Ageing: Its economic implications

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Outline

- A framework for thinking about ageing and its economic impacts
- Sectoral impacts
- Pensions and old age income support
- Issues for the healthcare sector

A Framework

Components of “ageing”

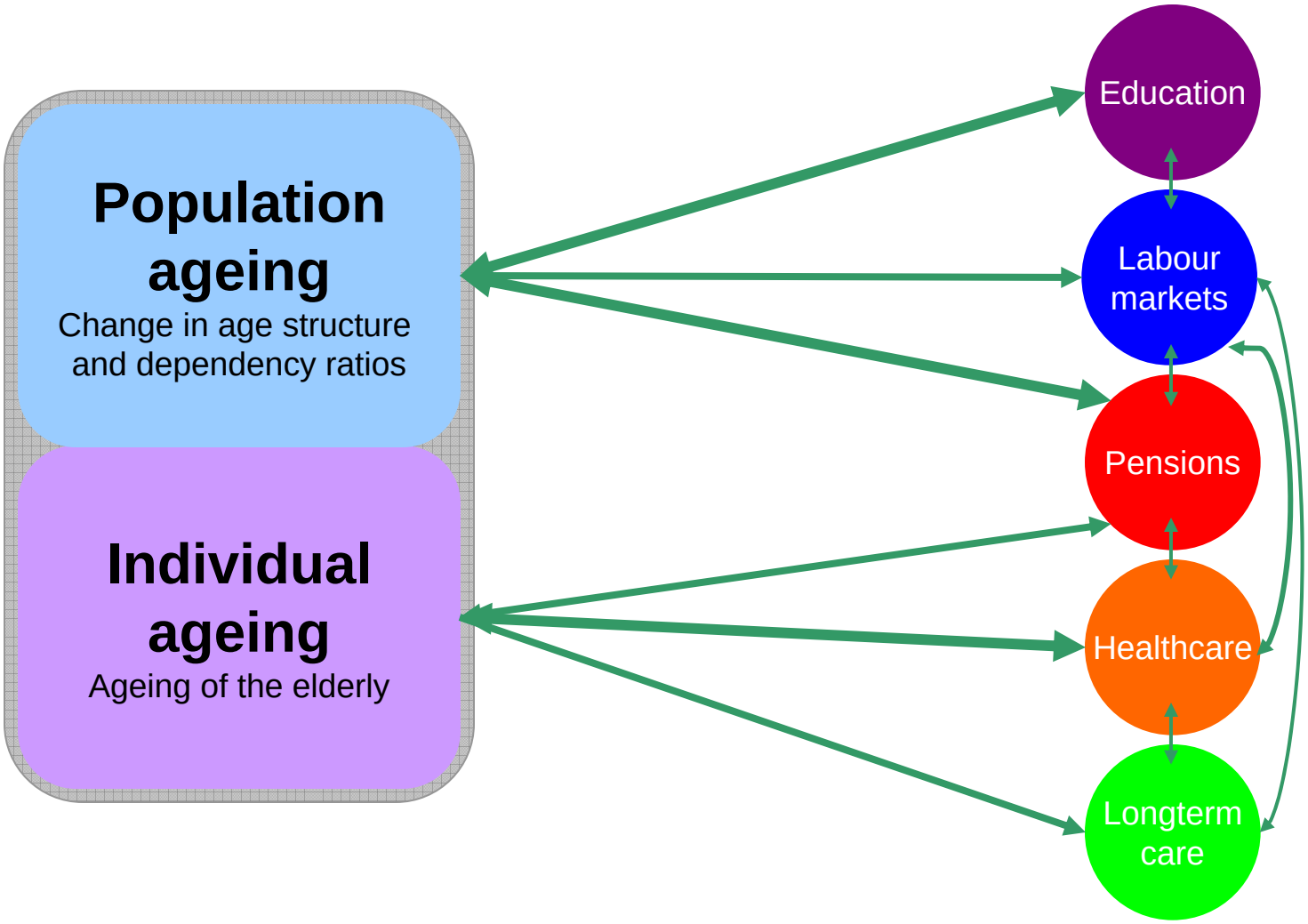
Population ageing

- The change in age structure of the population due to changes in mortality and fertility
- An increase in the share of the population in older age groups
- An increase in the ratio of older persons to younger adults

Individual ageing

- The increase in the numbers of adults at older ages
- The increase in the time spent at older ages

Sectoral impacts of ageing



Sectoral Impacts

Education and labour markets

- Education
  - Opportunity and need to shift focus of investment from primary education to secondary and post-secondary education
  - Provision for life-long learning and reskilling
- Labour markets
  - Need to support and increase labour force participation (e.g., women)
  - Encouraging and facilitating people to work longer
  - Encouraging greater labour market flexibility, e.g. part time work for older adults/women, moving between sectors

Long-term care

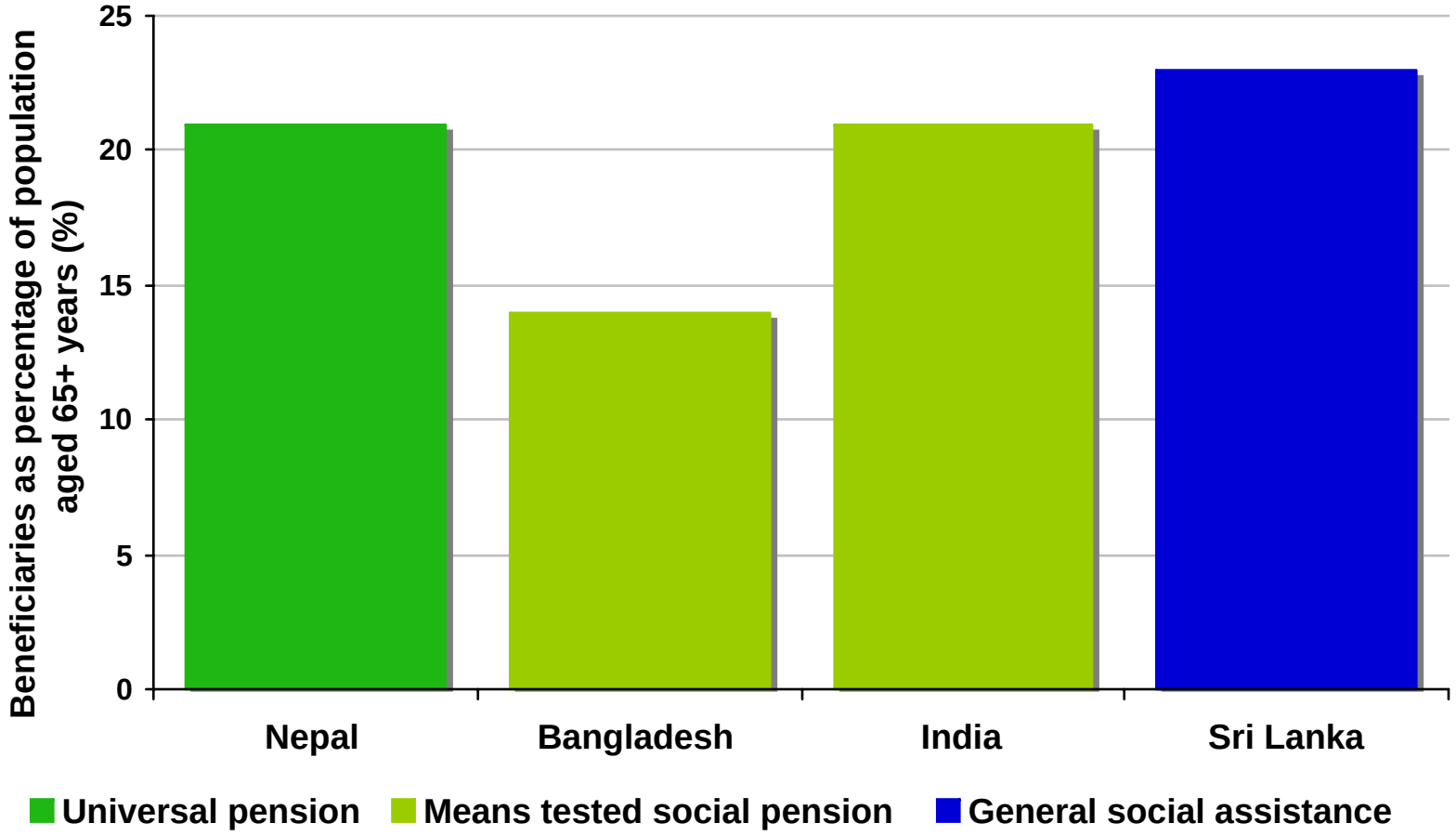
- Older elderly (>80 years) more likely to be physically weak/frail, disabled and dependent on others for care
- Economic development and ageing implies:
  - Increasing need for LTC
  - Decrease in ability of informal/household care systems to cope, with growing need for formal provision
    - Reduced number of women carers, smaller family sizes, increased labour force participation, changing social norms
- Emergence of LTC as a distinct area of social provision, separated from healthcare systems
  - Shift from informal care to formal care systems seen even in more advanced Asian countries, e.g., Japan, Korea, Malaysia, Singapore, Sri Lanka, Thailand
  - In developed countries, costs reaching 1-4% of GDP

Pensions

Pensions and old age income support

- Ageing implies increased numbers of retired older adults whose consumption must be supported by production of current workers
  - Reduced biological capacity to work
  - Social and labour market norms and rules
  - Increased desire for leisure
- Decline in co-residence, and increase in monetisation of economy creates need for more formal systems of income support
  - If not pensions
  - …. then social transfers

Pensions or not?



The pension debate since the 1980s

- Not disputed:
  - Percentage of population in retiring requiring income support will increase in all countries
  - The value of the financial transfers in existing systems will grow
  - Formal systems required
- What has been disputed:
  - How these systems should be financed - PAYG vs "Pre-funding"
  - Global debate affecting all countries
    - Dispute has centered on the financing mechanism, and the extent of government intervention and voluntary action

Funding versus PAYG

- Most pension systems in developed countries/Latin America, and most civil service schemes started as pay-as-you-go (PAYG), funded by contributions from workers or taxes
  - USA, UK, Japan, France, Germany, India, Sri Lanka, Thailand, etc
- Initial impact of ageing was to destabilise these systems, and make many think them unsustainable
  - Process of “reform” from the 1970s - Major source of political controversy in both developed and developing countries
  - The “Funding” side has advocated shifting away from PAYG schemes to pre-funded schemes backed by investments
  - Greatest shift in favour of pre-funding occurred in Latin America, mostly under military dictatorships, and in some East European former communist states
  - Considerable advocacy of funding by World Bank, etc

An assessment of the debate

- The push for funding can be largely seen as a case of ideology and bad economics
  - Who says this? IMF, OECD, most leading economists, WB Chief Economist (Stiglitz, 2000)
  - In practice, no advanced OECD economy has changed its pensions financing to funding, and also few Asian countries,
  - … nor has the WB changed its staff pension scheme
- Why?
  - Funding does not make the economic costs of pensions any lower, and may make them higher in the short-run
  - Funded pensions cannot provide coverage to the informal sector, low-wage earners, or to current older workers close to retirement
  - Governance and insurance problems can be even greater with funded schemes than PAYG

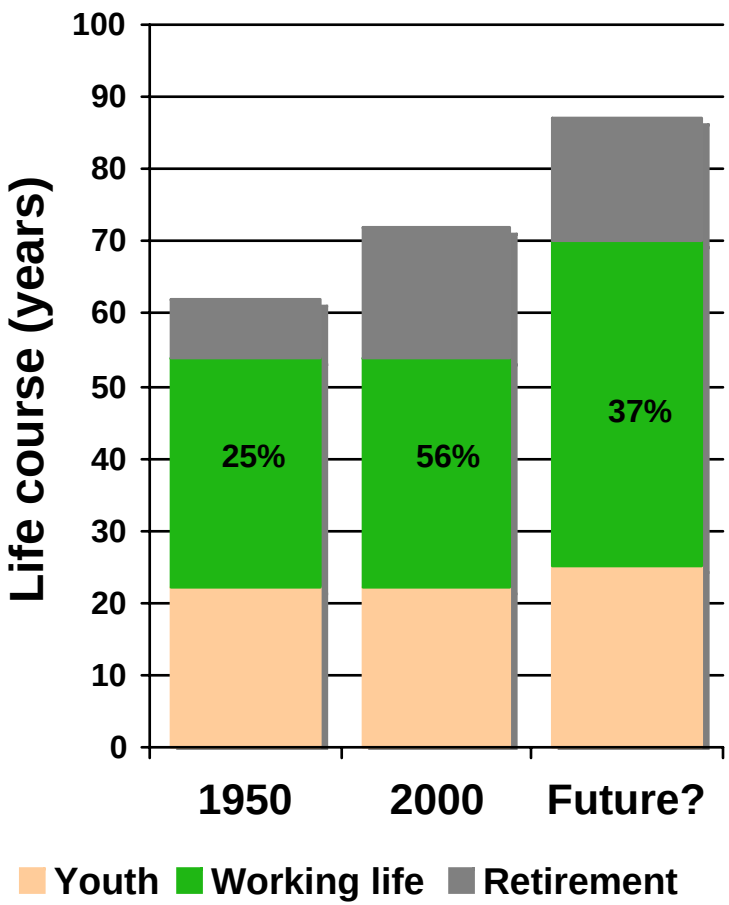
The parametric reform of pension systems

- Incremental reforms of pension systems have taken centre place in developed economies

- **Parametric reforms**
  - Increases in retirement ages (to 70+ years)
  - Changes in indexation & reduction in pension benefits
  - Greater adjustment of pensions for early retirement or part-time work

Importance of raising retirement ages

The need to change work-life norms



- The increase in life expectancy has not been accompanied by an increase in working lives
- Result has been increasing ratio of years spent in retirement to those spent in work
- What ever system is used, this means that a greater share of the potential consumption of workers must be diverted to the elderly

Challenge for health system

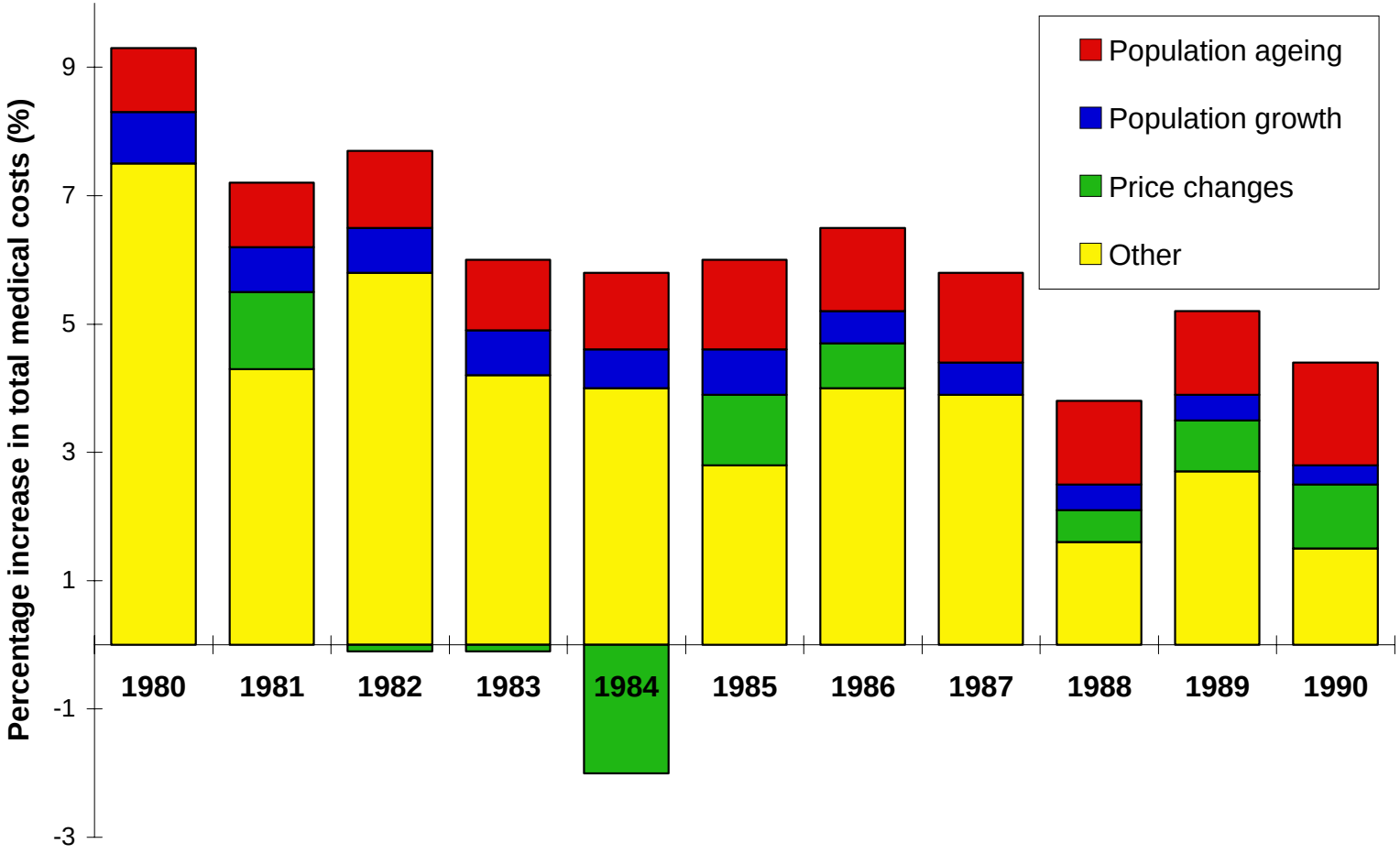
- To enable people to be able to and to want to work longer

Issues in Healthcare Sector

Impact of ageing on future healthcare costs

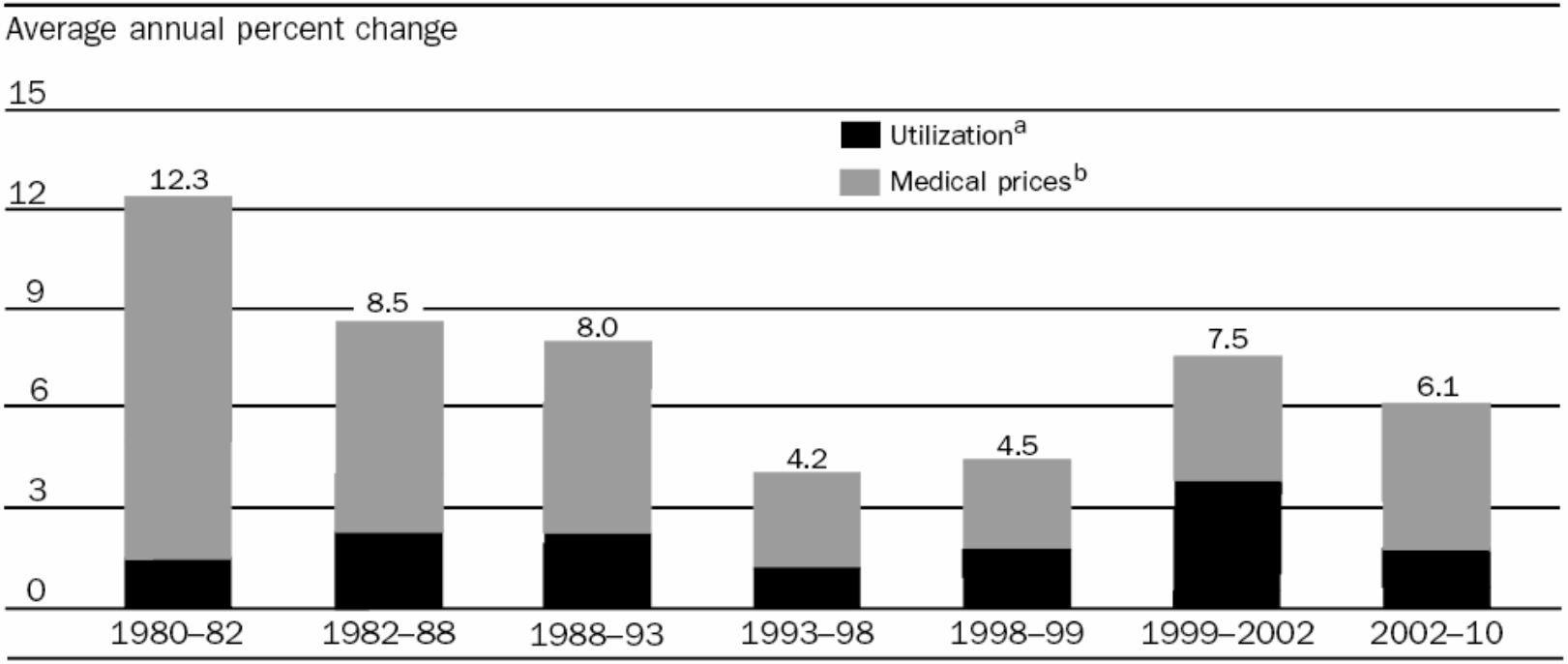
- Global experience
  - Ageing is not as large a factor as often feared
  - Cost drivers of future health spending
    - Ageing (+)
    - Changes in health behaviour (+)
    - Productivity change in public sector and price inflation in private sector (- / +)
    - Technology (+)
    - Morbidity compression (-)

Cost drivers, Japan 1980-90



Cost drivers, USA 1980-2010

Factors Accounting For Growth In Per Capita Personal Health Care Expenditures, Selected Periods 1980–2010

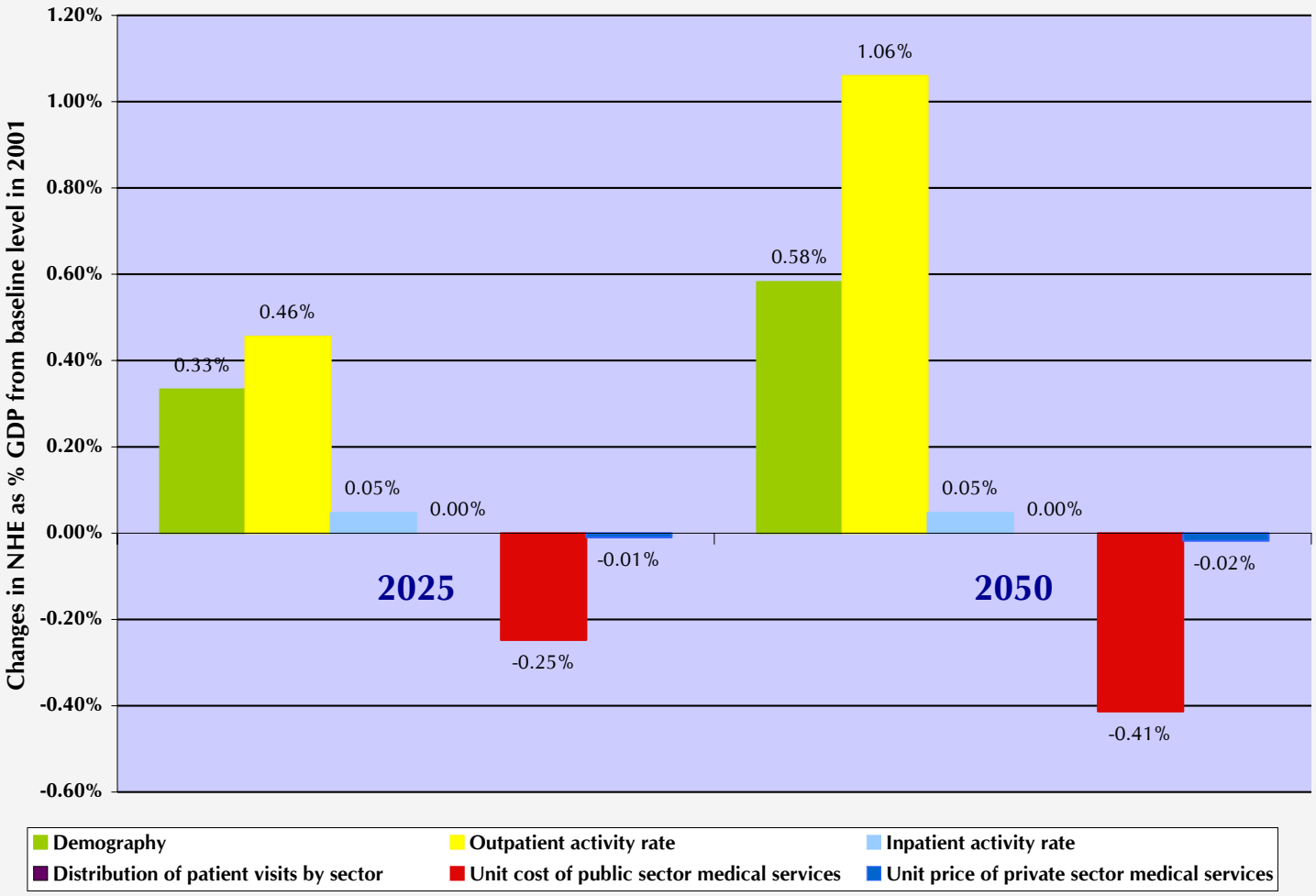


SOURCE: Health Care Financing Administration, Office of the Actuary, National Health Statistics Group.

[a] Includes quality and mix of services. As a residual, this factor also includes any errors in measuring prices or total spending.

[b] Medical inflation is calculated using the personal health care (PHC) chain-type index constructed from the Producer Price Index for hospital care, Nursing Home Input Price Index for nursing home care, and Consumer Price Indices specific to each of the remaining PHC components.

Cost drivers, Sri Lanka 2001-2051



Implications of ageing projection models and global experience

- Countries need to focus on controlling those cost drivers which are subject to policy leverage
  - Public sector productivity gains
  - Control of private sector price inflation
  - Controlling adoption of high-technology
  - Promoting healthy ageing
- These imply increased role for public financing (and reduced role for private)
- Need to inform policy with forecasting models

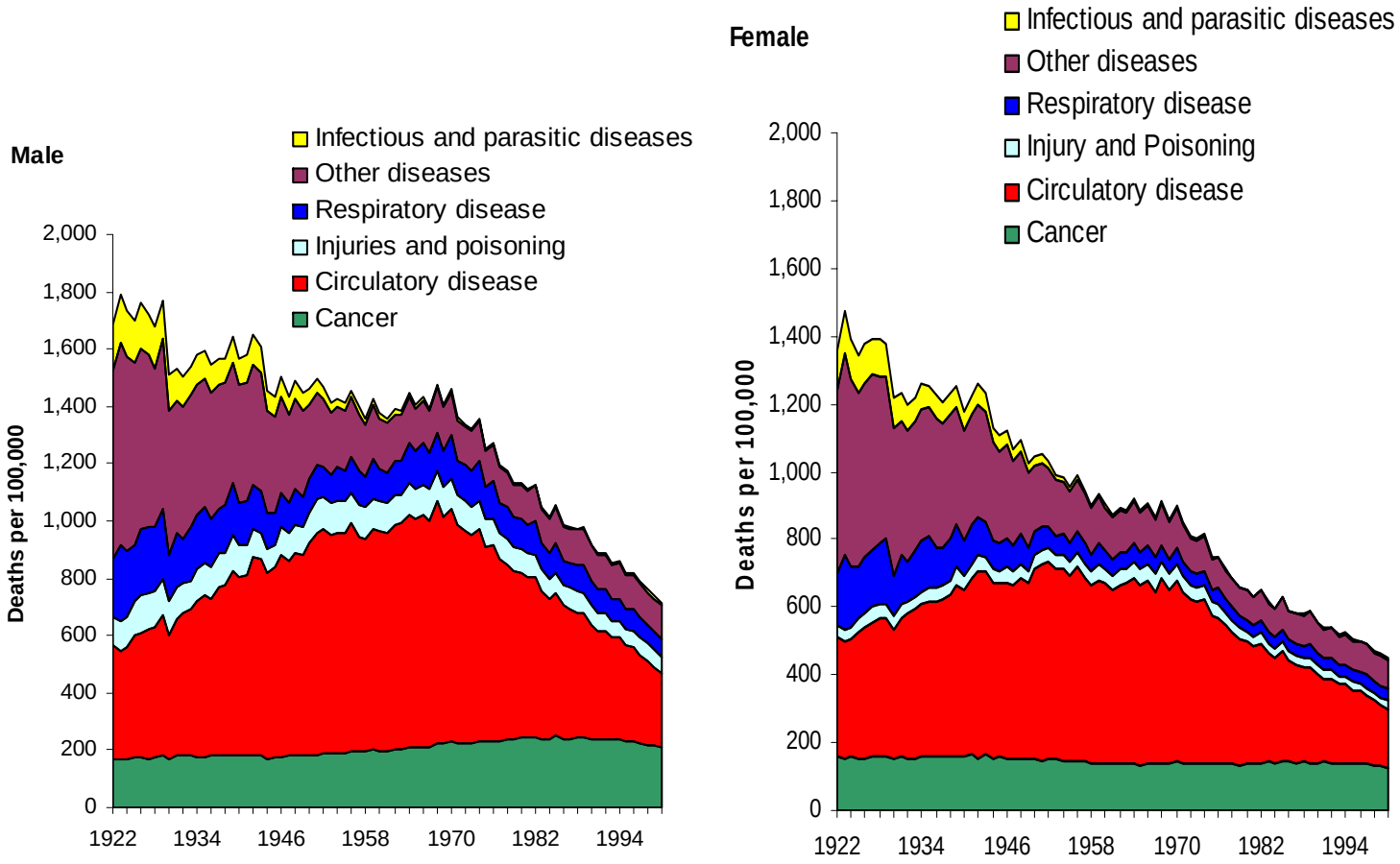
Morbidity compression

- Morbidity compression is the delay in onset of disability and ill-health to higher ages with increasing life expectancy
- Evidence for this in many developed countries:
  - USA 1970-2005: Declines in mortality, disability and morbidity in older adults in most age groups (1-3% per year)
- Consequences:
  - Reduction in impact of ageing on health costs
  - Increase in healthy life expectancy extends working lives
- Problem:
  - Until recently, explanation for morbidity compression was unknown

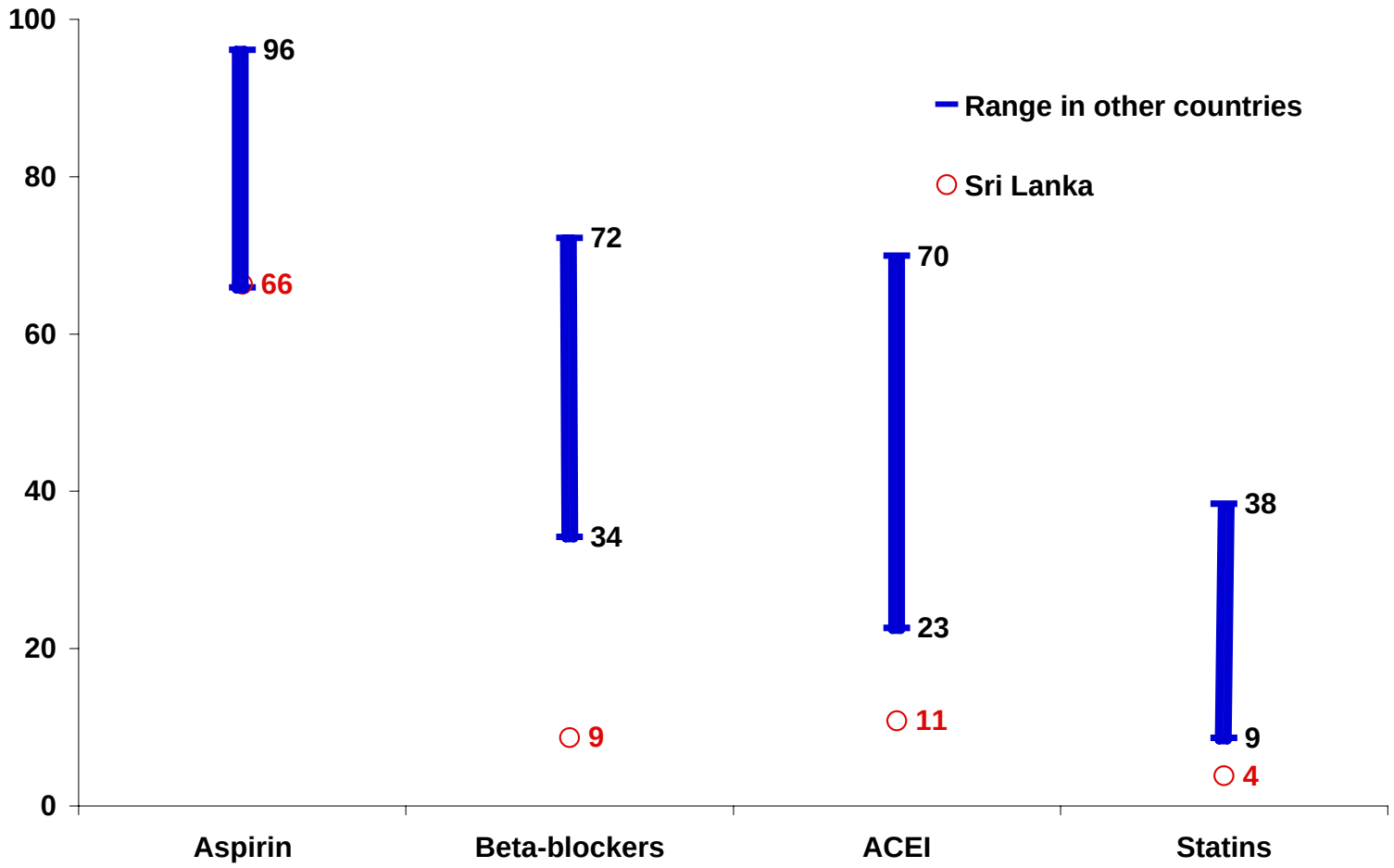
Recent evidence on morbidity compression and NCDs

- Developed countries (2004-2007)
  - Indicates that a major driver of morbidity compression is medical intervention for NCDs, particularly IHD medications
  - Sub-clinical IHD may explain the onset of frailty in very elderly
- Developing countries - Limited evidence on trends
  - Almost no data on trends in developing countries, but SL evidence indicates no compression
  - Evidence indicates systematic failure to adopt proven, cost-effective secondary treatments of NCDs, particularly IHD
  - Possibility that negative trends in adult mortality, morbidity, etc may be linked to failure to invest in treatment of chronic diseases
  - SL Aging Study - NCDs and chronic disease the largest single factor explaining early retirement by workers

Age-standardised death rates for major causes of death, Australia 1922–2000



Under-treatment of IHD in diagnosed patients, Sri Lanka 2003



Implications for developing countries

- Declines in mortality and disability in older adults in developed countries increasingly driven by medical interventions for NCDs
  - Secondary prevention >> primary prevention
- Gains may not be seen in developing countries:
  - Systematic failure to adopt cost-effective, medical treatments for NCDs
  - Need to reorient investment towards secondary prevention, particularly medications
- Failure to invest in NCD treatment will have negative impacts on pensions, labour markets and long-term care

Implications

- Ageing will have multiple, interacting impacts
  - Must focus on healthy ageing and extension of working lives
- Strengthened public sector financing and management of health sector should be basis for mitigating healthcare costs with ageing
- Need for shift from primary prevention focus to balanced investment in treatment and prevention of NCDs
  - This will require upgraded primary care systems based on family medicine specialist model
- Need for research at regional level onto understanding morbidity compression and NCD trends
- Enhanced regional collaboration on policy research related to ageing responses, similar to that of OECD