

# Are welfare states financing their growing elderly populations at the expense of their children?


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In most OECD countries social expenditure takes almost one third of national GDP and represents half of total government expenditure. Within social expenditure, the largest proportion of spending is taken up by old age pensions. In 1998, the OECD countries<sup>1</sup> spent an average of 8 per cent of GDP, the equivalent of 36 per cent of total social expenditure on cash benefits and services to the elderly. At the same time, expenditure on family benefits and services, on average, made up 2 per cent of GDP and 9 per cent of total social expenditure (OECD National Accounts Data 2003).

The population of every OECD country is ageing as a result of sub replacement level fertility rates and increased life expectancy. In all the countries included in Figure 1 the proportion of children (under 19) has fallen and the proportion of elderly (over 65) has been rising between 1980 and 2000, although at rather different rates. OECD projections estimate that as the large post-war baby-boom generations reach retirement age, the old age dependency ratio will increase from 37 per cent of the working population in 1995 to 51 per cent in 2020 to 72 per cent in 2050 (Busse et al. 2003). These increasing old age dependency ratios have generated anxiety about whether existing pension and health care systems can be sustained.

The problems posed by the changing demographic make-up of societies have been examined from several perspectives: intra-national political organisation and welfare regime type; political power relations; and labour market dynamics.

Pampel (1994) has suggested that there is a distributional clash between the generations that is influenced by national institutional arrangements. In some countries the social partners can soften the impact of national distributive consequences. In uncoordinated political economies on the other



hand, special interest lobbies can block pension reforms. Esping-Andersen and Sarasa (2002) have argued that on the basis of welfare regimes types, the aged-bias is especially pronounced in Continental and Southern European welfare states, while Scandinavian social democracies are more youth-biased.

Some have expressed concerns that the ageing of the electorate might impose a pressure on governments to maintain a high spending on the elderly (Esping-Andersen and Sarasa 2002). In the presence of constant resources, the growing number of elderly and the diminishing number of children, it is feared that the political interests of the elderly will dominate and expenditure on children will fall. The imbalance of political power between the generations was first described by Myrdal (1940): "The aged have votes; children and the unborn do not" (Hinrichs 2002). Hence intergenerational inequality might arise as the older generation increases its relative strength within the electorate.

Recommendations of think-tanks and supranational organisations (OECD 1996) include the advice to governments to use the "window of opportunity" for making radical, irreversible reforms in public pension schemes before the elderly populations grow numerically powerful enough to block such changes (Hinrichs 2002). However, evidence shows that although citizens aged between 60 and



total jobs, but there is no statistical evidence that there is a relationship between the two. Employers shift older workers onto pension schemes, enabling a high workforce turnover without focusing on age management. Early retirement enables employers to cope with industrial restructuring, the high pace of technological advance, and the need for the regular renewal of workforce knowledge and skills (Ducatel et al. 1999). Compared with the 1960s when workers retired after the statutory retirement age of 65 or over, by the early 1990s actual retirement age started to decrease dramatically. Currently half of the European Union countries barely reach the 60-year mark as the average age of retirement (Fahrenkrog et al. 1999). Early retirement increases the cost of social security provision which may reinforce the cost of retirement schemes at the expense of families with children.

Generational accounting has been developed as a technique to monitor equity between successive generations. Generational accounting assesses the degree of intergenerational redistribution that will result as a consequence of current policy legislation, thus indirectly measuring the reform pressure arising from demographic change. Advocates argue that generational accounting can be used as a tool to facilitate assessments of policy changes on generational equity (Auerbach et al. 1994; Feist 2003).

### Comparing expenditure

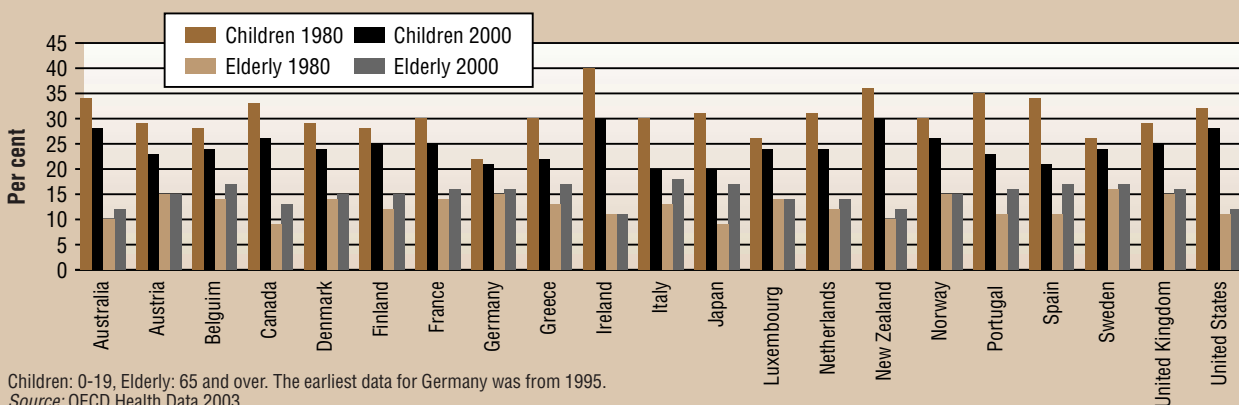
In the light of the concerns that demands on social expenditure by the elderly will be met at the expense of benefits and services for children, the aim of this article is to review what has been happening in selected OECD countries in the last 20 years or so. Two measures of equity are considered: public expenditure on benefits and services for the elderly and families with children; and the relative poverty rates of the two groups.

The OECD publishes data on public expenditure on different groups including expenditure on cash benefits and services for the elderly, and cash benefits and services for families with children. This enables

70 years show the highest, consistent voter turnout among all age groups, their political orientation is not entirely homogeneous (although leaning towards the conservative), and they do not form a distinct, unified political force (Hinrichs 2002).

In some countries, the desire to exchange income for leisure, together with deliberate government policies, induced a trend towards early retirement (Busse et al. 2003). Early retirement policies are intended to reduce youth unemployment under the hypothesis of a fixed number of

**Figure 1** Change in population age distribution between 1980 and 2000, children and elderly as % of total population



us to explore the extent to which expenditure on the elderly people has increased at the expense of expenditure on families with children.

However, it is necessary to acknowledge some drawbacks with the data.

First, there are reasons to be anxious about the consistency of the classification of expenditure between countries. Some countries use different means to deliver the same benefits. So, for example, the OECD classification of public social

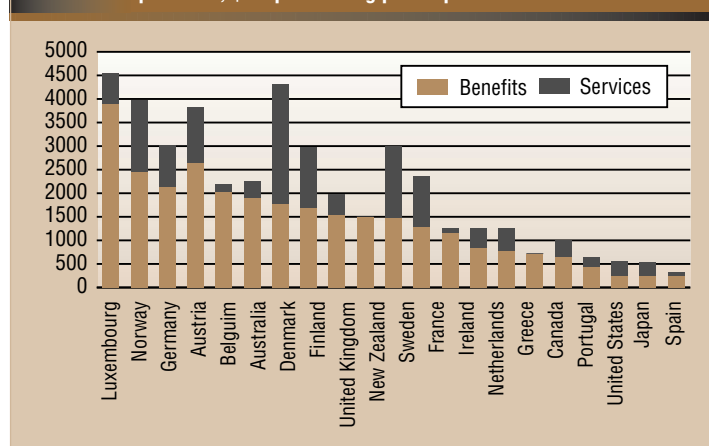
expenditure does not include tax expenditures, mandatory occupational provision, occupational benefits, housing benefits, health and education expenditure, or child support (alimony). Nor does it take account of the fact that benefits are taxed back in some countries. Adema (2001) at OECD has been working to take account of some of these problems and to incorporate some of these types of expenditure on a more consistent basis, but as yet there are no net social expenditure data for different age groups.

Second, for the same reasons, there are reasons to be anxious about the consistency in the classification in any one country over time. Thus, for example, some countries have turned elements of their cash benefits for children into tax benefits in recent years.

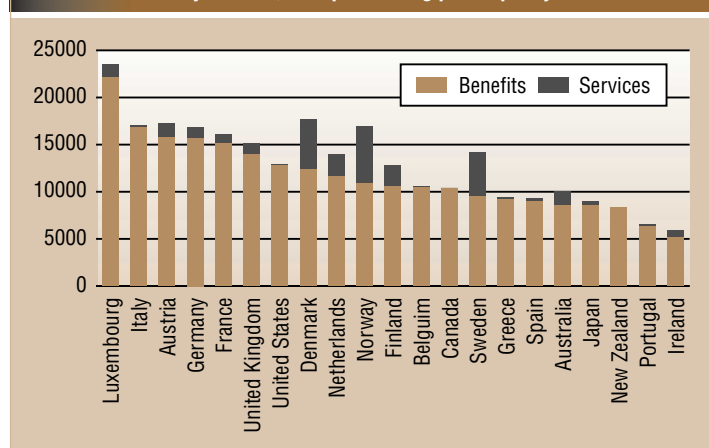
Finally, the OECD takes time to accumulate the data from national sources, and the latest data available are for 1998.

Given the first two of these reservations we need to be rather tentative about the conclusions of this analysis.

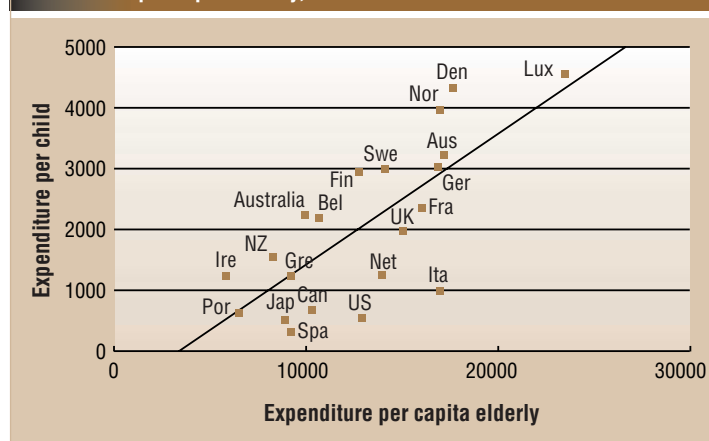
**Figure 2 Expenditure on family cash benefits and services in 1998 per child, \$US purchasing power parities**



**Figure 3 Expenditure on cash benefits and services per capita elderly in 1998, \$US purchasing power parity**



**Figure 4 Expenditure on family benefits and services per capita child by expenditure on benefits and services for the elderly per capita elderly, 1998**



### Per capita expenditure

There is large variation between countries in the amount they spend on children, and big differences in the balance between spending on cash benefits and services. In Figure 2 it can be seen that Luxembourg and Denmark provide by far the most generous family cash benefits and services per child. In contrast, Portugal, the United States, Japan and Spain spend less than 10 per cent of the spending of those two countries. The Nordic countries and France have the highest proportion of their expenditure devoted to services. These big variations in expenditure on families indicate that some welfare states are supporting their families with children more than others.

Are they doing so at the expense of their elderly? Spending on the elderly per capita is higher in all countries than spending on children per capita (see Figure 3). Also there is rather less variation in spending on the elderly – most countries were spending between \$10,000 to \$15,000 per capita elderly in 1998. Compared with spending on cash benefits, spending on services for the elderly is far less significant and again it is the Nordic countries (and the Netherlands) which have the highest proportion of their spending on services.

Figure 4 plots spending on the elderly per capita against spending on families per child. It can be seen that there is a positive association – that is, countries which spend more on their children are also spending more on their elderly and vice versa. If countries as a whole were spending on the elderly at the expense of children we might expect to observe a negative relationship. Nevertheless there are some interesting outliers to the general trend. To the right and below the line are countries including the Netherlands, Italy and the United States which are relatively more generous to their elderly than to their children. To the left and above the line are countries which relatively favour children, including the Nordic countries and Australia.



*Welfare of future pensioners is conditional on today's children, who will need to have sufficient human capital to finance the coming pension burden.*

Nordic countries had small reductions after 1995. Most other countries either show a general upward trend in spending on family cash benefits and services over the 1980s and 1990s (including Australia, France, Germany, Ireland, and Greece), or relatively stable expenditure as a proportion of GDP (especially the other Anglophone countries and Japan).

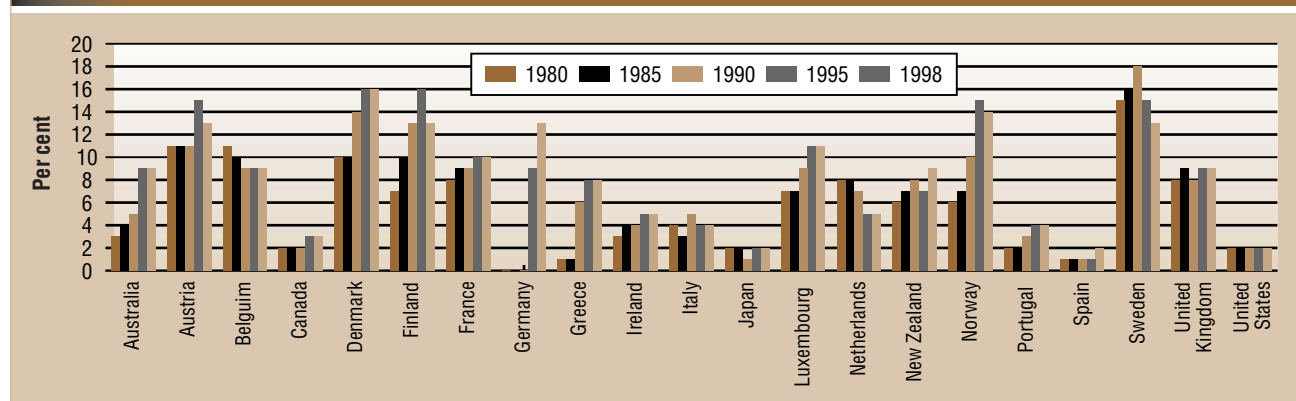
### Expenditure ratio

As we have seen, all countries spend more per elderly person than they do per child. Figure 6 shows the results of a calculation of expenditure per child as a proportion of expenditure per old person, and how this has changed over time. Expenditure on family benefits and services per child as a proportion of spending on the elderly varies from under 5 per cent in Italy, Japan, Spain and the US to nearly 25 per cent in Belgium, Denmark, Finland and Norway. Between 1980 and 1990 the family expenditure per child in Sweden was over 35 per cent of the expenditure per capita elderly. This percentage had dropped to almost 20 per cent by 1998. Relative expenditure on families with

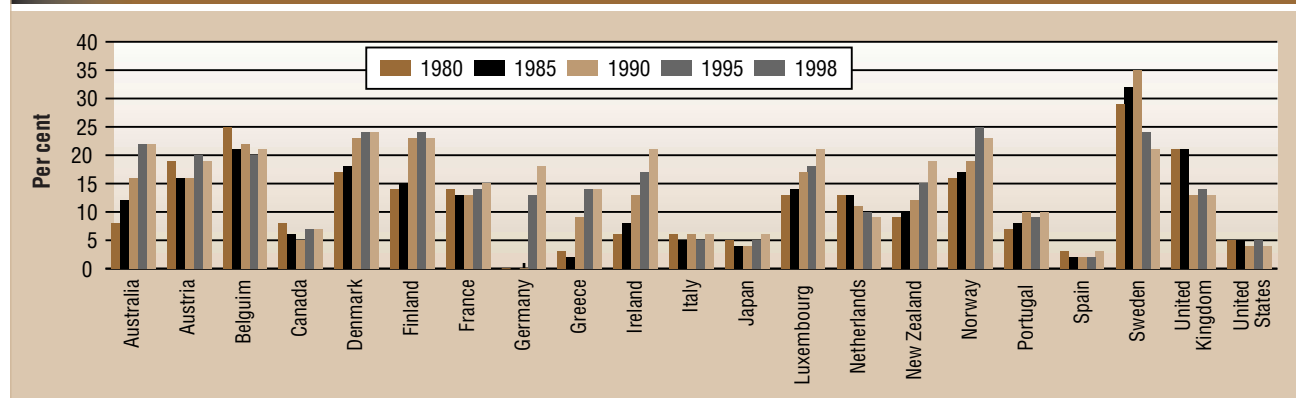
### Expenditure over time

Nevertheless, is there any evidence that expenditure on families with children has been declining as countries face the increased needs of a rising elderly population? There does not seem to be a consistent trend in expenditure on family cash benefits and services per child (expressed as a percentage of GDP) over time. In Figure 5 only Belgium and the Netherlands show a consistent downward trend in family expenditure. Sweden's expenditure also fell after 1990 and the other

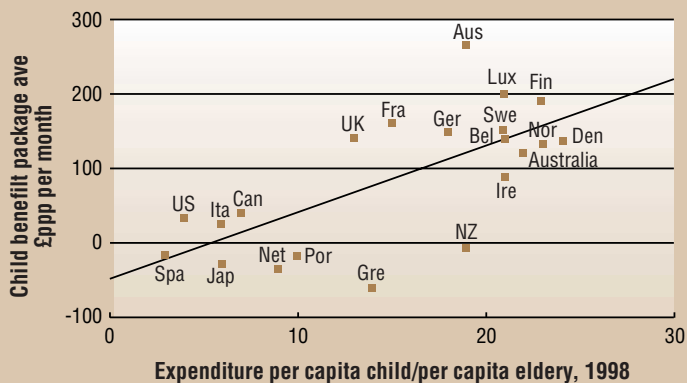
**Figure 5 Expenditure on family cash benefits and services per capita child as % of per capita GDP**



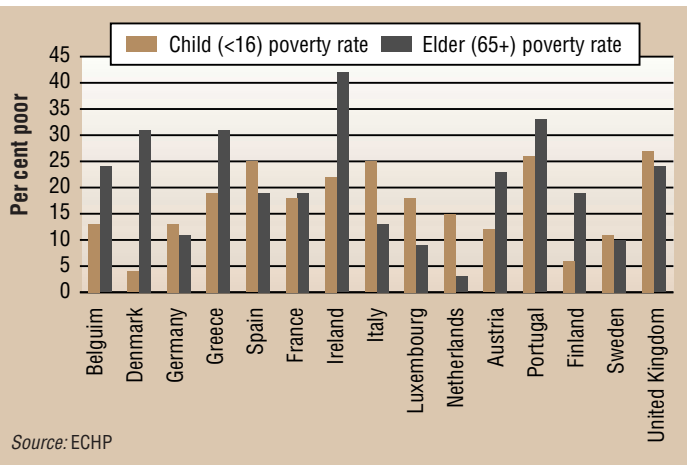
**Figure 6 Expenditure per child as percentage of expenditure per capita elderly, 1998**



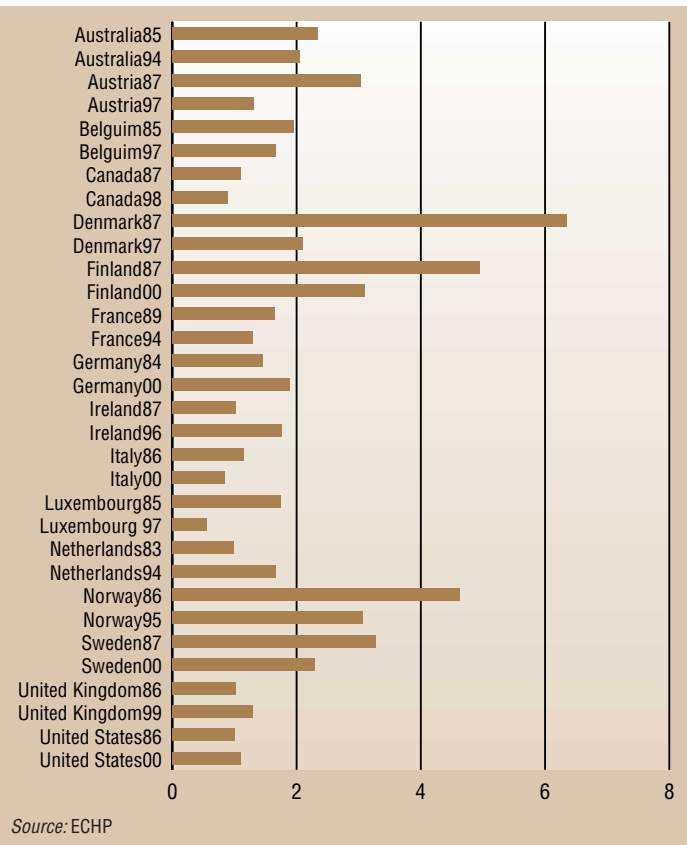
**Figure 7** Level of child benefit package (in 2001 £ ppp) by child/elderly expenditure ratio in 1998



**Figure 8** Poverty rates <60 per cent of median equivalised income (2000)



**Figure 9** Changes in the relative risk of poverty elderly/children



children as against the elderly also fell in the Netherlands, the United Kingdom, Sweden and Belgium. However, most countries either experienced an improvement in spending on children relatively to the elderly (Australia, Denmark, Greece, Ireland, Luxembourg and New Zealand) or a stable pattern.

There is really not much evidence here of a consistent movement of spending towards the elderly at the expense of children. Rather it appears that in some countries this may be happening, in others equity is being maintained at different levels of generosity and in others families with children have actually improved their relative position – possibly at the expense of the elderly.

There is no doubt that countries do make choices. A comparative study by Bradshaw and Finch (2002) produced an estimate of the overall value of the child benefit packages in 22 countries for an illustrative sample of model families with children. Figure 7 shows the relationship of the average value of the child benefit package in purchasing power parities in July 2001 and overall spending on family benefits and services in 1998 (so there is an unfortunate disjunction between the years).

It appears that there are two clear groups. In the bottom left hand corner of Figure 7 there are the low spenders on families with children compared with the elderly who also have comparatively low or non-existent child benefit packages. These include the United States, Italy, Canada, Spain, Japan, the Netherlands and Portugal. In contrast, at the top right hand of the Figure are the countries with large child benefit packages spending relatively more on families with children than the elderly. These include the Nordic countries, and Australia. The other countries either fall between or are outliers (possibly because of the disjunction in dates).

### Poverty

So far we have considered the question of whether families with children have been losing out compared with the elderly purely in relation to expenditure – *inputs*. It is possible to explore the question using *outcome*, in terms of risk of poverty. The latest European Community Household Panel Survey shows that in 2000 in nearly half the European Union countries (Germany, Spain, Italy, Luxembourg, the Netherlands, Sweden and the United Kingdom) the risk of poverty is higher for children than for older people (see Figure 8).

How have relative poverty rates changed over time? On the basis of harmonised questionnaires on detailed distribution and poverty indicators derived from national micro-economic data, Förster and Pellizzari (2000) found that in 11 out of 15 OECD countries the poverty rate of children and young people increased in the mid 1990s relative to that of the elderly population.

Figure 9 draws on more recent data from the Luxembourg Income Study and shows changes in the relative risk of poverty<sup>2</sup> between the mid 1980s and the latest available year. Thus, for example, in Australia in 1985 older people had a poverty rate 2.35 times that of children. By 1994 that ratio



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have been struggling to reform their public pension system, often facing considerable resistance from their populations, and often without much success. Also the elderly versus families with children trade-off is not the full picture. In many countries a substantial extra burden on the social security systems is being generated by early retirement that is not accounted for in our analysis. There is clearly a need for further research on whether equity between generations is suffering in the face of ageing.

had fallen to 2.05. Thus old age poverty had fallen compared with child poverty. This was true for the majority of countries in the analysis. The exceptions were Germany, Ireland, the Netherlands, the United Kingdom and the United States.

## Conclusion

Esping-Andersen and Sarasa (2002) have argued that the welfare of future pensioners is conditional on today's children, who will need to have sufficient human capital to finance the coming pension burden. Further, child poverty has long-term negative consequences for both the individual and society. Knowledge-intensive economies require well educated workers. Among the outcomes of child poverty are low educational attainment, resulting in low paid jobs and the repetition of the poverty cycle. High child poverty rates will bring rise to a large poorly skilled workforce not well equipped to raise the required funds to provide social security to the increasing numbers of elderly.

In this article we have found that if there is generational inequity it does not stem from demography alone. Nations make choices about the level of resources they commit to children and the elderly, and the countries that are most generous to children also tend to be most generous to the elderly.

At the margin there is inevitably a trade-off between spending on the elderly or children, or on something else. The most recent comparative expenditure data shows that there is little evidence that ageing has resulted in the trade-off shifting systematically in favour of the elderly at the expense of children except in the Netherlands, Sweden after 1990, and the United Kingdom after 1985. The other OECD countries seem to have maintained generational equity in expenditure or increased expenditure on families with children compared with (and possible at the expense of) the elderly. But as far as poverty is concerned, the majority of countries do reveal an increase in child poverty relative to elderly poverty.

However, both the expenditure and poverty data in this analysis are now rather old. Many countries

## Endnotes

- 1 Countries included in the analysis: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Japan, Luxembourg, Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, United Kingdom, United States
- 2 Calculated as the elderly poverty rate divided by the child poverty rate, so the ratios are a measure of the differences in the risks of being poor.

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