rates, stock market averages, electricity prices, or GDP.

When: 7:30 - 9:00am, Wednesday, July 13th

Where: UCSD Faculty Club

Registration required. Contact Edie Munk at (858)822-0510, or emunk@ucsd.edu for more information. For upcoming events, please click <http://econ.ucsd.edu/roundtable/index.html>.

Alums, let us know where you are and what you're doing. Email your information to: econnews@econ.ucsd.edu

Alumni News

Michael S. Kim, CFA CPA, Economics, '91. "I now live in Portland, OR, working for PPM Energy as the Manager of Risk Analytics and Development for merchant energy trading activities. I develop risk measurement tools and analyze market risks for merchant energy trading activities. My Economics/Econometrics courses at UCSD really prepared me well for all the quantitative work that I do on a daily basis. Mindy (wife), Hailey, Emily and I enjoy living in the Pacific Northwest, but we really miss San Diego." Michael earned his MPA from the University of Texas, Austin, in 1994.

Stephen J. Huxley, PhD, '75. "I entered the UCSD PhD program in 1966 and was the 13th graduate of the program in 1975. I bet Richard Attiyeh and Ramu Ramanathan remember me!" Stephen published, with co-author J. Brent Burns, *Asset Dedication: How to Grow Wealthy with the Next Generation of Asset Allocation*, through McGraw-Hill last year. He is a Professor of Information and Decision Sciences for School of Business and Management University of San Francisco.

Andrew Betz, Management Science, '00. "I am at USC's Marshall School of Business pursuing an MBA with an expected graduation of May 2006. Prior to business school, I was a traveling consultant with Stockamp & Associates, which I got through on-campus recruiting during my senior year...I just got married to a fellow UCSD graduate (Ya-Lei Yang, Communications at Muir 2000) on October 15th. The ceremony was in Rancho Palos Verdes and because of my school schedule we have yet to take a honeymoon but plan to take one soon!"

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