Aging Population Poses Global Challenges
Health Care, Other Rising Costs to Strain Budgets in U.S. and Abroad

By Jonathan Weisman
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When President Bush delivers his State of the Union address tonight, his prescriptions for Social Security are likely to vault that issue to the front of the nation's political agenda. But Social Security's financial problems are a relatively small sliver of the far larger challenges posed by an aging population, economists say.

From untamed health care programs to military pensions, housing and heating assistance to coal-miners' benefits, programs for the elderly have proliferated and grown more generous, even in the face of an aging trend that demographers have long seen coming. In that light, the fight over Social Security marks only the beginning of a national debate over the cost of a graying society -- and the inevitable reallocation of resources that is sure to produce winners and losers, in the United States and around the world.

"The question is whether we can support the elderly with a decent standard of living without imposing a crushing burden on the young," said Richard Jackson, director of the global aging initiative at the Center for Strategic & International Studies. "Whether we can is a real concern."

In just 10 years, spending on the elderly will total nearly $1.8 trillion, almost half the federal budget, according to new Brookings Institution and Congressional Budget Office projections. That is up from 29 percent in 1990 and 35 percent in 2000.

The bulk of that growth is spending on the federal government's two largest health care programs, Medicare and Medicaid. Their combined costs are projected to more than double, to a combined total of $1.2 trillion in 2015 from $473 billion last year. Social Security spending is expected to rise to $888 billion from $492 billion in that span.

To straighten out Social Security's financial problems, Bush will probably cut promised benefits for future retirees and divert up to a third of Social Security taxes to private investment accounts. The White House expects the investment gains in those accounts to mitigate -- if not erase -- the cuts in guaranteed benefits.

Bush has offered no plan to slow the sharper growth in federal health care spending beyond his hope that the prescription drug benefit he approved for Medicare will cut down on costly hospitalizations and surgeries.

Other countries are not likely to help foot the bill for the United States' aging population, as they currently do with the U.S. trade and budget deficits. The populations of Japan, Germany and other countries that have large pools of savings are aging even faster than the United States', and as they do, retirees will start to spend their nest eggs, sapping the capital that now helps drive business expansion and rising living standards worldwide, including in the United States.

China, because of its one-child policy, will face a demographic crisis of its own, and India, though growing fast, cannot hope to accumulate enough capital to help, international economists say.

No challenge "is as certain as global aging," said the Center for Strategic & International Studies in another recent study, "and none is as likely to have as large and enduring an effect -- on the size and shape of government budgets, on the future growth in living standards, and on the stability of the global economy and even the world order."
Some economists and interest groups say such fears are overblown. The real problem, they say, lies not so much in demography but in a health care system that is the world’s most expensive and least efficient. The cost of Bush’s Medicare prescription drug benefit alone -- $8.1 trillion in 75 years -- dwarfs the $3.7 trillion estimated shortfall in Social Security in that stretch.

Get control of federal health care costs -- through better use of technology and better management of chronic illnesses and disabilities -- and the problem of an aging population will look a lot less intractable, said John Rother, policy director at AARP, the advocacy group for retirees and near-retirees.

Europe and Japan have already entered the demographic crunch that American policymakers fear, Rother said. And although economic growth in those countries has slowed, standards of living have remained high. If the U.S. economy could better harness the strength of an elderly workforce, through job creation and volunteerism, he said, some of the anticipated economic impact of a growing pool of retirees could be mitigated.

Besides, technological progress will continue to make workers more productive, even as their numbers diminish relative to retirees, said Dean Baker, co-director of the liberal Center for Economic and Policy Research.

"Previous generations had sacrificed to build our infrastructure, to invest in technologies" that help current and future workers, Baker said. "If they're paying a larger amount of taxes to help their parents, I don't see where the harm has been done."

But such arguments are held by a minority. Many liberals, such as Isabel V. Sawhill, director of economic studies at the Brookings Institution, say the what-me-worry position of some Democrats in Congress could prove self-defeating. If Democrats stand resolutely by programs for the aged, education and anti-poverty programs will end up being squeezed.

Richard Kogan, a budget analyst at the liberal Center on Budget and Policy Priorities, agreed: "This is big enough that you can't wish it away."

The Congressional Budget Office estimated five years ago that federal spending on the elderly would grow to more than $1 trillion -- 43 percent of the budget -- by 2010 from $615 billion -- or 35 percent of the federal budget -- in 2000. By 2015, spending on the elderly will consume nearly half the federal budget, through Medicare and Medicaid, pensions for federal workers and military retirees, veterans' health care and pensions, coal miners' benefits, Supplemental Security Income, food stamps, heating and housing assistance, and other programs for the elderly, according to the Brookings Institution.

At that point, Medicare spending will be growing at more than 8 percent a year and Medicaid at nearly 9 percent -- rates that dwarf the problems of Social Security, said Douglas Holtz-Eakin, the CBO’s director.

"Medicare and Medicaid spending triples, maybe quintuples by 2050, while Social Security goes up by 50 percent," said Holtz-Eakin, a former White House economist.

In contrast, federal spending on children will only inch up between 2000 and 2010, to $229 billion -- or 9.4 percent of the budget -- from $148 billion, or 8.4 percent of the budget. As a percentage of the gross domestic product, federal spending on children will have stagnated, while spending on the elderly will climb steeply.

"The issue has to be seen in the context of what are the needs of the larger society," the Brookings Institution's Sawhill said. "Where do we want to put our resources? The elderly versus the young is the question to be debated."

All of that spending on the elderly has had an effect. The income of households age 65 and older has risen by more than a third since 1975, while incomes of households under 45 have stagnated, according to the
Concord Coalition, a nonpartisan budget watchdog. The elderly, once mired in poverty, now have incomes nearly on par with the national average.

"Should age itself entail an entitlement to public subsidies?" asked CSIS's Jackson. "That may have made sense in 1935 or 1965, when age was a decent proxy for poverty and class, but it doesn't anymore."

As it begins to confront the costs of an aging population, the United States is in far better shape than most of the developed world. By 2040, 26 percent of the U.S. population will be at least 60 years old, up from 16.3 percent in 2000, according to CSIS. But that will make the population relatively spry. At least 45 percent of the populations of Japan, Spain and Italy will be 60 or older by then. In each of those countries, there will be one retiree for every worker.

China, seen by some as the rising economic power on which other countries will be leaning by mid-century, will be grappling with a demographic problem of its own. By 2040, 28 percent of China's population will be at least 60, a higher percentage than in the United States, and because China has a thin social safety net, the burden of an impoverished elderly class could be especially acute, according to a CSIS study on China's aging problem.

Those countries' misfortunes will be shared by the United States, according to the McKinsey Global Institute, the think-tank arm of consulting firm McKinsey & Co. Since the 1980s, spendthrift Americans have forced U.S. companies to turn to the savings of other countries, especially Japan, for the capital needed to expand and improve productivity. But as people in those lender countries age, they will be spending their savings and making claims on the debts the United States owes.

"We've had this global dynamic with Japan providing a lot of its excess saving to make up for our significant dis-savings," said Diana Farrell, the McKinsey Global Institute's director. "That cannot continue. This is a short-lived party we're in."

Within 20 years, Japan's household financial wealth will stop growing and begin to decline. By 2025, financial wealth in that country alone will be $8 trillion, or 47 percent, less than it would be if wealth growth followed recent trends, McKinsey estimated.

In the United States, McKinsey estimates that growth in household financial wealth -- including 401(k) retirement savings and other assets -- will slow to a crawl, from the 3.8 percent increases enjoyed since the 1970s to a paltry 1.6 percent by 2025.

Such global economic dynamics will only make it more difficult for future U.S. policymakers to confront America's problems, said CSIS's Jackson. Poorer U.S. households will be less able to handle a higher tax burden, and government borrowing could become untenable.

"Do we have a problem?" Jackson concluded. "Yeah, I think we do."

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A Graying Population

As the U.S. population grows considerably older in the coming years, programs for the elderly are projected to consume an ever larger share of federal tax dollars. Indeed, the problems that President Bush has highlighted for Social Security will be dwarfed by the costs of health care, veterans’ benefits and myriad other programs that may squeeze out other spending.

Elderly Spending in the Federal Budget

All numbers in 2004 dollars

1980 Federal spending on the elderly is nearly a third of the federal budget.

1980 $1.4 trillion
1990 $1.8 trillion
2003 $2.2 trillion
2015 $4 trillion

For comparison This line represents defense spending

O F F I C I A L B U D G E T S P E N D I N G O N T H E E L D E R L Y

Mandatory Federal Spending

The cost of Social Security, Medicare and Medicaid is rising.

In billions of dollars


Social Security $414 billion
Medicare $473 billion
Medicaid $49 billion
Medicare/ Medicaid $1.2 billion

Retirement Benefits

Retired couples are receiving more.

Typical couples retiring today will get a government-paid benefits package worth about $600,000.

Those now in their early 40s will retire with about $1 million in today’s dollars.

Federal Spending on Elderly vs. Children

In the coming years, growth in federal spending on the elderly is projected to well outpace the rise in federal spending on children.

A Global Issue

The U.S. population is relatively young compared with those in other industrialized nations.

Percentage of population age 60 and older, in selected countries

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<thead>
<tr>
<th>Country</th>
<th>2000</th>
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<tr>
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<td>26</td>
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<tr>
<td>Spain</td>
<td>22</td>
<td>28</td>
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