Labor Force Participation, Aging, Social Security and the Budget

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Why Retirement Age & Labor Force Participation Are So Important

Tend to be associated mainly with Social Security

Much bigger issue: how society should adjust to demographic changes affecting

- GDP
- Personal Income
- Revenues (mainly income tax)
- Spending in the budget
  - CBO chart on spending (next slide) leaves out the first effects
  - A later study brings them back in
Factors Explaining Future Federal Spending on Medicare, Medicaid, and Social Security

Percentage of GDP

Effect of Excess Cost Growth in Health Care Spending

Effect of Aging

In the Absence of Aging and Excess Cost Growth

Social Security Cost and Income, Excluding Interest

A Digression on “Aging”

Living longer vs. lower birth rates
Both unfortunately defined as “aging”

Policy Problem:
• Past and scheduled increase in retirement years over the decades involves very
  large per person benefit expansion
• Baby boom hump does mean a larger portion of population in last years of life and
  a smaller portion in more healthy years

Research Problem:
• Estimates over time should often classify those with equivalent need by remaining
  (or relative remaining) life expectancy
  – Else not “sampling from same set”
• By life expectancy, a 68-year in 1940 is similar to a 75 year old today
Program Retirement Age, Indexed for Life Expectancy

Based on data from the Social Security Administration, Birth Cohort Tables.
We’ve been underestimating LFPR of older individuals for some time

**WHY?**

- Theory naively conflated full retirement with leisure
- Models left out some inelasticity of labor demand
  - Thus, earlier retirement largely supported by women and baby boomers in last half of 20\textsuperscript{th} century
  - Consider if fertility rate falls
    - From 3.0 to 0.0
    - From 3.0 to 2.0
      Wouldn’t you expect LFPR of older individuals to rise?
Burtless: Past Trends and Further Implications from Persistence

- Higher LFPR and earnings of older workers
  - At all educational levels
  - Not just part-time work
  - Often through continuous employment
- Based on already observed increases in “persistence,” SSA projections too low
Employment Rate Among Adults Age 16+ by Year and Simulation

- Alt 1
- Baseline

Year: 2010 to 2040

Employment Rate:
- Baseline: 60% in 2010, decreasing steadily.
- Alt 1: Starting at around 69%, peaks around 2020, then declines.

Comparison:
- The baseline scenario shows a steady decrease in employment rate from 2010 to 2040.
- Alt 1 has a higher starting rate compared to the baseline, with a peak around 2020 before declining.

Note: The graph illustrates the projected employment rates for different simulations over a span of years.
My Conclusions on LFPR

• Yes, SSA Projections definitely too low
• “A Prediction: Older Individuals Will Work More (2001)”
  – SSA’s own type of “persistence” bias:
    • Today = tomorrow
    • For each age group
  – As if size of each age group (weights) don’t matter
• Burtless projections very helpful
  – But may still underestimate future LFPR
    • Because of labor force demand
Participation Rates: Trustees' Assumptions versus Actual
(Men, Ages 65-69)

SSA Projections

Source: Bureau of Labor Statistics and authors' compilations of data from Social Security Actuary.
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Policy & Policy Process Implications

• LFPR effects extend well beyond Social Security
  – GDP, personal income, and income tax revenues
    • Johnson, Smith, and Steuerle;
    • Johnson & Smith (this study)
    • CBO recent study
  – Largest gains for those with lowest earnings

• A huge policy process problem
  – SSA doesn’t show most of these effects in reform efforts
  – CBO so far hasn’t either
Main Influences on Early Retirement

Health? No
• Most report good or excellent health

Physical demands? No
• Declining over time

Benefit ages & announcement effects? Yes
• Cushing-Daniels and Steuerle—initial age
• Joyce Manchester & others—changes in normal retirement age
Percent of Population Reporting Fair or Poor Health by Year and Age

U.S. Department of Health and Human Services, Center for Disease Control, "Health, United States, 2011 with Special Feature on Socioeconomic Status and Health."
U.S. Workers in Physically Demanding Jobs

Consequences of Middle Age, Old Age, and Survivors Insurance

• Expected years of benefits (couple) approach 30
• Benefits less & less concentrated among old
• Large consequences for revenues & income
• “Replacement rates” fall significantly in retirement (e.g., age 62 versus age 90)
• Distribution of income among old becomes more unequal?
Expected Years of Retirement Benefits, Earliest Retirement Age

Percentage of Men's Social Security Benefits Going to Men With Less Than 10 Years Remaining Life Expectancy

Summary

• Demand for older workers likely to continue rising
  – These papers one more piece of evidence
  – Most models fail to account for labor force demand
  – Older workers to the first half of the 21st century like women in last half of 20th:
    • The largest pool of underutilized talent in the country

• Defining longer lives as “aging” misleading
  – For policy & research

• Social Security reform not just about Social Security
  – Estimators need to show effects on GDP, income & revenues

• Many reasons to restore retirement systems to old age, not middle age, support
  – LFPR adds to them
  – Regardless of Social Security’s long-term balances