Is Low Fertility and Rapid Population Aging Really a Problem?

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Based on:
ISSUE

• Widespread concern that low fertility and rapid population aging will lead to:
  – Severely strained public budgets
  – Reduced standards of living
• Governments of more than 50 countries reported to the UN that their birth rates were too low.
• Many governments are adopting programs to encourage couples to have more children.
Findings

• Moderately low birth rates, below replacement fertility, are actually ideal for achieving a high material standard of living.

• Fiscal problems can be addressed by:
  – Investing more, and more effectively, in human capital
  – Adjusting retirement ages and eligibility for public support in response to the improved health of older adults
  – Adjusting public spending and tax systems as needed

• Only if birth rates are very low, should governments actively pursue pro-natalist policies.
Low Fertility Does Create Fiscal Problems
Evidence: Public Sector

- Detailed estimates of public benefits and taxes paid at every age in 29 economies.
- Determined the fertility rate the would produce an age structure allowing the highest age-specific benefits per tax dollar spent.
SRG summarizes the adjustments to taxes and/or spending required to maintain current balance between inflows and outflows.

Best possible outcome
- TFR of 2.7 and mean age in the mid-30s
- Spending cut of 16% or
- Tax increase of 19%

Status quo outcome
- TFR of 1.34 and mean age in the mid-50s
- Spending cut of 30% or
- Tax increase of 45%

Given age profiles of public transfer inflows and outflows and 2009 mortality schedule.

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Moderately Low Fertility Is Best for Standards of Living
Evidence: Standards of Living

- Detailed estimates of public benefits received and taxes paid at every age in 29 economies.
- Detailed estimates of private costs and benefits at every age in 40 economies.
- Capital costs of a larger labor force.
- Determined the fertility rate that would produce an age structure allowing the highest level of consumption at every age.
Current TFR and TFRs that maximize standard of living

<table>
<thead>
<tr>
<th>Income group</th>
<th>Current TFR</th>
<th>Standard of Living</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>K/Y=OECD average</td>
</tr>
<tr>
<td>Upper-middle income</td>
<td>2.19</td>
<td>1.52</td>
</tr>
<tr>
<td>High income</td>
<td>1.58</td>
<td>1.79</td>
</tr>
<tr>
<td>- low TFR</td>
<td>1.35</td>
<td>1.74</td>
</tr>
<tr>
<td>- high TFR</td>
<td>1.88</td>
<td>1.86</td>
</tr>
</tbody>
</table>

Upper-middle income Economies: Argentina, Brazil, Chile, Colombia, Costa Rica, Jamaica, Mexico, Peru, South Africa, Turkey, and Uruguay.

High income Economies:
TFR<1.5: Austria, Germany, Hungary, Italy, Japan, Slovenia, South Korea, Spain.
TFR>1.5: Australia, Canada, France, Sweden, UK, US.

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Effect of TFR on Consumption (K/Y = 3, own mortality schedule)

Very low birthrate of 1.3 births per woman will reduce consumption by about 7%.

Note: Average values for NTA economies using their current survival schedule and consumption and labor income profiles.
Summary

• Changes in age structure in recent decades have led to a very favorable but transitory demographic dividend.

• Going forward, for any demographic scenario, major adjustments to the public sector will be required.

• In most countries, encouraging higher fertility is the wrong answer. It will lead to lower standards of living.

• In a few countries with VERY low fertility, pro-natalist policies should be explored.