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Australia's Ageing Population: Meeting the Challenge

1. Introduction

Australia has an ageing population. From around 13 per cent today, the proportion of the population aged 65 years and over is now projected to rise to between 27 per cent and 30 per cent by 2051.

This ageing of Australia's demographics has taken on greater public policy significance, as it presents major challenges about how Australia should address the economic, fiscal and social impacts, including the impact on the future growth in living standards of Australians.

The *Intergenerational Report* (IGR) projected that the change in the age structure of the population, coupled with lower participation in the workforce and an assumed return to the average productivity growth rate of the past 30 years (i.e. from around 2¼ per cent per year in the 1990's to around 1½ per cent over the past 3 decades) would lead to slower economic growth, slower growth in government revenues, and slower growth in living standards.

When combined with the expected increased demand for government services—such as health, aged care, and pension payments—it could lead to persistent budget deficits, unless taxes are raised or government spending is curtailed. In this regard, the issue of user-pays versus government intervention and the balance between public and private provision of services will assume greater prominence in the policy choices decided by Australians.

2. The Challenges Arising From Ageing Demographics

2.1 Framework for Analysis

CEDA has drawn on the IGR framework to identify the major challenges arising from Australian's ageing demographics. *Population*, *participation* and *productivity* are the factors which contribute to economic growth and each presents separate challenges.

While commentators vary in their optimism about Australia's capacity to manage potential increases in *spending*, nevertheless the policy responses need to be formulated. The final dimension requiring analysis is *saving*, both in the context of intergenerational equity and adequacy for retirees.

2.2 Population Projections

The issues arising from an ageing Australia have emerged because both fertility and mortality have declined faster than was foreseen three decades ago.

The most recent ABS demographic projections show that: -

- ? Australia's population will grow from 19.7 million in June 2002 to between 23.0 million and 31.4 million in 2051.
- ? The median age of the population will rise from the present 35.9 years to between 46.0 years and 49.9 years.

- ? Life expectancy will increase from the present 77 years for males and 82 years for females to around 84 years and 87 years respectively in 2051.
- ? The proportion of people aged 65 years will grow from 13 per cent in June 2002 to between 27 per cent and 30 per cent in 2051
- ? The proportion of 'old-old' people (aged 85 years and over) will increase from 1.4 per cent of the population in June 2002 to between 6 per cent and 9 per cent of the population in 2051.

Changes in trends in fertility and mortality will affect these projected outcomes, as will net migration. In the latter regard, net migration of 100,000 per annum would have a beneficial impact on slowing the ageing of the population (by 3.8 percentage points), especially when fertility rates fall to very low levels, but levels beyond that would be less beneficial from the perspective of slowing the rate of ageing. Likewise, pronatalist policies—such as those related to work-family balance and family support—would have an impact, although it would be at least 25–30 years for an increase in the birth rate to have an effect on the working age group.

2.3 Labour Market Participation

Australia's labour force participation rate has increased from around 60 per cent in the mid 1960's to around 64 per cent in recent years. However, the IGR projections are for the overall participation rate to fall from around 64 per cent at present to just over 55 per cent by 2041–42, primarily due to more of the population moving into the older age groups. The male workforce participation rate has fallen from around 94 per cent (30 years ago) to 85 per cent in 2001, while female participation has increased from around 47 per cent to 66 per cent. Significantly male workforce participation has dropped even more sharply for over 55s. Between 1973 and 2001 participation dropped 16 per cent for the 55–59 age group and 29 per cent for the 60–64 group. These trends reflect many factors including the following: -

- ? stronger demand for skilled professionals relative to manual workers and tradesmen;
- ? involuntary and 'voluntary' retirements by male workers during extended periods of structural adjustments;
- ? lack of necessary skills by males in adapting to change; and
- ? plummeting male participation in conventional work.

Increasing the rate of economic growth is vital to increase the demand for labour, and hence, labour force participation. However, to target over 55 male participation a range of specific programs and measures are required. These should focus on facilitating mobility and flexible work arrangements to suit mature aged workers; lifetime learning; removal of disincentives to work in tax, superannuation and income support programs; and attitudinal change about older employees.

Overall, it is desirable to lift the rate of workforce participation in Australia back towards where it used to be for males. Most importantly over 55 participation rates should match those in the OECD. Retention of older workers will also enhance productivity levels, as productivity does not peak until late mid-life, staying high until late in life. These factors would also ensure no increase in the aged-dependency ratio in the future.

2.4 Productivity Growth

Australia's level of productivity is only around 80 per cent as much as the US per hour, although productivity performance has been impressive since the early 1990s. However, the IGR suggests that productivity growth could fall from around 2¼ per cent per annum experienced in the 1990s to around 1½ per cent per annum in the next three decades. This will happen if the drivers of growth in the 1990s, microeconomic reform and the adoption of IC&T, are not replicated in decades ahead.

Data from IBIS World on productivity gains across the 17 industry divisions over the past 5 years show: -

- ? faster growth in service industries such as transport, finance and insurance, and accommodation and cafes, than the all-industries average; *but*

? poor productivity gains in the four industry divisions for which there is expected huge future demand: health; personal and other services; cultural and recreational services; and education and training.

It is clear that Australia needs to achieve productivity growth at levels greater than the 1½ per cent per annum suggested by the IGR over the next three decades, in order to sustain living standards and provide for growing health needs.

Maintaining a commitment to continuing the economic reform agenda is not optional. There are many areas of on-going reforms such as in energy, infrastructure, water resources and labour markets, where the momentum should be re-ignited. And there are further industries (such as health and education) identified by IBISWorld data, where the poor productivity gains must be reversed given the expected huge demand for these services over the next few decades.

2.5 Government Expenditures

The IGR identifies that without policy change, and if current trends are maintained, the ageing population will create increased demand for health, aged care and pension payments, which potentially will lead to budget deficits equivalent to over 5 per cent of GDP by 2041/42. Commonwealth Government spending on health will rise from around 4 per cent of GDP in 2001/02 to 8.1 per cent in 2041/42. But spending on the Pharmaceutical Benefits Scheme could grow more rapidly—from 0.6 per cent of GDP to 3.4 per cent by 2041/42. While there are many reasons to expect such spending increases can be averted, it is vital to identify the challenge to be faced.

The fiscal challenges are just as significant for State Governments faced with burgeoning health costs and population ageing related impacts on state revenue, arising from projected reductions in stamp duties and payroll taxes.

There are also emerging issues involving localized and regional patterns of ageing, especially in coastal areas experiencing substantial in-migration of older people, where infrastructure is insufficient and the demand for services by the aged population will exceed the supply potential of the local labour force.

2.6 Savings

The challenges, however, are not only macroeconomic and fiscal based, but also personal and social. Australians are living longer and studies show that many will outlive their savings, reflecting inadequate superannuation provisions and savings. Such a scenario may mean many disappointed and disenfranchised older Australians.

If governments react to spending pressures by implementing more user pays programs then the call on private savings will increase further. A range of innovative measures are needed to address the adequacy of savings, both to provide more incentive to save and also to remove constraints that limit savings options.

3. The Way Forward: A CEDA Policy Perspective

3.1 Continued Debate

CEDA supports heightened levels of discussion and debate on the key economic and social challenges facing Australia arising from an ageing population and, in particular, the implementation of public policies that are required to reverse the following impacts: -

- ? lower labour participation rate leading to slower economic growth and a higher dependency ratio;
- ? fiscal pressures on governments to reduce spending or to raise taxes in order to fund budget outlays, arising from the expected increase in the demand for aged care, health care, and pensions; and
- ? lower living standards due to constraints on government services and inadequate savings, leading to economic and social inequities and disappointment.

CEDA encourages further analysis, not only by Commonwealth and state governments, but also other independent analysis, so that the community clearly understands both the opportunities and threats.

3.2 Economic Growth

The challenge for Australia is to develop policies and measures that will generate sustainable strong economic growth, focusing on population, participation and productivity growth strategies.

Population policies will not have a significant impact in the short term, but are necessary to stop a long term decline in population and economic growth, and include

- ? Maintenance of a net migration program of a minimum 100,000 per year
- ? Pronatalist policies, such as those related to work-family balance and family support.

Labour market participation rate improvement is the key to addressing the immediate intergenerational challenge, particularly targeting over 55 male participation rates. An integrated strategy is necessary which encompasses mature age worker retention measures, elimination of income support and retirement income policies that discourage labour force participation, and strategies to support workplace reform to become more 'older worker friendly'.

Policies to encourage mature age workers, particularly males, to remain in paid employment include:

- ? promotion of labour force flexibility facilitating mobility, and flexible work arrangements to suit older employees;
- ? increased access to lifetime learning;
- ? labour market programs and retraining for mature age workers to retain them in the workforce; and
- ? phased retirement.

Measures necessary to eliminate the negative impacts of income support and retirement income programs include:

- ? limiting access to lump sum from superannuation;
- ? ensuring part-time work and partial retirement is not discouraged through high marginal tax rates;
- ? removing disincentives to continue working that result from defined benefit schemes that provide the majority of benefit after 20 years in the scheme; and
- ? increasing incentives to work for those receiving income support.

Employees also need to take action to make workplaces more 'older worker friendly'. This process can be assisted by government through initiatives including:

- ? educational programs to overcome negative attitudes about 'older workers';
- ? best practice studies of organizations who successfully develop and implement age management strategies; and
- ? leadership from government as an employer itself, in implementing age management strategies.

Productivity growth is an essential ingredient for economic growth to provide the demand necessary to support increased labour force participation. Such growth requires continued attention to reform measures including:

- ? a strong competition policy framework to enhance competition in product and labour markets;
- ? enhanced adoption of IC&T, and new industry specific systems and technologies in public and private sector organizations;
- ? development of new Commonwealth—State service delivery models to promote efficient resource allocation, remove duplication of services, and better target customer needs in health, aged-care, social services, education and training, and in the provision of income and other welfare support;

- ? acceleration of the on-going reform agenda in areas such as energy, water management, transport, communications and infrastructure; and
- ? a strategy to support higher levels of innovation in Australian business.

3.3 Spending measures

Clearly government spending cannot continue to grow as projected in the IGR. Inevitably innovative responses will be found as price signals lead to market responses. However, responses can and should be put in place now, including:

- ? achieving a dividend from improved health technology by focusing on wellness and illness prevention, thereby lowering health costs;
- ? strategies to focus on the last few years of life, where health costs are highest, such as a national strategy to tackle dementia;
- ? consideration of different funding options for government services such as more user charges;
- ? reviewing the balance between public and private provision of major services, such as health, medicines and aged care; and
- ? ensuring services and infrastructure spending can be retargeted away from areas of population decline to new areas of growth, such as regional and coastal centers of concentration of older Australians.

3.4 Savings Adequacy

While Australia, chiefly through compulsory superannuation, has made significant changes to prepare for the retirement of our ageing population, many Australians will still find their savings inadequate. The most important strategy to increase savings adequacy is to extend workplace involvement.

Other measures which address the adequacy of savings include:

- ? Improvement of incentives for savings through superannuation by transferring tax totally to the benefit stage, and through co-contributions and matched saving programs targeted at low income groups;
- ? Increasing compulsory superannuation by introducing compulsory employee contributions; and
- ? Unlocking investment in housing by encouraging and facilitating more flexible and less restrictive mechanisms to draw upon housing equity.

This Policy Statement draws on material contained in the following CEDA publication: Australia's Ageing Population: Fiscal, Labour Market and Social Implications, March 2004 (Growth 51).