



Problem! What problem?

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This presentation has been prepared for the 2016 Financial Services Forum.

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Problem! What problem?:

An heretical perspective on the
ageing population



What's the problem?

- Who's funding things?

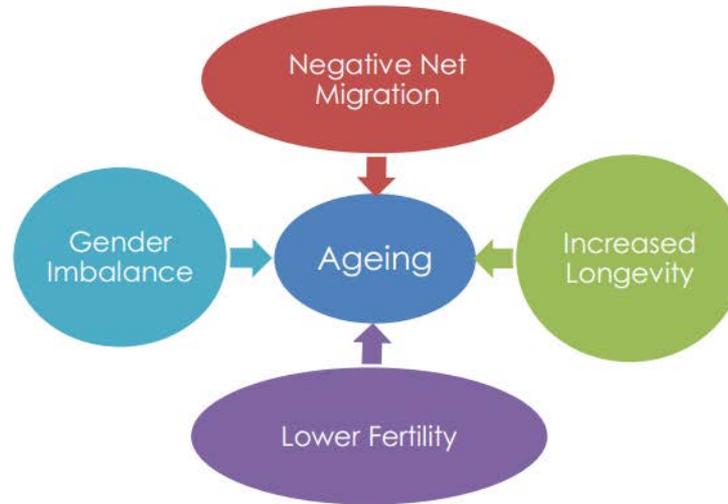
Unless action is taken to increase the growth potential of the economy and ensure spending is sustainable, spending will exceed revenue and result in a fiscal gap of 2¾ per cent of GDP by 2049–50.

If steps were not taken to close the fiscal gap over time, it is projected that net debt will emerge in the 2040s and grow to around 20 per cent of GDP by 2049–50. Acting now to address fiscal pressures posed by ageing will minimise the fiscal adjustments required in the future.

From a colleague:



2. Population Ageing – A multi-waved tsunami

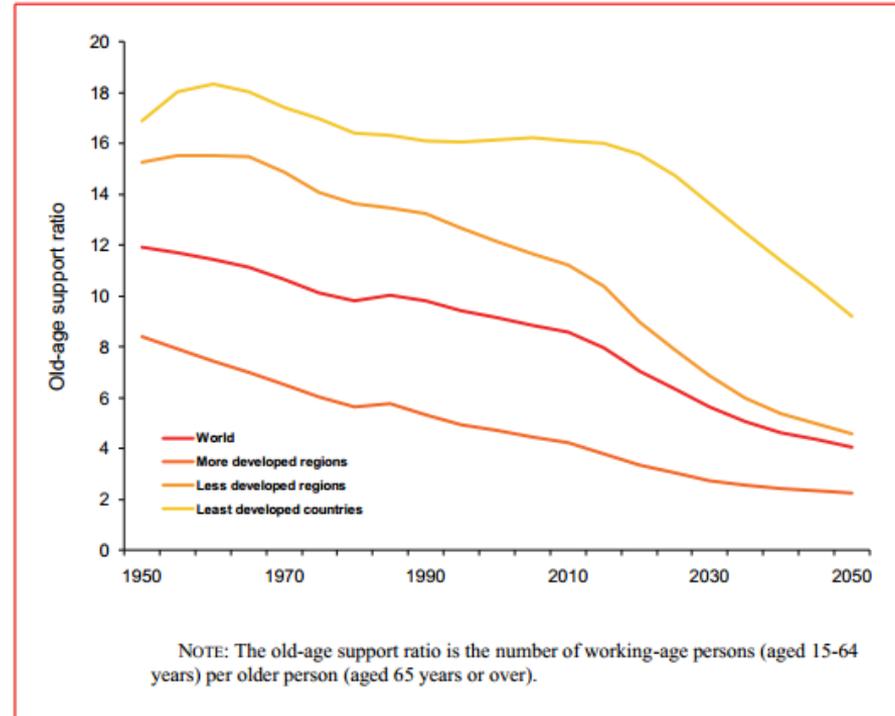


- *tsunami* is a loaded word



And the UN is onto it!

Figure 2.6
Old-age support ratio: world and development regions, 1950-2050



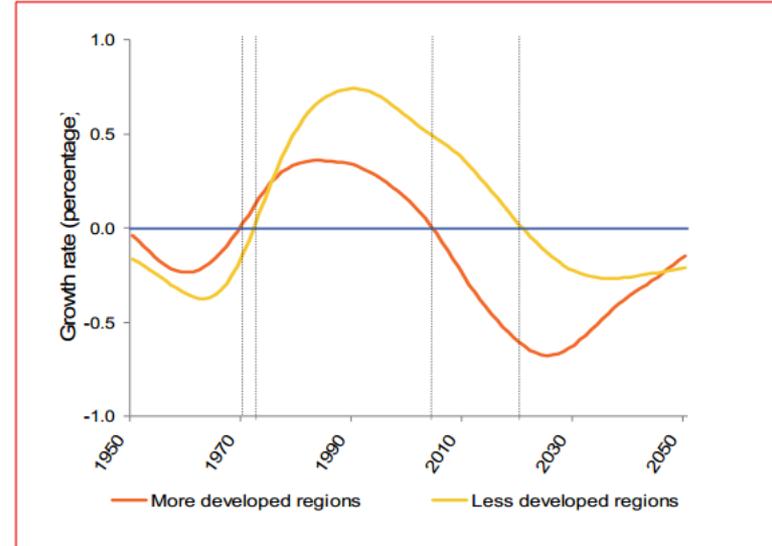
Shock! “Negative demographic dividend”



Dividend is
another
loaded word

Figure 2.10 shows the projected demographic dividend, that is, the difference between the growth rates of equivalent producers and consumers induced by demographic change alone. Values above zero reflect positive economic growth, while values below zero indicate a “negative dividend”, that is, a period during which demographic change is contributing to a reduction in economic growth, all things being equal.

Figure 2.10
Demographic dividend (demographically induced economic growth rates) by development region, 1950-2050



China: Old before it gets rich



Demography

China's Achilles heel

A comparison with America reveals a deep flaw in China's model of growth

Apr 21st 2012 | From the print edition



2.8k



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Source: The
Economist



Health costs rise!

Our population is predicted to live significantly longer and forecasts indicate that spending on health care across all levels of government is expected to grow from 6.5% to 10.8% of GDP over the next 50 years.

Some intergenerational cross subsidy is an inevitable part of our health care system (as it is with other services) but the cost on the working population through taxation needs to be addressed in order to protect the quality of Australia's health care services and system.

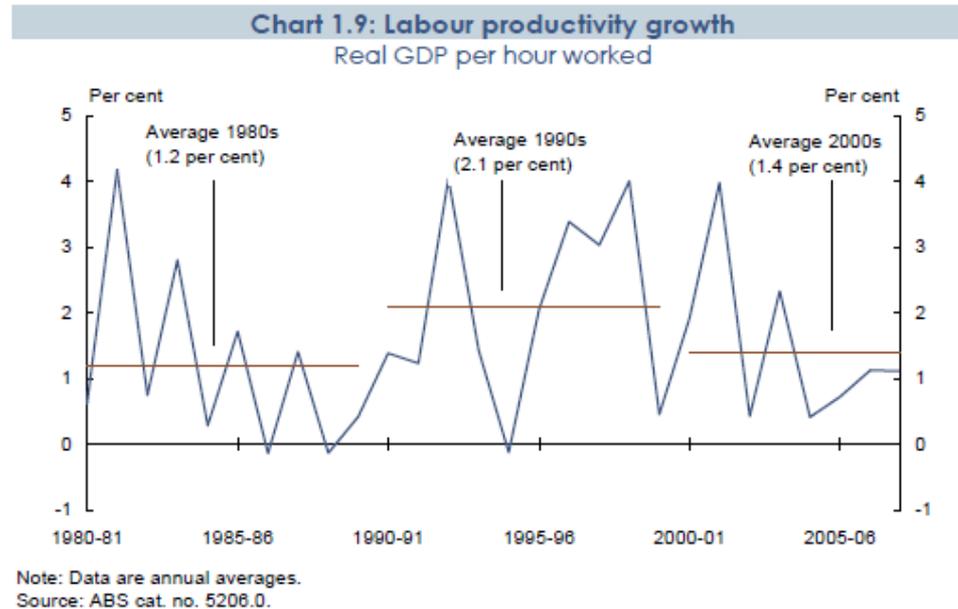


Talking “money” is the problem

- Primary questions shouldn't be about finance
- **Primary:** can we produce and distribute the goods and services to meet projected demand?
 - **Secondary:** can we distribute money to facilitate the efficient production and distribution of goods and services

Australian Productivity

- Projected at 1.6% next 40 years



US productivity

- Projected at 1.6%-1.7% for the future

Table 1: Improvements in Living Standards, 1870 to 2010

Period	Total Factor Productivity (Average Annual Growth Rate)	Main Sources of Growth	Change in Life Expectancy at Birth (Years per Decade)
1870 to 1900	~ 1.5% to 2%	Transportation, communications, trade, business organization	1.3
1900 to 1920	~ 1%		3.2
1920s	~ 2%	Electricity, internal combustion engines, chemicals, telecommunications	5.6
1930s	~ 3%		3.2
1940s	~ 2.5%		5.3
1950 to 1973	~ 2%	Widespread	1.4
1973 to 1990	< 1%		2.4
1990s	> 1%	Information technology	1.7
2000s	~ 1.5%		1.4
1870 to 2010	~ 1.6% to 1.8%		2.3
1950 to 2010	~ 1.2% to 1.5%		1.8

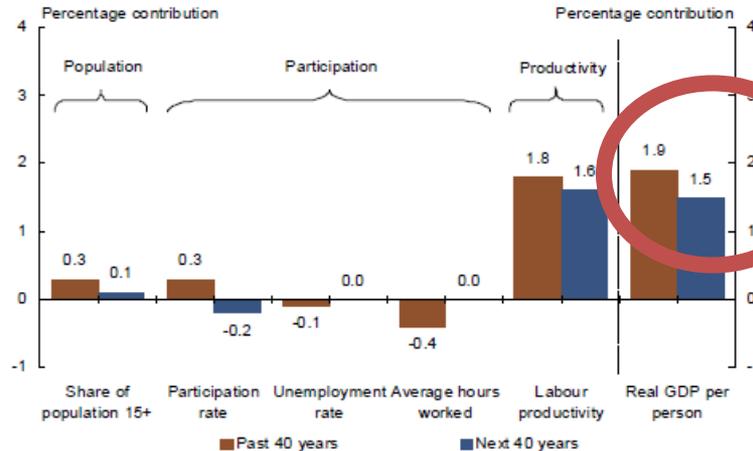
Sources: Field (2012), Gordon (2010), Carter et al. (2006), Center for Disease Control and Prevention (http://www.cdc.gov/nchs/data/dvs/deaths_2010_release.pdf).

Source: US CBO - Total Factor Productivity Growth in Historical Perspective 2013

Can we produce the goods?

- Australia example – **Real GDP per person**:

Chart 1.10: Growth in real GDP per person based on the 3Ps



Source: ABS cat. no. 5206.0, cat. no. 3105.0.65.001 and cat. no. 6202.0, and Treasury projections.

- Yes we can!

- +1.5% p.a.
- Double GDP per person over 40 years

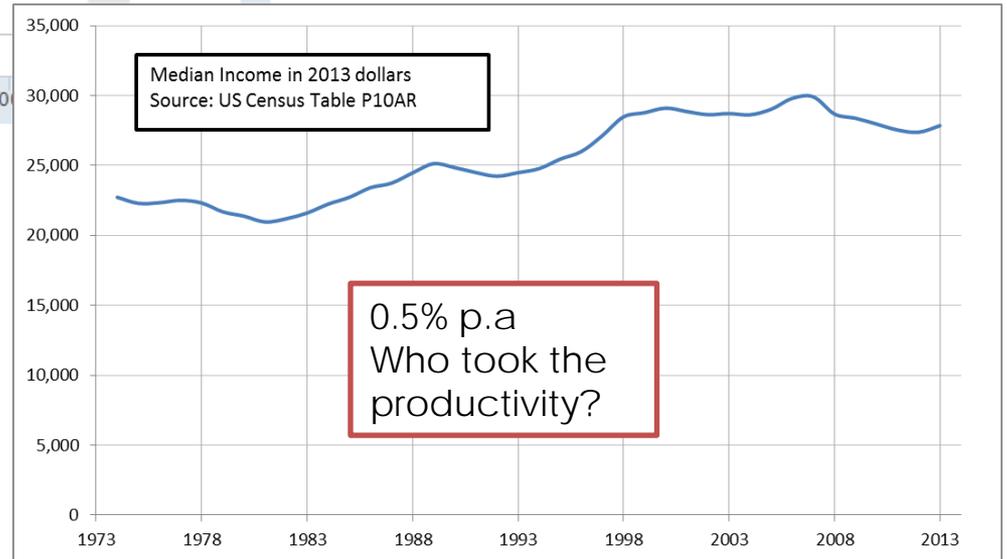
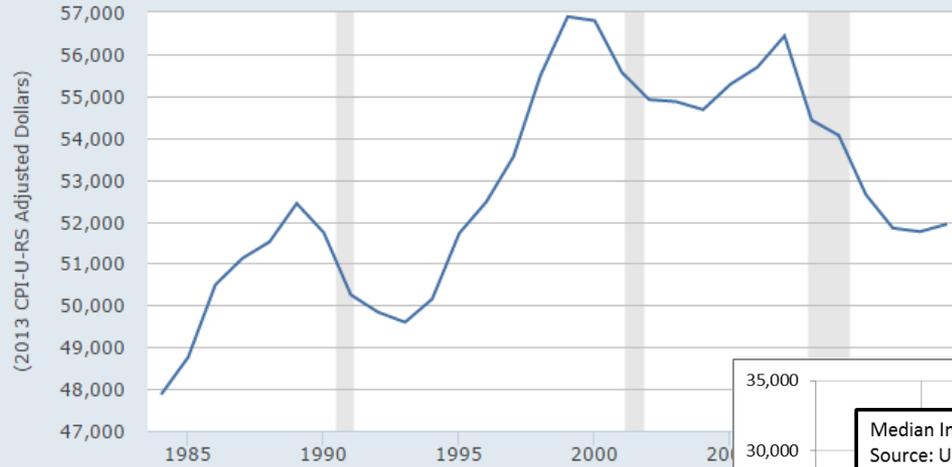
Recap:

- GDP growth is not a problem
- Productivity is the important factor
- We need to distribute the resources appropriately
- Want to avoid US problem of little rise in real income



FRED

— Real Median Household Income in the United States



Supply and Demand

- Usual perspective – reduce transfer of government funding of aged persons' expenditure
 BUT
- Will an aged society have the demand to employ the workers?
- Government might need to increase demand to keep employment up
 - See current debate on *secular stagnation*



Distribution in the macroeconomy

- The government is not like a household or a company
- The economy as a whole is a closed system
 - My spending is someone's income
 - My saving is their borrowing or capital raising
 - Government* deficit means more private sector assets
 - Surplus means less private sector assets

* Sovereign government



Private sector funding?

Unless action is taken to increase the growth potential of the economy and ensure spending is sustainable, spending will exceed revenue and result in a fiscal gap of 2¾ per cent of GDP by 2049–50.

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- Private sector needs to net save if we want to private sector to provide the future payment for the resources for ageing
- This means the government sector runs a deficit
 - or something happens on the current account.

Interjection!

- Q. Why don't the old people save in the private sector?
- A. Consider what happens when they want the money?
 - The younger people have to give it to them by maturity of their bonds, buying their equity, paying coupons, dividends
 - The usual argument is that we can't tax the young people (workers) enough. But, via saving, the transfer is the same only by a different means.
 - We have the same economy, and need to create the same demand for goods by the old
 - What if the young want to consume – maybe they don't buy the equities? Older people then don't have the desired resources to buy the goods produced

Novel bonds for saving

- Government borrowing by bonds is an interest rate swap
 - Fixed rate for known term for floating cash rate
- Different sorts of swaps could meet private demand for financial products to help provide retirement income e.g.
 - inflation linked payments,
 - linked to nominal GDP,
 - perpetuities

Standard partial solution

- Increase liquidity of non-liquid assets
 - negative mortgages;
 - reduce taxes on transactions
 - remove legal impediments for securitisation
 - but strengthen regulation
 - ...
- Fully agree

Change happens

- Medical costs as a proportion of GDP does not matter - economy is a closed system.
- So what if we spend a lot of money on end-of-life care, if that's what we decide to do.
- Over 40 year periods economies change a lot
 - We can't predict what will happen



Morality and economics

- Beware of subconscious moral judgments that interfere with economic decisions
- Economic debt is not a moral issue
 - (OTOH moral debts can't be paid economically)



Morality and economics (ii)

- ▶ Beware status snobbery
 - ▶ Caring service jobs that do not require a university degree or much training are menial
- Large increase in service industry for aged care;
 - needs workers;
 - low current pay does not attract workers;
 - need to increase wages;
 - if we want decent aged care this is what we must do

Conclusion

- Problems raised with ageing are a false perspective
- Wrong words to frame the debate will lead to sub-optimal solutions
- *Meryl Streep speaking as Margaret Thatcher:*
 - *Watch your thoughts, for they become words.
Watch your words, for they become actions.
Watch your actions, for they become habits.
Watch your habits, for they become your character.
And watch your character, for it becomes your destiny.
What we think, we become.
My father always said that.*
- Before rushing to solutions we need to look at the problem from proper macroeconomic and historical perspective
- Don't worry, be happy