The EEAG Report on the European Economy

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Intergenerational Fairness

The intergenerational contract – the welfare state

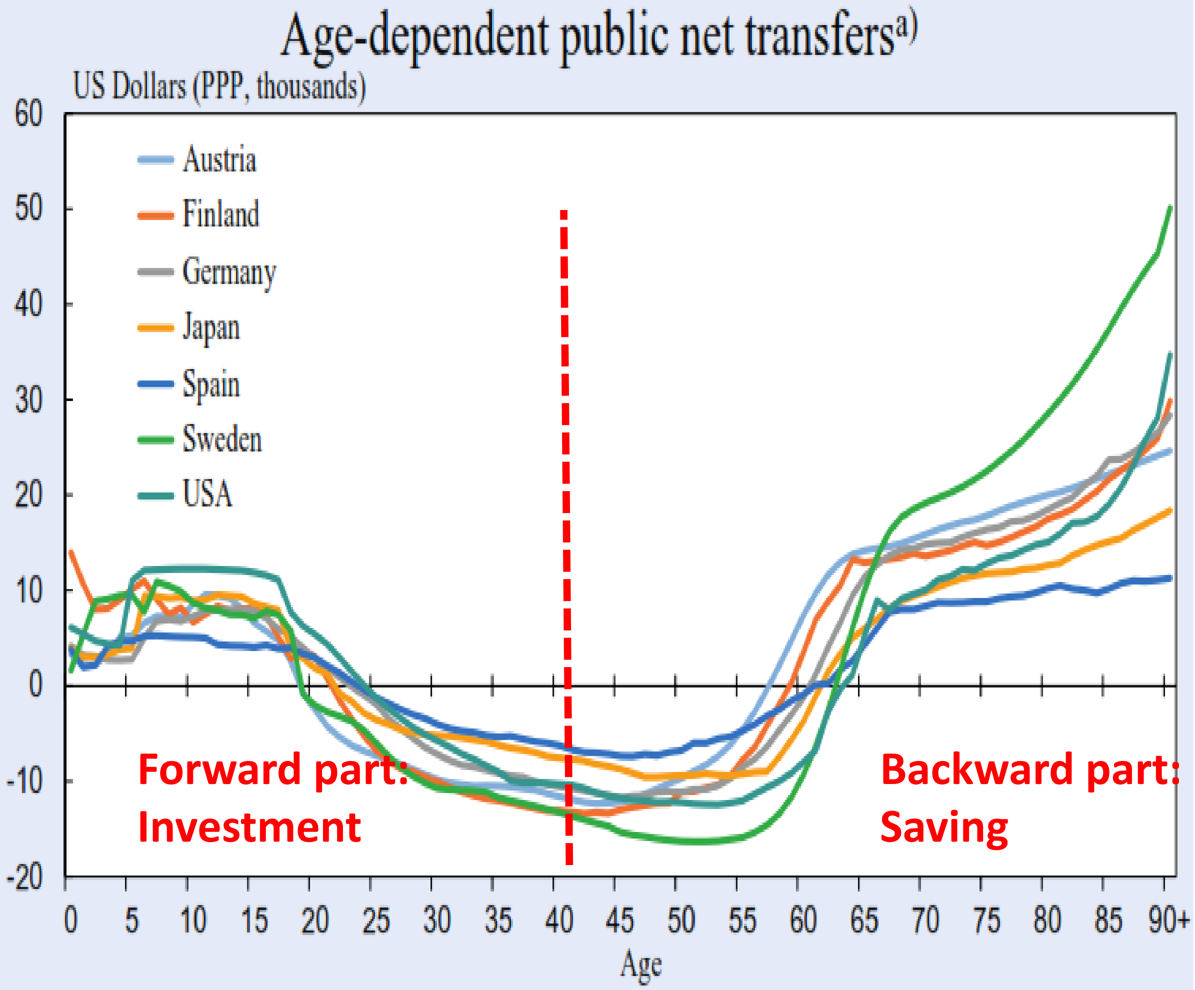
- Strong age dependencies- benefits and contributions

- Similar pattern across countries – amplitude depends on the extent of the welfare state

- Economic implications:

- Distribution and insurance

- Efficiency gains – front loaded – investing in the young



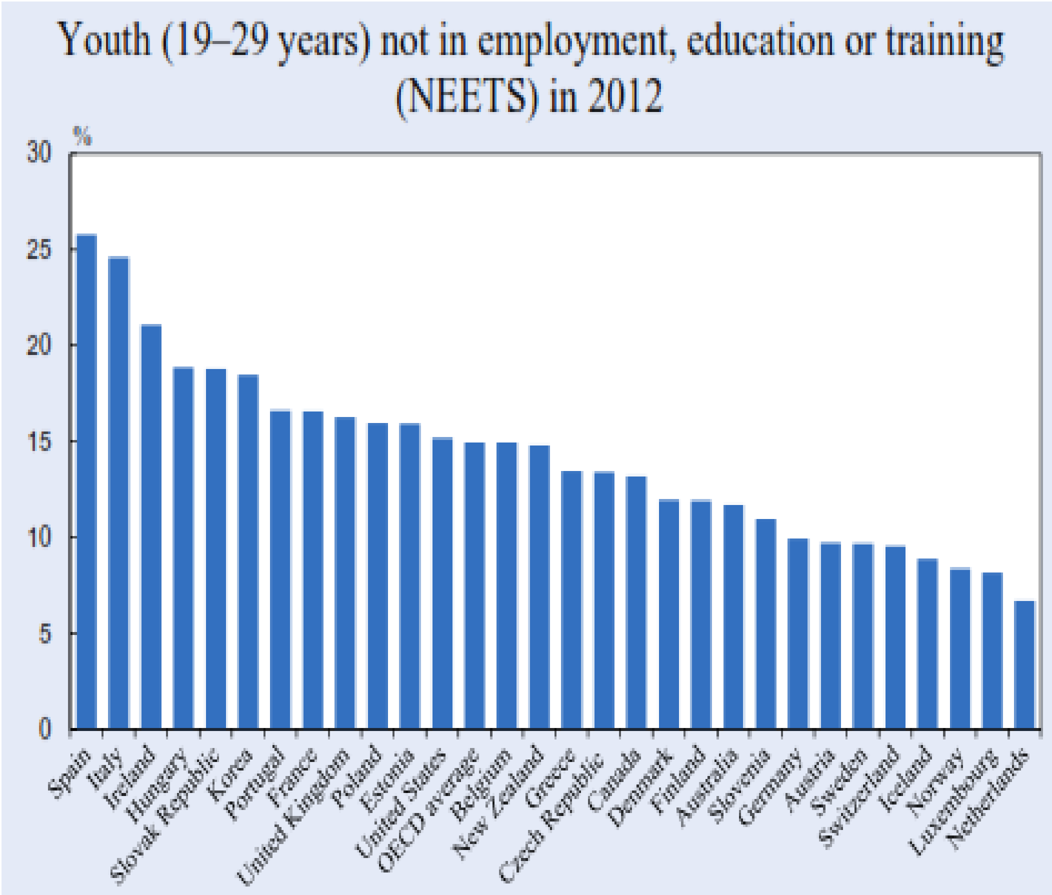
Intergenerational conflict

- Changing demographics
  - Fertility decline – implicit return falls
  - Mortality/Longevity – changing balance between contributions and benefits
  - Migration – adverse selection
- Transition
  - Delayed reform shifts adjustments burdens on future generations

- Who gains and who losses?
- Intergenerational
  - Current elderly: high return, increasing longevity, unchanged/falling retirement ages
  - The young: falling return; debt; reduced investment in the young
- Intragenerational
  - Social gradient in education, health, longevity – in a life-time perspective the model the model is less redstributive

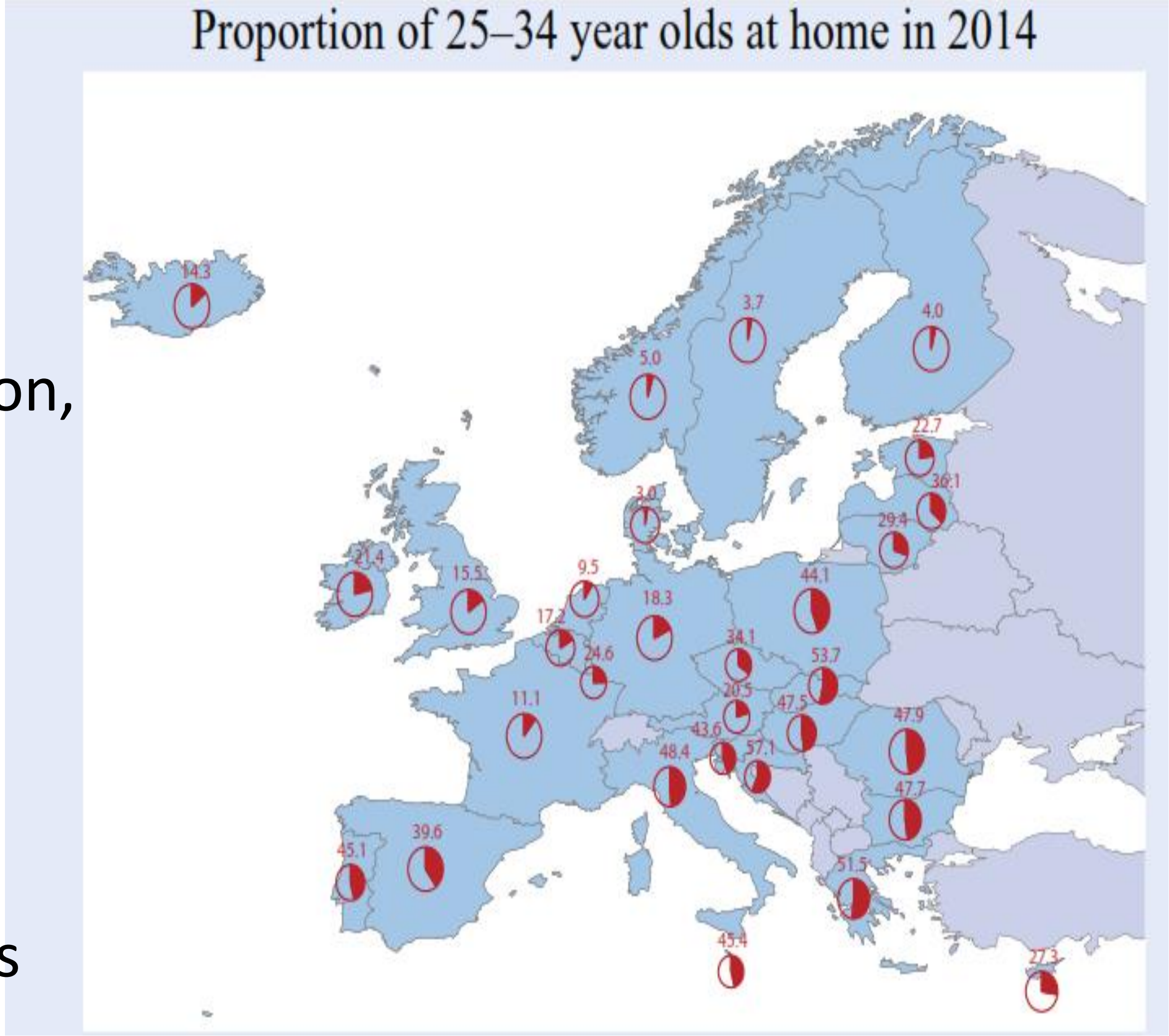
Entry – the young

- Increasing divide; insiders vs outsiders
- Marginalized youth – neither in job or education
- Job possibilities – short-term/temporary jobs (gigs)
- Risk of long-term unemployment and marginalization
- The financial viability of the social contract depends on a high employment rate



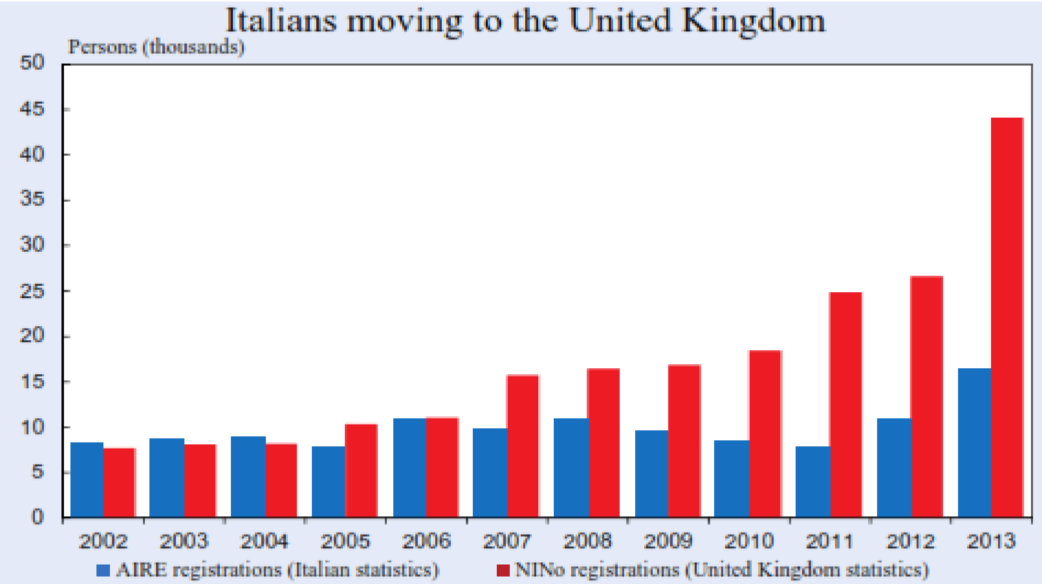
Housing and family formation

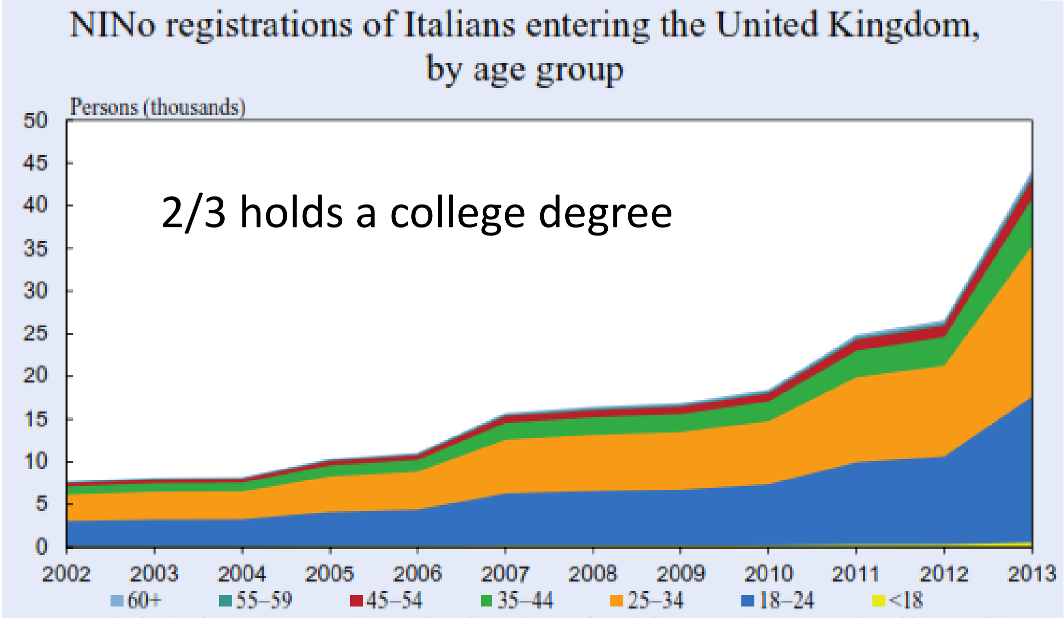
- Access to housing
  - short supply; expensive
- Involuntary "staying at home"
  - Implications for family formation, fertility
- Inefficient housing allocation
  - Locking-in (failure to adjust housing size to family size)
  - Lenient taxation (capitalized)
  - Bequests reinforce inequalities



Exit – the young and the educated

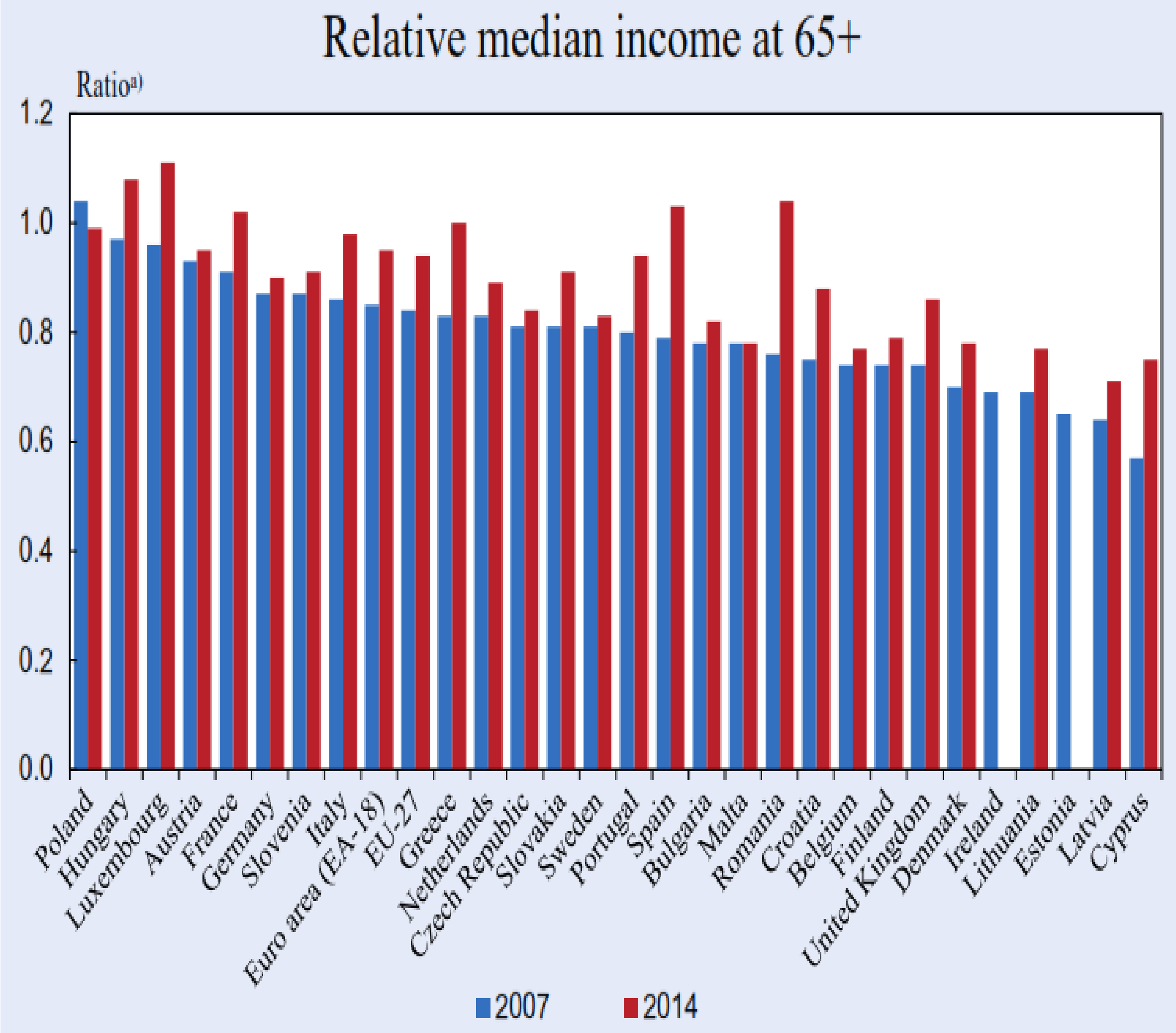
- Adverse selection in the social contract
- Exit: The young educated
- Human capital =Mobile capital
  – social return to education falls
- Vicious circle : “double” ageing effect: worsens the long-run sustainability of the contract





Pensions and medical care

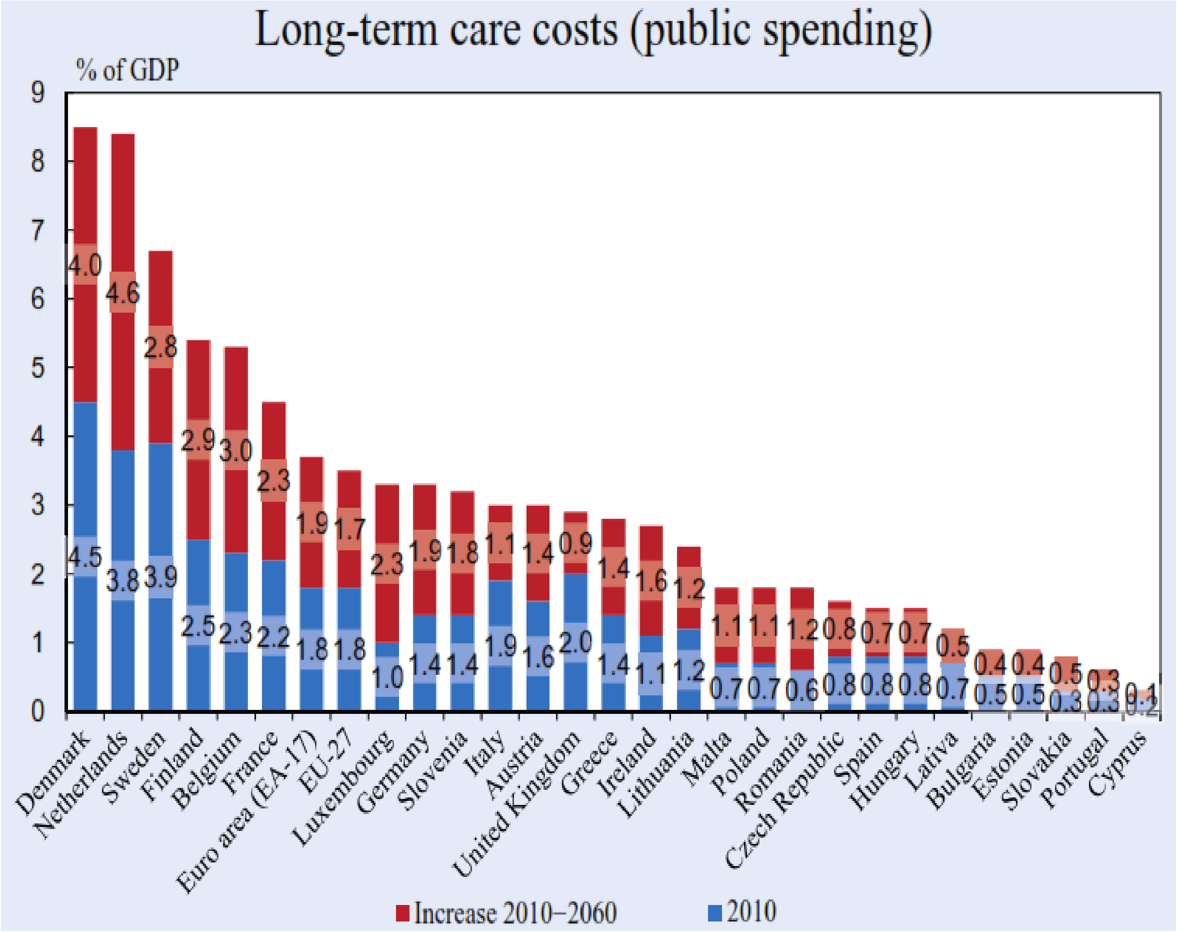
- Demographic burden on public budgets – for unchanged welfare arrangements!
- Longevity (healthy ageing) – individual gain; adjusting retirement age to keep share of life on work unchanged
- Pension reforms: Defined contribution schemes (double-burden)
- Delayed reforms have increased the burden and shifted costs to future generations



Health care

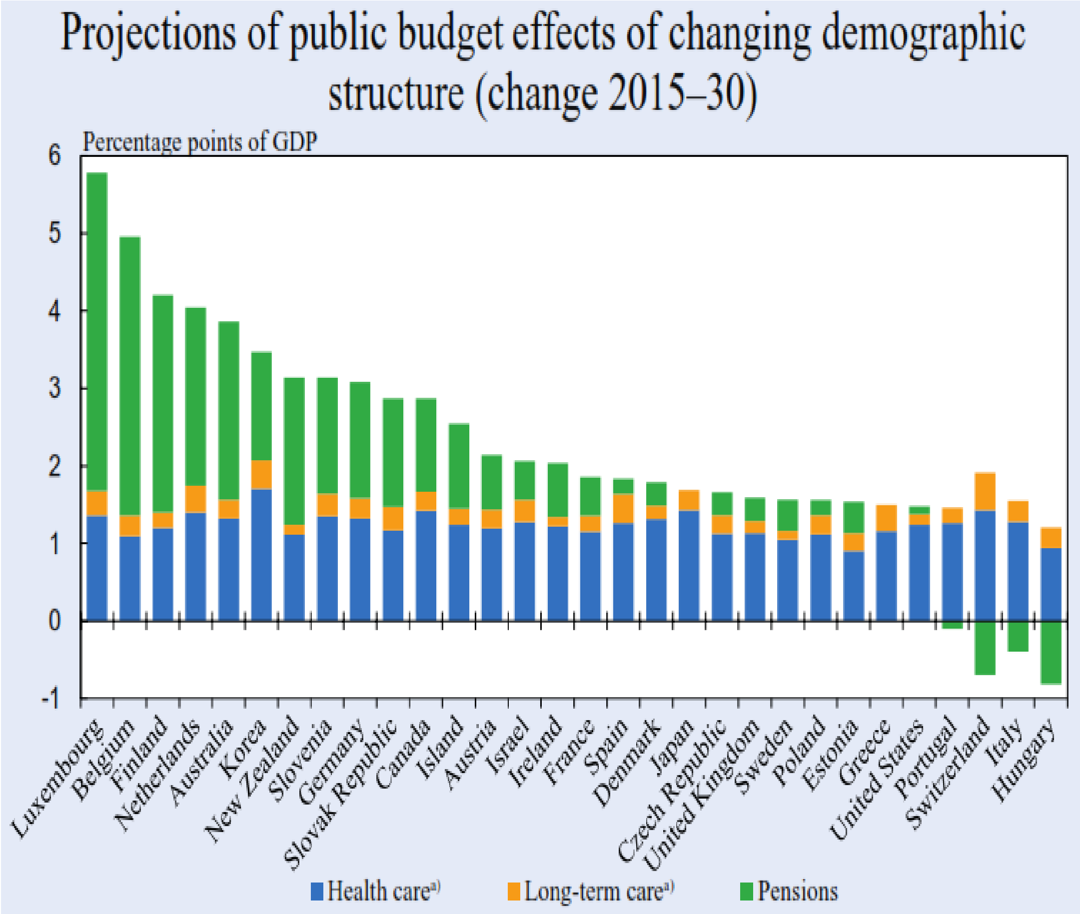
Expenditure drivers:

- Demographics (even allowing for healthy ageing)
- Demand: high income elasticity
- Opportunities: New and better treatments
- Cost: Care is intensive in human input (Baumol's costs disease)



Financial sustainability of the intergenerational contract

- Large pressure – even with pension reforms
- In some countries – also high debt levels
- Environmental ”debt” left to future generations



Conclusions

- Youth at a disadvantage
- The social contract not as favourable as to previous generations
- Failure to adjust have significant effect on intergenerational distribution
- Intergenerational distributional conflict - social cohesion
- Political balance is shifting in favour of older voters (gerontocracy)