How U.S. Governments Understate Inflation to Lower Payouts for Social Security and Other Entitlements

Bonanza! The 2015 1.7% Social Security Cost-of-Living-Adjustments (COLA)

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Global Research, January 07, 2015
Activist Post
Region: USA
Theme: Global Economy

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Seniors on Social Security are no doubt celebrating after learning that, come January 2015, their payouts will go up a whopping 1.7%. By federal law, Cost-of-Living-Adjustments (COLA) link to the inflation rate of the Wages Consumer Price Index (CPI-W). In 1975, when Social Security disbursed the first COLA, recipients got an 8% raise.

A 2015 COLA of less than 2% is based on the current rate of CPI-W inflation. Yet, how is it possible for inflation to be this low when everyone experiences the meteoric rise in the price of the most basic goods and services? For example, between September 2013 and September 2014, the cost of food (eating at home via grocery stores) increased 3.2% according to the U.S. Department of Agriculture Economic Research Service. Additionally, the National Energy Assistance Director's Association, (NEADA), projects that heating costs will rise an average of 10.5% for Americans during the winter 2014-2015. Not to mention, the skyrocketing costs of medical services and health insurance.

Beneficiaries of an 8% Social Security COLA in 1975 paid a whole lot less for everything than do the beneficiaries of the 2015 1.7% COLA. An item costing $100 in 1975 in 2014 costs $442.00 (Bureau of Labor Statistics inflation calculator) and in 2015, that same item will cost even more. The increase in the cost-of-living comes as no surprise to Americans who need credit just to make ends meet. It just does not add up.

For the retired worker in 2014, the Social Security website says the average monthly check is $1,294. Pretty scary. How can a 1.7% COLA help seniors to meet even the most basic costs of food and energy? The short answer? It cannot.

The longer answer confirms what many suspect: Not only is this 1.7% increase insufficient, but it does not accurately reflect actual inflation. Economist John Williams tells the whole story, and proves that the real rate of inflation in 2014 would be 9.4% if it were not for what he calls "governments gimmicks for understanding inflation." On his website, ShadowStats.com, he wrote this back when G.W. Bush was president:

- During the Kennedy administration, unemployment was redefined with the concept of "discouraged workers" to reduce the unemployment rate.
- If Lyndon Johnson didn't like the growth that was going to be reported in the GNP, he sent it back to the Commerce Department, and he kept doing so until

Commerce got it right.
- The Carter administration was caught deliberately understating inflation.
- The first Bush Administration began efforts at the systematic reduction of the reported rate of CPI inflation.
- The current Bush administration has expanded upon the Clinton era … setting the stage for the adoption of a new and lower-inflation CPI.

One cannot help but wonder why, for decades, administrations have focused on "new and lower-inflation CPI." Might self-interest cloud the government's purpose for keeping the official CPI low? Consider this: The lower the inflation calculation, the lower the COLA payouts for Social Security and other entitlements.

Why Saving Money is Difficult

What's more crazy is thinking about how the next generation will be able to retire. A recent Wells Fargo Bank survey of middle-class Americans was released October 22, 2014. Below are some of the highlights of "Wells Fargo Survey Finds Saving for Retirement Not Happening for a Third of Middle Class."

- Over 70% don't think Social Security will be their primary revenue source yet 46-56% of respondents, not yet on Social Security between ages 50 and 75, do believe it will be their primary source.
- 30% said they will probably need to work in a traditional setting until 80 years of age.
- 68% stated that saving was harder than they expected with 34% not participating in any form of retirement savings.
- Across all age groups was the expectation of needing $250,000 for retirement.
- There was a lack of confidence (over 50%) across all age groups of being able to live the life they wanted in retirement. The percentage rose to over 70% for those 50-59 years old.
- 25% said they feel depressed when thinking about their financial life in retirement with 22% saying they would prefer to die early.

The banks want you to start saving when you are young (with them, of course) so you can successfully meet your retirement goals. They somehow forget to factor-in that today's cost-of-living prohibits many families from being able to save unless earnings put into savings are offset by increased credit access. And also, what they never tell you is the degree to which you will suffer the loss of purchasing power once you access retirement funds. They, too, rely on the official (low) CPI calculations.

What Lies Ahead?

Unfortunately, the imminent future of Social Security appears dismal, especially as the government has been scrambling since the 2008 economic meltdown. Congress has been discussing how the government could lower its financial obligation to Social Security while continuing to make guaranteed monthly payments and COLAs. The option most mentioned is about changing how COLAs are calculated. By un-linking the COLA to the CPI-W index and instead linking it to an index called "chained CPI," the government would slow the rate at which benefits increase, and thereby, save billions. Given the 2014 election year, chained CPI remains on the back burner but is said likely to resurface.

> There had been proposals, for example, by the Bowles-Simpson deficit reduction commission in 2010 and by President Obama in the budget he proposed for 2014, to change the index for computing COLA. Instead of the CPI-W, the proposal is to use the chained CPI. This index usually rises more slowly than does the CPI-W, potentially saving billions of dollars for the federal budget through smaller increases in Social Security benefits for years to come. – Polina Vlasenko, PhD, Senior Research Fellow, COLA to Exceed 2014 Increase, American Institute for Economic Research (AIER), October 15, 2014

How would this shift change things for the beneficiary? The good news first. If, and once the index transitions to the chained CPI, initially, a beneficiary's check will end up showing only a slight amount less than with the current CPI-W index calculation. But as you probably have already guessed, the beneficiary ultimately ends up with the short end of the stick. Though the initial loss is negligible, the cumulative loss over the long term brings the bad news. This same AIER article continues:

> The cumulative effect of 10 years of lower COLAs would be Social Security benefits about 3 percent lower than they are today. The average Social Security benefit of a retired worker in 2014 is $1,294 per month. Had the COLAs for the past 10 years been based on the chained CPI, the same average benefit would have been $1,256, which is $39 per month lower.

The article concludes with the recommendation of yet another CPI, "the experimental CPI-E," for Americans 62 years and older who "spend more on medical care and housing, but less on education, communication, food, and transportation." Most likely, this experimental index would also reflect the government's goal of keeping the official CPI artificially low.

With the geometrical loss of purchasing power, the government formula for your later year's financial well-being leaves you begging. The only way most Americans will be able to thrive throughout their retirement is if they plan for and develop additional streams of revenue, and the sooner the better. We are on our own to see the future realistically and plan for it accordingly. Reinspirement™ is an idea whose time has definitely come.

***Susan Boskey** is author of the book, The Quality Life Plan®: 7 Steps to Uncommon Financial Security. The information in the book not only exposes the systemic-root cause of the 2008-09 economic meltdown but, perhaps more importantly, provides critical steps to help everyday people turn the tide and build real wealth. To learn more or to purchase the book, visit her website at http://TheQualityLifePlan.com*