

Privatization of social security – how it works and why it matters?

Laurence Kotlikoff

The study uses the Auerbach-Kotlikoff Dynamic Life-Cycle Model (AK Model) to examine the macroeconomic and efficiency effect of privatizing social security. It proposes a simple privatization method, the Personal Security System, as a framework to discuss some issues associated with the privatization of social security, including transition rules and changes in the overall degree of progressivity.

According to the AK Model's simulations, privatizing social security can generate major long-run increases in output and living standards. These gains materialize mostly, though not exclusively, at the expense of coexisting generations. Pure efficiency gains from privatization can be substantial. These consist in the welfare improvements available to future generations after full compensation of existing generations for their losses from privatization. The precise size of the efficiency gain depends on the existing tax structure, on the linkage between taxes (wage contributions) and expenditures under the existing social security system, and the choice of instruments to finance benefits during the transition.

The illustrative Personal Security System shows that there are several ways to privatize the retirement portion of the U.S. Social Security System and to credit workers for their past social security contributions. However, the analysis also suggests that the gains from privatization must be set against a possible reduction in progressivity and a likely growth in the longevity risk.

On the factors determining direct foreign investment in Hungary – a quantitative analysis

Péter Kaderják

Relying on a cross-section analysis of direct foreign investment into the Hungarian manufacturing industry until the end of 1993 the study examines the main factors determining the development of direct investments. The results do not contradict the assumption that the foreign investors are attracted by the relatively cheap and well trained labour as well as that through their investments they make attempts at circumventing the usual trade restrictions. It could also be shown successfully that the inflow of foreign capital was significantly drawn also by the air pollution intensity of some activities. But the results do not support the hypotheses which underline in explaining why foreign investors undertake a role in Hungary the importance of production relations prior to 1989 and of the dominating market position attainable on the Hungarian market.

Families and schools – the chances of education policy*István Kónya*

In the recent past we could hear about several debates on the extent to which and the instruments with which the state should support schooling. The author presents in his article an economic model that may provide help in settling the dispute. The model puts the problem of investment in human capital into a family framework. Thus it may be well used for examining the impact of diverse government programmes related to education.

Externalities on the labour market*Sándor Oroszi*

The study examines the role of externalities, well known from economic theory, on the labour market. Since externalities can in themselves prevent the development of a Pareto-optimum, the market mechanisms asserting themselves without correction cause losses in efficiency and welfare. This is why economic and employment policies not only must compensate for the negative effects caused by market imperfections, but they also have to counterbalance continuously the external impacts through interventions – with differentiated instruments. The author calls the readers' attention to the fact that the various economic branches are characterized by externalities of different nature and intensity. These should be taken into account when setting strategic goals for structural changes.