COMMENT ON AUSTRALIAN DEMOGRAPHIC CHALLENGES
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Summary

Neither the *Intergenerational Report* (IGR) nor *Australian Demographic Challenges* (ADC) pays more than lip service to the notion of shifting burdens between generations. This is just as well because generations, as such, have no behavioural significance. The purpose of the IGR is, in fact, to provide "a basis for considering the Commonwealth's fiscal outlook over the long term, and identifying issues associated with an ageing population." The principal interest of ADC is how to increase the ratio of the working population to the dependent one in order to help deal with the consequences of this ageing process. The other major means of coping with increasing age dependency is to increase the productivity of the work force. Its importance in ADC is emphasised but effectively taken for granted. This is unfortunate because productivity is the real driving force behind the easier handling of future ageing issues. Through its essential link with capital formation it brings to the forefront of public attention that the critical requirement, so that every individual can obtain the retirement income they think they deserve, is that they do the saving necessary to provide the productive future capital stock that will produce that desired income stream when it becomes necessary. The way to cope with future ageing is through increased community saving. Whether or not the form of that saving is superannuation is of secondary importance. The need to save more, which means the need to consume less, is the bitter pill the ADC neglects to emphasize.

Some demographic issues

Some of the important arguments of both the Treasury papers rely on the assumption, and it is an assumption, that Australian fertility will continue to fall. Whether that belief is fully justified is questionable. The issue is somewhat technical and is not taken up here but in the attached paper somewhat provocatively entitled '*Australian fertility has stopped declining*', which was written for publication elsewhere.

That paper can speak for itself. It is sufficient here to note that its theme is that the total fertility rate has been virtually stable for the last six years. This stability is the outcome of offsetting continued declines in fertility at ages below 30 and continued rising increases in fertility for women aged 30 and above. The statistical trends and, more importantly, signs of an increasing ability of families to cope with the competing pressure of work and child-rearing, give weight to the hypothesis that the balance of these trends is now in the direction of a net increase in the total fertility rate rather than a further decline. The rate of fertility decline assumed in the '*Intergenerational Report 2002-03*' is reasonably likely to be a significant understatement of fertility in the medium term future. If that should be the case then the Treasury's age dependency worries are over-stated. The total dependency situation is unlikely to be altered much, because the possible increase in fertility, relative to that projected by the Treasury, carries with it a compensating increase in youth dependency. Nobody's more distant population projections should be taken very seriously.

The above is not intended to deny that there is an impending age dependency problem. It is intended to imply that sophisticated and complex hypotheses about the future are much less rewarding than the Treasury appears to think they are. Only the broad outlines of future population trends are necessary to guide present actions for dealing with them. The specific nature of the problems of the distant future, whatever they may be, have to be handled by future generations, or by present generations when they reach that distant future, not by present generations now.

Consider, for example, the implications of a more generalised view of the interrelationships between fertility and mortality in the Australian context. The current elderly age dependency rate of about 12.5% is in no sense normal. On the contrary it is quite low. In particular it reflects the low level and low growth rates of births that prevailed through the early 1920s to the late 1930s. Conversely the projected age dependency rate of 25% in the early 2040s is exceptionally high. This is partly because of the relatively high growth rate of births from the early 1940s to the early 1950s which then continued, but at a significantly lower rate, until 1961; and partly because of the decline in births in the 1970s and their relatively low level since then. The high dependency rate is more a consequence of alternating high and low levels of fertility trends than it is of increasing longevity taken by itself. If the Australian population level had been stable over a century; or if it had grown at a constant rate over the same period; and if it had experienced stable life expectancies in either situation at the current age-specific levels; then the age dependency rate now would be about 20%. We are not, except to a relatively minor extent, necessarily on an ever upwards age dependency path. The apparent implication of *Australia's Demographic Challenges* (ADC p.18) that an age dependency rate of 25% is permanent is incorrect.

The best demographic policy for handling long term age dependency problems is to attempt to maintain a stable population level or one which grows at a steady rate. Unfortunately, or perhaps fortunately, governments are not capable of determining either fertility or mortality trends. In particular, as China is now being induced to realise, policies which are limited to one side of the balance between births and deaths can have serious unwanted consequences.

In an Australian context demographic policy must have regard to the role of net immigration. In its projections IGR takes as its benchmark number 90,000 per annum and it comments on the projection effects of a 135,000 alternative. As ADC is primarily concerned with ageing, and as the level of immigration has little influence on the age structure, serious attention is not given in ADC to the full implications of variations in immigration on our demographic future.. Two points should be made here. First, for reasons indicated above, whatever level of immigration is chosen as a demographic dimension of national policy it should be treated as a parameter of the system, varied only rarely, and not adjusted up and down at the whim of politicians or public servants responding in the short term to influential pressure groups. Second, it is irresponsible to consider any level of immigration as an element in a demographic policy challenge without regard to the effects of population growth on the natural environment, the urban built environment, and the depletion of non-renewable resources.

In implying that demographic events constitute 'challenges' that have to be met the Treasury is implicitly putting demographic policies, in themselves, into the too-hard basket. This is so even when the scale of the perceived challenge is partly of the Treasury's own making. In democratic societies government demographic policies with respect to fertility necessarily have to take the form of encouraging people to act in a manner which it is expected will be in the community interest. If it should be granted that the maintenance of stable population trends is in the community interest; and that, in the present instance, *further* declines in fertility, as *assumed* by the Treasury, can but exacerbate projected age dependency problems; then one of the most important ways in which the future *demographic* ageing challenge can be reduced is by discovering the ways in which the balance of pressures on women to manage work and child rearing can be eased now. From this perspective paid maternity leave would appear to be a minimum desirable policy objective. A less stressful life for working women with young children over the next forty years would be a cheap price to pay for less age dependency then.

Nor should mortality be taken simply as an act of God, tempered by the efforts of the medical profession, the makers of medical equipment and the pharmaceutical industry. The ageing of the population in recent decades has witnessed, world wide, the emergence of an euthanasia movement. Its principal supporters are the elderly who see death approaching and who wish to exercise their own control over when and how it happens. As the aged population doubles proportionately support for euthanasia can be expected to more than double. The likely effects on projected mortality rates are ambiguous. Much will depend on the social and cultural changes brought about by the difficulties of ageing and on the rationality of the responses made to them.

Economic responses to the challenge

The Treasury's preferred economic solutions to the prospective severe age dependency problem are increased labor force participation and increased productivity. Both will indeed be appropriate when that time comes. The relevance of the former to the here and now is not clear.

If the falling participation rates in recent years of the over 50s are a function of the use of wealth by some of the wealthier members of this group, or if others have decided that they have sufficient means to follow a simple life-style in the future, it is difficult to see that this is a problem for government. If, as appears to be the case, a substantial proportion of the fall in older ages work force participation is involuntary, a result of times when the long-term security of employment has fallen and when employers have continued to treat elderly people as unemployable, then the present problem is how to retrain employers, not how to provide incentives for potential workers. Apart from the needs of this group the present concern of government about early retirement now ought to be, and is, to limit the opportunities for those indulging in a spending spree on accumulated savings in order to ensure entitlement, later, to an age pension. The abuse of lump sum benefits ought to be of concern to all taxpayers.

Government policy appears to be centred around a combination of carrots and whips to increase labour force participation. Proclaimed supporters of free markets have become detailed regulators of labour market incentives and disincentives. If government policies were less focused on maintaining annual surpluses for electioneering vote buying, and more willing, in trend terms, to give the economy a greater head of steam, then the market itself would probably dispense with the need for manipulation of this sort.

An emphasis on productivity growth for both present and future economic needs is undoubtedly appropriate. The higher the productivity of the economy in the 2040s the easier will be the task of the necessary transfers between workers and dependents, young as well as old. But the real issue is not productivity then but the trajectory of its path between now and then. The higher that path at all points of time the better will be the economic benefits for all generations between now and then.

The Government's initial preferred solution in ADC is: "to grow the economy more quickly. A larger economy will provide us with higher improved living standards and better enable us to meet the costs associated with an ageing population." It is only towards the end of the document that productivity is given pride of place. It is not self evident that these propositions are mutually consistent. Is it really the case that the largest Australian economy is necessarily the one which is the most productive per worker which is the relevant criterion with respect to age dependency? This is a critical issue that shouldn't be taken for granted.

From an individual's perspective the main way to make provision for life when aged and no longer employed is the appropriate level of pre-retirement saving. Can one anticipate that Australians will eschew their prevailing propensity to borrow in order to consume now and revert to an old fashioned willingness to save in the present in order to consume more in the future? This is essentially a personal decision for everyone. It is not an intergenerational problem.

The outlook for such a change is not promising. As Clive Hamilton has recently, and somewhat stridently, pointed out the world's wealthy economies are now consumption driven. The consumption habits for all but the poorest members of the society have little relevance to their biological food, clothing, and shelter needs. Consumers' demands are driven by the competitive actions of profit-seeking producers of gadgets from toasters, through mobile phones, to cameras, computers, and cars. Conspicuous consumption of housing should not be forgotten. This unholy mixture is gift-wrapped by the advertising industry which is the main supporter of the media whose chief economic function is to propagate the consumption message. This twenty-first century version of bread and circuses is politically sacrosanct and condoned by economic advisers who fear the possible consequences of the curtailment of consumption on the economic growth band-wagon.

It is not appropriate for an economist, as an economist, to make value judgments about the individuals' propensities to consume but it is within his/her brief to observe how tastes are created by the competitive nature of modern market economies and their associated political institutions. It is also a proper economist's function to make the point that if people were to be encouraged to follow a more abstemious life-style, which many of them are now doing, and maintain it through their working lives, then the economic age dependency problem envisaged by the Treasury would be of a very different character. This possible vision of the future no doubt has a utopian (or Spartan?) flavour. Should the increasing signs of dissatisfaction with to-day's very materialistic and environmentally damaging life-styles gather strength, then both politicians and their economic advisers may well have to turn their attention to the politics and economics of a more frugal future.

Both the IGR and the ADC pay occasional lip service to the concept of present generations passing on burdens to future generations. Fortunately no serious attention is given to it. The term generation has come to have very little useful content. We have 'the baby-boom generation', the 'X generation' and the 'Y generation'. None of these terms corresponds to the average period between births of parents, children and grand-children which defines generations within individual families. These days that time interval is probably about 30 years. The age span of the work force, which is the relevant length of time in relation to dependency, has nothing to do with generations. In short the practical meaning of generation is fuzzy and, more importantly, it has no behavioural content. Generations, as such, don't do anything.

The reported decline in personal saving in the national accounts is almost certainly over-stated .It arises because national income accounting conventions do not recognise wealth as a source of spending. Even if adjustments are made for this national accounting error it is likely that personal saving has been falling. This has arisen for a variety of reasons. They include: the increase in the ease of spending associated with the almost universal adoption of credit cards; the lax personal budgeting that this encourages; and the bias in the financial system as a whole to make credit more accessible to the public as a source of profits rather than of benefit for customers.

One of the consequences of the philosophy that small government is good government that has influenced the budgetary behaviour of both major political parties in recent decades has had is the paradoxical effect of down-grading personal responsibility for saving. The philosophy relies on the assumption that the market knows best. What the market knows best with respect to saving is to facilitate spending. The common sense virtues of saving before spending are as antiquated as the nineteenth century in which they flourished. Government response to this situation has been to force-feed superannuation. The more fundamental habit of voluntary personal saving has been left to wilt on the vine. Governments which, explicitly or implicitly, proclaim the virtues of personal responsibility have made a virtue of necessity by organising public finance in such a way that the taxation system funds government capital formation rather than relying on tapping inadequate personal saving to fund it through publicly issued government securities. The short-fall in the national personal willingness to save is covered by the ease with which the banking system borrows abroad on a short term basis for what have become bad long term habits. The Reserve Bank's preaching against an over-reliance on borrowing falls on the deaf ears of the public, the bankers and the government. While this systematic preference for spending here and now prevails the wellbeing of the aged in the future remains at risk.

Alerting us to the possible implications inherent in our present demographic structure is a useful function. But the Treasury's version of these possibilities cannot be taken too seriously. They are more an illustration of current demographic and economic presuppositions than they are of the shape of the future. The situation calls for much greater examination of possible alternatives and of ongoing discussion which is independent of an arm of government.