Mexico and the Challenge of Global Aging

Presentation by

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This could be the news in the year 2023.

- The GDP of Europe has not grown for a decade.
  Economist
  “Permanent Aging Recession?”

- France enacts 5th payroll tax hike in 5 years.
  Le Monde
  “Pension Party tells Business Leaders: No Choice, Defense Already Zeroed Out”

- Japan, world’s largest debtor, asks IMF for bailout.
  Financial Times
  “Beijing Says No More Credits for Tokyo”
The world stands on the threshold of a great revolution called global aging.

Global aging could overwhelm government budgets in the developed countries, destabilize the global economy, and even overturn the geopolitical order.

There is still time to avert crisis. But time is running short—and the problem is worse than is generally supposed.
The developed countries fail to confront their aging challenge…

- Mexico could face a future of widespread capital shortages, declining export markets, and rising protectionism.

The developed countries enact timely reforms…

- Mexico and the developed countries both reap huge benefits from the growing integration of their economies.
The whole world is aging—and today’s developed countries are leading the way.

Source: UN (2001)
Global aging is what happens when people start having fewer babies.

Lower fertility shrinks the relative number of younger people in the population.
Fertility in the developed economies has fallen far beneath the replacement level.

Source: UN (2001)
Two forces behind global aging.  Force two: rising longevity.

Global aging is what happens when people start living longer.

Longer life spans enlarge the relative number of older people in the population.
Life expectancy has risen more over the past 50 years than the previous 5,000.

Source: UN (2001)
Global aging poses five challenges for today’s developed countries.

- the **FISCAL** challenge of rising retirement costs
- the **LABOR** challenge of a graying and shrinking workforce
- the **GROWTH** challenge of stagnant markets
- the **FINANCIAL** challenge of asset devaluation and capital-flow swings
- the **GEOPOLITICAL** challenge of demographic power shifts and tight defense budgets
The fiscal challenge.

- Declining support ratio of workers to retirees
- Rising cost of pay-as-you-go retirement benefits
- Large tax hikes, large benefit cuts, or exploding public debt
- Growing political paralysis over unpopular budget choices
On average, public retirement benefits are due to grow to one-quarter of GDP.

Public Retirement Benefits as a Percent of GDP, Developed Country Average, * 2000 and 2050

The labor challenge.

- Shrinking workforces and labor shortages
- Aging workers and aging union memberships
- Pressure to increase immigration—and popular backlash
- Growth in cross-border outsourcing
In many fast-aging countries, the size of the working-age population will shrink dramatically.

Percent Change in the Working-Age Population (Aged 15-64), 2000 to 2050

Source: UN (2001)
The growth challenge.

- Long-term zero or negative GDP growth
- Declining rates of savings and investment
- Falling demand for infrastructure (highways, housing) and capital goods (offices, mills)
- Shrinking consumer markets and growing pressure for protection and cartels
Some developed economies may soon see GDP decline even in years of full employment.

ITALY: Past and Projected Growth in Employment and Real GDP*

*Assumes 1.0% annual productivity growth
Source: OECD (2001) and CSIS (2002)
The financial challenge.

- Danger of “Great Depreciation” in financial markets when Boomers retire
- Unsustainable government borrowing to fund pensions
- Possible collapse of regional economic entities like the EMU
- Capital-flow reversals: Emergence of developed debtors (Japan? Germany?) and developing creditors (China? Mexico?)
Yawning public pension deficits threaten to devour the savings of the developed world.

Growth in Deficit* of G-7 Public Pension Systems, as Percent of G-7 GDP

* Deficit = Annual cash deficit plus accrued interest on prior years
The geopolitical challenge.

- Will youthful developing societies...
  - feel demographic pressure to expand?
  - translate faster economic growth into global leadership?

- Will aging developed societies...
  - find the resources to meet their security commitments?
  - be willing to sacrifice for the sake of the future?
If demography is destiny, global leadership may pass from the “First” to the “Third” world.

12 Largest Countries Ranked by Population

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<tr>
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<th>1950</th>
<th>2000</th>
<th>2050</th>
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<tr>
<td>1</td>
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<td>Russian Fed.</td>
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<td>5</td>
<td>Japan</td>
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<td>Brazil</td>
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<td>9</td>
<td>United Kingdom</td>
<td>Japan</td>
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<td>10</td>
<td>Italy</td>
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<td>11</td>
<td>France</td>
<td>Mexico</td>
<td>Mexico</td>
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<td>12</td>
<td>Bangladesh</td>
<td>Germany</td>
<td>Philippines</td>
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Source: UN (2001)
The developed countries must:

- Reduce the cost of old-age benefit systems
  - Scale back pay-as-you-go programs
  - Put in place funded alternatives—like personally owned accounts

- Pursue “out of system” strategies that boost the size of the workforce and economy
  - Increase employment among working-age adults
  - Encourage later retirement
  - Reward families for raising children
Globalization is an essential strategy for an aging world.

- There are great advantages to cooperation between the developed and developing worlds:
  - immigration and outsourcing
  - cross-border investment

- Bottom line: An open global economy allows young people to support old people across international borders.
While its population is still young and growing, Mexico needs to...

- Complete the reform of labor markets and capital markets that it began in the 1980s
- Invest heavily in modern infrastructure and an educated workforce
- Prepare for its own age waves that looms just over the horizon
Mexico’s demographic dividend: Declining dependency ratios.

Number of "Dependents" (Under Age 20 plus Aged 65 & Over) per 100 Working-Age Adults

Source: UN (2003)
Mexico’s demographic dividend: A fast-growing working-age population.

Percentage Change in the Working-Age Population (Aged 20-64):
2000-2025

- **US**: 19.4%
- **Mexico**: 55.0%

Source: UN (2003)
Mexico will grow old in its turn.

Percent of Population Aged 65 & Over

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<th>Year</th>
<th>Mexico</th>
<th>US</th>
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<tr>
<td>2000</td>
<td>4.8%</td>
<td>12.3%</td>
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<tr>
<td>2025</td>
<td>9.5%</td>
<td>17.8%</td>
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<tr>
<td>2050</td>
<td>20.0%</td>
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Source: UN (2003)
Mexico enjoys considerable advantages in confronting the aging challenge.

- No large unfunded liabilities for pay-as-you-go retirement systems
- Strong extended families that serve as informal care networks for the elderly
- Time to learn from the mistakes of its older and more affluent neighbors
Mexico must overcome a large disadvantage.

The United States and the other developed countries got rich before they grew old.

Mexico may confront an old-age dependency burden equal to the United States—but with one-third the per capita income.
We live in an era defined by many challenges, from global warming to global terrorism. None is as certain as global aging. And none is likely to have such a large and enduring effect on the shape of national economies and the world order.