# Paying for Investments in Children

by Isabel V. Sawhill, Ph.D.

Advocates for children are hoping that with a new administration and a new Congress in 2009, investments in children will get enhanced priority. Although not as high on the agenda as the economy or the war in Iraq, the need to invest more in the education and health of children and their families is supported by a large majority of the public.[1] Moreover, unlike the short-term benefits of winding down the war in Iraq or reviving the economy, these investments can improve the future productivity of the nation. They speak to the concern among many that the next generation will not be as well off as the current one, and that the nation may even be in decline.

These concerns are being expressed at the same time as rigorous research has identified many proven and promising interventions that could enhance the educational success and future productivity of the youngest generation.[2] Numerous studies have shown, for example, that greater investments in early childhood education bring society long-term benefits that greatly exceed their costs. All that seems to be lacking is the money to fund these promising initiatives and the leadership to make them a higher priority in the competition for funds.

In this essay, I argue that to address these challenges and opportunities, we first need to reframe the debate. Specifically, we need a new intergenerational contract that invests more in people when they are young, but then expects them to assume somewhat greater responsibility for their own support during their retirement years. If we make wise investments in the young, their ability to be more self-sufficient during their later years will be enhanced, as will their ability to finance the health care and retirement needs of those who have been less fortunate. But we need to start now. The longer we wait, the more likely it will be that today's children will be incapable of supporting either themselves or their parents during the latter's golden years.

The need to reframe the intergenerational contract is premised on a number of assumptions or principles.[3] First, although tax increases and savings from ending the war can finance in a fiscally responsible way some of the needed investment in the youngest generation, they will not be sufficient. Second, linking investments

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in the young to reform of entitlements has bipartisan appeal. Third, the current allocation of resources between the young and the old is premised on outmoded assumptions about the relative needs of each. Generational equity requires a recalibration of the needs of different age groups. Fourth, the miracle of compound interest means that well-chosen investments in the young can produce a growth dividend and new revenues that would make any venture capitalist drool and that can make the revision of the intergenerational contract a positive sum game. Fifth, by phasing in any changes to the intergenerational contract slowly and paying careful attention to the genuine needs of the older population, no one need be seriously hurt in the process. If we start now, we can maintain commitments to current beneficiaries and provide a robust safety net for vulnerable groups into the future, while also gradually reallocating more public resources to the young.

## Moving Beyond Wishful Thinking

Many people are now convinced that unless we make major investments in the health and education of the youngest generation, we will not be able to compete with other countries or assume that future generations will be better off than previous ones. Money alone will not solve all of the problems. However, whether it's addressing the fact that one third of young people don't graduate from high school or that the U.S. has one of the highest rates of infant mortality in the world, money is surely needed. So where is this money to come from? The federal government is already running deficits, and these deficits will balloon over the next decade, initially because of the depressed economy, but more importantly because of the retirement of the baby boom generation and the pressures that the growing costs of Social Security and Medicare will place on the federal budget. According to Eugene Steuerle, rising costs in these programs for the elderly will absorb most of currently projected revenue growth between now and the end of the next president's second term.[4] Not only will there be no new money for children, there will be a fiscal squeeze on existing programs for children.

Many progressives assume that the solution is simply to raise revenues enough to simultaneously keep deficits at a reasonable level and to pay for the most promising investments in children and their families. But this is wishful thinking. Let's assume that we need to keep the deficit below 2 percent of GDP. This is a much more modest goal than trying to balance the budget and will not satisfy the fiscal hawks of the world, but it's a level below which the burden of the national debt can at least be kept at a sustainable level.[5] Let's further assume that we want to invest an extra one-half to 1 percent of GDP in children or their families by the end of the new president's first term.[6] These two goals require freeing up 1.5 to 2 percent of GDP or roughly $300 billion per year between 2010 and 2013.[7] Some of the funds would be used to keep the deficit from wrecking the economy or undermining future standards of living, and some would be devoted to new investments in education, health care, and the like.

Why can't this be achieved simply by raising taxes? First of all, poll after poll shows that the public is not enamored of new taxes, with the result that both presidential candidates have pledged either to reduce taxes across the board (John McCain) or to reduce them for the middle class (Barack Obama). Although Senator Obama would raise taxes on people with incomes above $250,000 a year, and both candidates have talked about the need to close corporate loopholes, these increases would only partially pay for Obama's spending increases and tax cuts, including those that would target the elderly making less than $50,000 a year.[8]

Even if the higher taxes that our 2 percent scenario requires were politically feasible, they would impose burdens on typical working-age Americans that many would find untenable. Their incomes have been stagnant, and their jobs and incomes are increasingly insecure. Further reducing their take-home pay to fund these investments is not a happy prospect.

Another hope among progressives is that a major overhaul of America's broken health care system will free up resources that can then be devoted to other national priorities. This, too, is wishful thinking. Most improvements in the health care system – from the adoption of electronic medical records to covering the currently uninsured – will actually cost more than the current system.[9] Over the long-haul, learning what works to improve health, and linking reimbursement of providers to evidence that treatments are effective, could indeed bring down costs, but not any time soon.[10] In the meantime, one of the most effective ways of getting more value for each health dollar spent is to put more emphasis on education rather than on health care per se. Education is associated with major improvements in people's health, independent of their income, their age, or the amount of health care they receive – probably because the more educated are more likely to adopt healthy life styles and to be intelligent users of whatever health care they consume.

Still a third contention is that an end to the war in Iraq will free up resources that can be used for other purposes. The problem with this argument is two-fold. First, the savings are not likely to be as large as many people think. We would be fortunate to recapture $100 billion from this source – about one third of the amount needed.[11] Second, and more importantly, any savings will be smaller than expected because only a portion of the expenditures for the war are included in the long-term budget baseline.

A final possibility is that our elected officials, faced with such daunting numbers, will simply say, in effect, "deficits be damned." What harm do they do anyway? In this case, advocates for children would do well to remember that it is the young who will suffer the consequences. By increasing the national debt, and the amount we owe to foreigners, deficits act like a stealth tax on the next generation. Already interest payments are the fastest growing item in the federal budget,[12] and we are financing most of each year's deficit by borrowing from countries such as China and Saudi Arabia. Eventually we will have to pay them back, with interest.

The preceding statements should not be misinterpreted. In my view, we can and should raise more revenues both to move the budget toward balance and to fund some new investments. We can and should reform the health care system to cover the uninsured, improve quality, and contain health care costs. And we can and should wind down the war in Iraq. But these steps will not be sufficient if we want to fund a robust agenda of investments in children. For this reason, advocates for the younger generation need, in addition, to consider ways in which we can rein in future commitments to the elderly while simultaneously protecting lower-income seniors, the disabled, those in poor health, and the truly aged.

## Dealing with Political Hot Potatoes and Forging a Bipartisan Compromise

A good negotiator doesn't reveal in advance what he's willing to give up to get what he wants in return. Democrats in Congress are not going to preside over any dismantling of the New Deal or the Great Society that put in place today's Social Security and Medicare programs. Not only are these extremely popular with the public, but the fear exists that any savings produced by even modest changes in these programs will be devoted to providing tax cuts to those who need them least. This fear is understandable in the context of recent history. However, such political concerns should not stand in the way of a robust, substantive discussion of the relative needs and responsibilities of people when they are young and when they are old.

Still, from a Democratic perspective, any proposal to reform entitlements will need to be combined with assurances that the money can be reinvested in other areas. Similarly, Republicans are not going to support more investments in the young if they believe they will require a much bigger government and a substantially higher burden of taxation. From their perspective, any set of proposals to invest more in children needs to be accompanied by a commitment to reform entitlements. While hardly ideal from either party's perspective, this linking of entitlement reform with greater investments in the younger generation, including lower-income families in particular, has the makings of a political compromise with long-term benefits for the nation. With strong leadership from the White House, it has a good chance of success.

Still another oft-cited concern is that talking about reallocating resources between the young and the old entails pitting one group against another. However, this concern rests on a basic misunderstanding of the life cycle process. Almost everyone who is young will eventually become old. So, putting some transition issues aside for the moment, this is not about a competition between the young and the old, but rather about making more investments in people when they are young so that they will be in a better position to support themselves or others when they are older. Individuals have the capacity – if not always the foresight – to smooth consumption over the life cycle. They do not have the capacity to

eliminate differences in ability, health, and productivity that are the products of their differing genetic and cultural endowments, and equally importantly, in the kinds of societal investments made earlier in their lives. By adopting a life cycle perspective, we can move beyond stale arguments about generational warfare.

## Generational Equity: Reassessing the Relative Well-being of the Young and the Old

The old intergenerational contract has been in force since Social Security was enacted in the 1930s. It was expanded in the 1960s with Medicare and Medicaid (which covers nursing home care), and yet again in this decade with the addition of prescription drugs to Medicare. It is built on a number of assumptions: that no one should be expected to work after the age of 65; that most seniors have insufficient resources to pay for their own retirement or health care; and that younger Americans are, on average, better off than older Americans. The system thus relies almost entirely on contributions from working-age Americans to finance these benefits along with supporting the other major dependent population, their children. And for the most part, the old contract has been a huge success, enabling people to retire at a reasonable age and reducing insecurity in old age.

**Table 1: Select Comparative Statistics for the Elderly and Non-Elderly**

| | Under 65 | 65 and Older |
|---|---|---|
| Poverty rate[1] | 12.7% | 9.4% |
| Average income per household member[2] | $26,350 | $24,095 |
| Mean income[2] | $72,906 | $41,928 |
| Median income[2] | $54,726 | $27,798 |
| Average annual change in real income (1994 – 2006)[3] | 0.74% | 1.11% |
| Average annual change in real income (2000 – 2006)[3] | -0.71% | 0.47% |
| Median net worth (in thousands)[4] | $69.40 | $190.10 |
| Homeownership[5] | 64.3% | 80.0% |
| Percentage of homeowners with no mortgage[5] | 24.0% | 75.0% |
| Percentage covered by health insurance[6] | 82.2% | 98.5% |

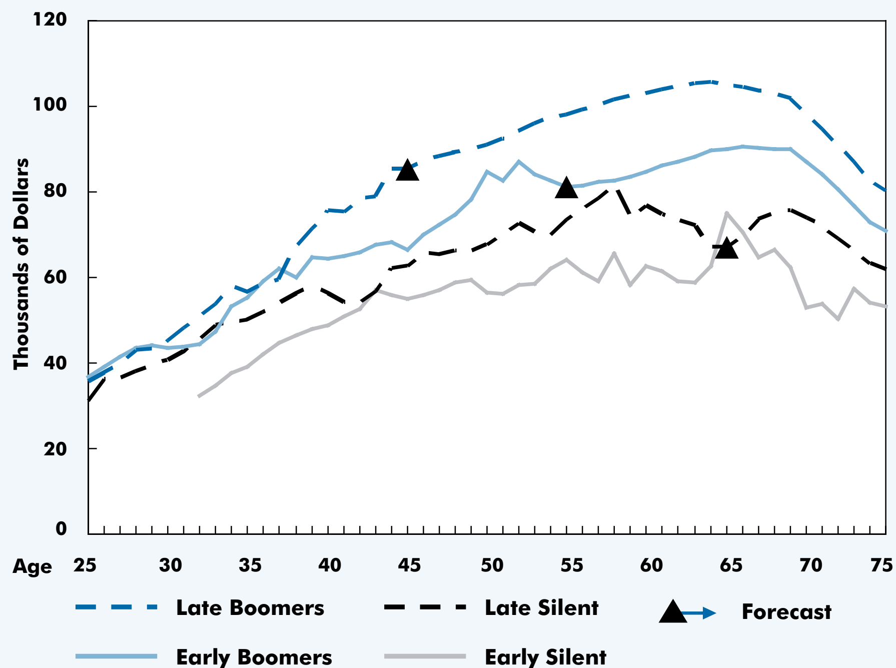
Note: Data is for year 2006 unless otherwise noted

Source(s):
[1] Author's calculations from U.S. Census Bureau, Table POV01
[2] U.S. Census Bureau, Table HINC-01
[3] Author's calculations from U.S. Census Bureau, Historical Income Table H-10 and Table HINC-01, 1995 - 2007.
[4] Data from 2004; data for those under 65 and 65 and older were not available for this statistic, so the age groups 35-44 and 65-74 were used. See Brian K. Bucks, Arthur B. Kennickell, and Kevin B. Moore, "Recent Changes in U.S. Family Finances: Evidence from the 2001 and 2004 Survey of Consumer Finances," Table 1, Federal Reserve Bulletin, vol. 92, February 2006.
[5] Author's calculations from the Consumer Expenditure Survey
[6] U.S. Census Bureau, Table HI05

Nevertheless, the contract hasn't kept up with the times. First, consider the facts about today's elderly. Like other age groups, they are a very diverse population. But whether we look at their income, their assets, their health, their longevity, or their own preferences to stay connected to work and community,[13] the elderly, as a group, have far more capacity to contribute to society than in the past. For example, the median household income of those 65 or over has increased 79 percent since 1967, while the median income of those in their prime earning years, aged 35 to 44, has increased by only 54 percent.[14] Even more striking is the decline in poverty among the elderly, from 35 percent in 1959 to 9 percent in 2006.[15] (Granted, if we excluded the Social Security benefits that the elderly receive, their poverty rate would be considerably higher.[16]) Compare this poverty rate of 9 percent to the much higher rate of 13 percent experienced by nonelderly households. Finally, 80 percent of people 65 and over own their own homes and three-quarters of these elderly homeowners own them free and clear of a mortgage.

Tomorrow's elderly – meaning today's baby boom generation – will be the wealthiest generation in history. Projections by the McKinsey Global Institute indicate that by age 65, average disposable income for late baby boomer households will be a little

**Chart 1**
**Real Disposable Annual Income Per Household by Cohort**



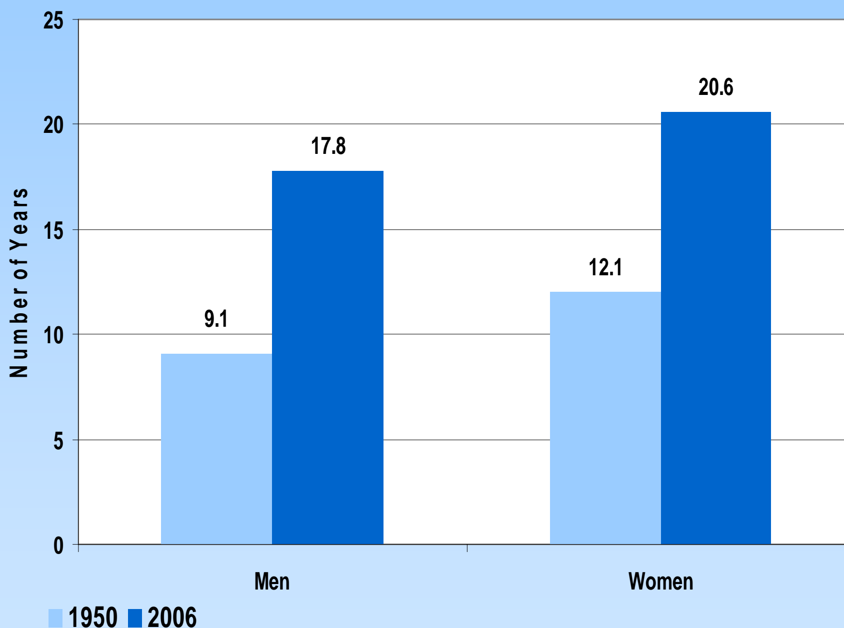

Note: Late Boomers born from 1955 through 1964; early boomers born from 1945 to 1954; late silent born from 1935 to 1944; early silent born from 1925 to 1934. See Appendix A, Chart 1.

Source: Diana Farrell et al, "Talkin' 'Bout My Generation: The Economic Impact of Aging US Baby Boomers," Exhibit 2, McKinsey Global Institute, June 2008.

over $100,000 a year or about 50 percent higher than the incomes of those currently that age. Although incomes fall as people retire, even those in their 70s, according to McKinsey, will have average incomes of about $80,000 a year. The problem, as the McKinsey report and others have noted, is that this generation is saving too little during their peak earning years with the result that there will likely be pressures not just to maintain but to increase the government benefits they receive. But the solution to inadequate saving is not additional government benefits. It is policies that encourage, or even mandate, greater savings when people are young. This must be part of the new intergenerational contract – the kind of personal responsibility that goes hand-in-hand with greater public investments in one's earning capacity at a young age.

We must absolutely maintain a robust safety net for the elderly. But all the evidence suggests there are many older Americans who, with or without government assistance, will be comfortably well off in the future, assuming they have access to good jobs and save enough during their working years. Even now, there are more than one million people over the age of 65 with incomes exceeding $100,000 a year.[17]

**Chart 2**
**Average Number of Years Spent in Retirement: 1950 and 2006**




See Appendix A, Chart 2.

Not only are the elderly economically better off than they used to be, they are living longer and healthier lives as well. In 1940, a 65-year-old could expect to live until age 78. Future retirees will live well into their 80s.[18]

Moreover, not only are today's elderly living longer, they are living better. Many of the elderly are experiencing what experts, such as Stanford researcher James Fries, call "compressed morbidity" – meaning that there has been a decline in disability rates among those over the age of 65.[19] Because this decline in disability has exceeded the decline in mortality, it has extended not just life, but healthy life and the ability to work. We should celebrate this progress, some of it made possible by the fact that the elderly – unlike the non-elderly – have universal access to health care through Medicare.

But while the elderly have improved their situation greatly since the intergenerational contract was first formed, working America has also gone through immense changes. In the economy of the 1950s or 1960s, the United States dominated world markets, jobs tended to last a lifetime, a high school education was sufficient for achieving a middle-class lifestyle, and firms could readily afford to provide generous benefits, in the form of health care and defined-benefit pension plans, to their employees. Similarly, schools worked better for a number of reasons, including the fact that there were fewer immigrants, and educated women had few professional job opportunities outside of teaching. Today, the United States has seen high school graduation rates decline over the last few decades, and it no longer leads the world in the proportion of high school graduates who go on to college.[20]

This is part of the reason why over the past three decades, young men have seen their wages stagnate. They are earning less, in inflation-adjusted terms, than their father's generation did at the same age.[21] Family incomes have crept up, but only because more women have gone to work. Poverty rates are now stuck at 1970s levels. Income inequality is as high as it was in the 1920s. And access to affordable health insurance has been sharply eroded. On a range of indicators from education to health care to rates of poverty, on average, children in the U.S. rank 18 when compared to children in 21 other advanced countries.[22] In addition, a college or other advanced degree has become the critical ticket to a good job and a middle-class life style, while the cost of higher education has escalated beyond the reach of many of today's families.

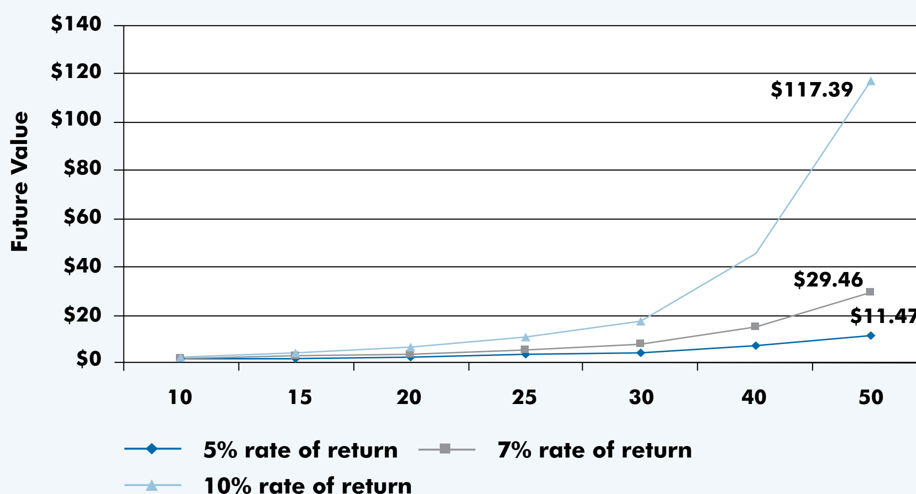
As a result of all these changes, the role of the government in providing economic mobility to workers or better education and job training for their children is more essential than ever. And yet, the historic commitment made to the elderly in the old intergenerational contract is placing a real burden on the working-age population. Although many people believe that Social Security and Medicare benefits are fully funded by the payroll taxes they have paid into the system, the reality is that these programs are not prefunded. Each dollar of benefits that goes to the elderly must come out of the income of younger, tax-paying Americans. So, the importance of balancing the needs of one group against the other must become part of our thinking. Those

progressives who argue that the way to handle the needs of both groups is to raise taxes to a much higher level seem to forget that the people who will pay those taxes are already struggling economically.

## The Miracle of Compound Interest

One of the strongest arguments in favor of gradually reallocating resources from the old to the young is the growth dividend that this can produce. In particular, eliminating the deficit any time soon is not a realistic proposition, but borrowing to make the young more productive is qualitatively different from borrowing to enable the old to consume. It is the reason that people take out loans to go to college but not (one hopes) to go on a cruise or buy a new set of golf clubs. When the nation invests in the young, assuming those investments are wisely chosen, the power of compound interest insures that future earnings and GDP will be greatly enhanced as a result. Most economists believe that the rate of return on investments in education, for example, is at least 10 percent. Moreover, the value of such investments can compound over time, since learning begets more learning, both in school and in the work force. Assume conservatively, and with some discounting of future benefits, that the nation could earn a rate of return of 5 percent on such investments. At the end of 20 years (when today's infants will be entering college and today's ten-year olds will be at the start of their careers), the value of $1 would be $2.65. At the end of 40 years, it would be $7. While I would not want to argue that all government programs targeted on children and younger families can achieve these kinds of returns, the point is that investing early should still pay big dividends.

### Chart 3
### Number of Years Investment is Allowed to Grow




Source: http://www.moneychimp.com/calculator/compound_interest_calculator.htm
See Appendix A, Chart 3.

## High Priority Investments and How to Pay for Them in a Fiscally Responsible Way

In an earlier publication, First Focus noted that the children's share of the federal budget has been declining for 45 years. In inflation-adjusted terms, spending on children increased by 1.4 percent from 2004 to 2008, while total spending increased by 12.2 percent. Moreover, the declining share of federal resources devoted to children shows no signs of abating any time soon.[23]

The good news about most programs for children is that they are relatively cheap. Total federal spending on children in fiscal year 2008 will total $233.2 billion.[24] Compare this to the $1,067 billion we will spend on Medicare and Social Security in the same year.[25] Just the increase in spending on these two programs over the next four years will exceed all spending on children.[26]

What this means is that one could fund major increases in spending on children with very modest changes in programs for the elderly. In an earlier paper on cost-effective investments in children my colleague, Julia Isaacs, suggested spending an additional $29 billion a year by 2012 in programs for children as shown in Table 2.[27]

| Table 2: High Priority Investments and How to Pay for Them | |
|---|---|
| **Cost-Effective Investments:[1]** | |
| Early Childhood Education | 20 |
| Infant and Toddler Programs | 4 |
| K-12 School Reform | 4 |
| Teen Pregnancy Prevention | 2 |
| **Total** | **29** |
| **Possible Ways to Pay for Them:[2]** | |
| Tax Social Security and Railroad Retirement Benefits Like Defined-Benefit Pensions | 36.6 |
| Base Social Security COLAs on an Alternative Measure of Inflation | 9.3 |
| **Total** | **45.9** |
| Note: All figures in billions and for year 2012. | |

Source:
[1] Julia Isaacs, "Cost-Effective Investments in Children," Table 1, Budgeting for National Priorities, January 2007.
[2] CBO, "Budget Options," Option 18 and 650-4, February 2007.

The majority of these funds ($20 billion) would be spent on early childhood education for which strong evidence exists that the benefits greatly exceed the costs. Indeed, this is a case where the miracle of compound interest is almost guaranteed to work. Not only are the benefit-cost ratios associated with such investments high, but additional work at Brookings on the likely effects of such investments on future educational attainment and economic growth suggest that they would have dramatic and positive long-term effects on GDP and on revenues.[28] The remainder of the $28 billion would be spent on nurse home visiting programs for those 0 to 2; on effective school reforms, such as Success for

All; on teacher quality initiatives; and on youth development programs that would have a variety of benefits, including reducing teenage pregnancy. Where there is insufficient evidence about the likely effects of different approaches, Isaacs proposes a serious federal investment in demonstration programs.

This investment, which would represent a 7 percent increase in funds devoted to children at the federal level, would require a 2 percent reduction in spending on today's elderly – hardly a big sacrifice among those who are, for the most part, are already concerned about the future of the country and the prospects for their grandchildren.[29] Indeed, one way to structure the financing would be to make some portion of it voluntary. That is, retirees who are currently receiving Social Security could be given the option of devoting some or all of their checks to a special fund dedicated to programs for children. Needless to say, no one knows how many people would contribute and in what amounts.

Two other options would impose minimal sacrifices on the elderly, while providing more than sufficient funds to pay for an agenda of enhanced investments in children. One would entail leveling the playing field between elderly and nonelderly citizens with the same incomes by taxing Social Security benefits more fully. Currently, only half of these benefits are taxed for those with incomes above $25,000 ($32,000 for a couple), and 85 percent are taxed for those with incomes above $34,000 ($44,000 for a couple). Fully taxing these benefits, after an exemption for the individual contributions made into the system, would raise $36.6 billion in 2012. (See Table 2)

A second option would be to change the way Social Security benefits are indexed for inflation. Many experts believe that the current consumer price index for urban wage earners and clerical workers (CPI-W), which is used to adjust benefits, now overstates the rate of inflation because it fails to account for the fact that people's spending patterns shift in response to a change in prices. For example, when gas prices increase, they drive less or purchase more fuel-efficient cars. An index that more accurately accounts for these changes in purchasing patterns would, if introduced now, save $9.3 billion by 2012 (and somewhat less if introduced at a later date). If this COLA reform were introduced for Social Security, it should also be introduced as a better way to index all benefit and tax changes. The extra resources that this would provide could be used to protect low-income beneficiaries.

These short-term steps need to be combined with longer-term efforts to slow the growth of entitlement spending in a way that will bring projected deficits under control, reassure financial markets, and restore confidence in government. Policy changes to accomplish these objectives need to be enacted now and phased in very gradually so that they enable people to plan for the future. This will also permit short-term investments in the younger generation to begin to affect their productivity and thus their ability to afford their own and their parents' retirements. In other words, the gradual phase in of these reforms, combined with

upfront investments in children, is exactly what is needed to ensure that those receiving the extra help when they are young are the same people who are asked to contribute more as they age. To jump start the process, it may be necessary to ask for some new taxes, some belt-tightening among the currently retired population, and some forbearance of continuing deficits in the short-run. But over time, each generation would be expected to invest in the next while in their prime earning years, in return for which the younger generation would be expected to take more responsibility for themselves as they aged.

The major Social Security options that should be debated include a gradual increase in the normal retirement age (now about 66) so that increased longevity does not lead to ever-higher lifetime benefits; progressive indexing of Social Security benefits that maintains future benefits for the less advantaged, but entails a slower rate of growth in benefits for the most affluent; and changes in a variety of policies that might encourage later retirement. Currently, most people retire at age 62 or 63. Some of this appears to be induced by the fact that the eligibility age for early retirement is 62. Even though people get actuarially reduced benefits as a result, the eligibility age sends a strong signal that may have led to a change in social norms about the appropriate time to retire. In the meantime, people are living longer and healthier lives, and far fewer jobs require the kind of physical strength or stamina that may have necessitated such early retirement in the past.[30]

The challenge of slowing the growth of Medicare will be much greater than the problem of restoring solvency to the Social Security system. Like Social Security, Medicare is affected by the aging of the population. However, in addition, its explosive growth is fueled by rapidly rising health care costs per person. Many experts now believe that the most promising long-term approach to this problem is to learn what works and to base reimbursement policies for providers on this knowledge. Because Medicare is the single largest payer in the system, it can lead the way in collecting this evidence and redesigning reimbursement policies accordingly.

## Conclusion

By revising the intergenerational contract, we can create a better future for all of our citizens. By investing wisely in children, we can enhance their productivity and enable them to contribute more to their own support and that of their parents in old age. The increase in GDP estimated to result from a high quality preschool experience to all three and four year olds is estimated to be more than $2 trillion by 2080.[31] This extra GDP will provide the higher incomes and increased revenues (a net fiscal dividend of $341 billion and much higher earnings) needed to pay for an aging population.[32] Current commitments to the elderly will need to be scaled back somewhat, but our best chance of making them affordable is to make the needed investments in the youngest generation now.

[1] See Celinda Lake polling data as reported to PAES, http://www.partnershipforsuccess.org/docs/ivk/iikmeeting_slides200801lake.pdf.

[2] The Committee for Economic Development has done much research on this subject; see http://www.ced.org/publications/subject.shtml#educ. Also see Julia Isaacs, "Cost-Effective Investments in Children," Budgeting for National Priorities, January 2007; James H. Heckman and Dimitriy V. Masterov, "The Productivity Argument for Investing in Young Children," Working Paper No. 5, Committee for Economic Development, Invest in Kids Working Group, 2007; Isabel Sawhill and Jens Ludwig, "Success by Ten: Intervening Early, Often, and Effectively in the Education of Young Children," Hamilton Project Discussion Paper, February 2007.

[3] Isabel Sawhill and Emily Monea, "Old News," *Democracy,* No. 9, Summer 2008.

[4] In Kids' Share 2007, the "squeeze" – in which spending on non-child Social Security, Medicare and Medicaid, defense, international, and interest on the debt will completely consume all revenue – was projected to occur in 2017; in the 2008 report, the squeeze is now projected to occur in 2021. See Adam Carasso, C. Eugene Steuerle, Gillian Reynolds, Tracy Vericker, and Jennifer Macomber, "Kids' Share 2008," Figure 19, June 2008.

[5] Max Sawicky states that the basic principle of deficit sustainability is that debt may increase at the same rate as GDP without creating a problem. Thus, if debt is approximately 40 percent of GDP and nominal GDP growth is 5 percent, on average, a sustainable deficit should be about 2 percent of GDP. See Max B. Sawicky, "Collision Course: The Bush Budget and Social Security," EPI Briefing Paper #156, March 16, 2005.

[6] In The United Kingdom in 1999, former Prime Minister Tony Blair initiated a campaign to end child poverty. The government has subsequently spent an extra 0.9 percent of GDP per year for low-income families with children. As a result, the poverty rate for U.K. children fell to 11 percent by 2004–2005, while the official U.S. child poverty rate was 18 percent in 2005. See John Hills, "The Blair Government and Child Poverty" in *One Percent for the Kids,* Isabel Sawhill, ed., The Brookings Institution, 2003; Timothy M. Smeeding, "Poorer by Comparison: Poverty, Work, and Public Policy in Comparative Perspective," Pathways, Winter 2008.

[7] Author's calculations from Brookings-Urban Tax Policy Center, Budget Outlook Tables, March 2008, Appendix 2.

[8] Isabel Sawhill, "Candidate Issue Index: Fiscal Responsibility," Opportunity 08 Candidate Views Index, July 2008.

[9] James J. Mongan, Timothy G. Ferris, and Thomas H. Lee, "Options for Slowing the Growth of Health Care Costs," *New England Journal of Medicine,* April 3, 2008 (1509 – 1514); Henry J. Aaron, "The Rising Cost of Health Care: Is it a Problem?" Remarks to the 2004 Annual Meeting, Institute of Medicine, October 2004; CBO, "Evidence on the Costs and Benefits of Health Information Technology," May 2008.

[10] CBO, "Research on the Comparative Effectiveness of Medical Treatments," December 2007.

[11] Even the Obama campaign estimates that ending the war in Iraq would free up only about $90 billion per year. See Peter Nicholas, "Adding Up the Cost of Obama's Agenda," *Los Angeles Times,* July 8, 2008.

[12] CBO, "The Budget and Economic Outlook: Fiscal Years 2008 to 2018," January 2008.

[13] For example, eight in ten boomers say their idea of retirement involves some kind of work, whether part-time or full-time. See Divided We Fail, "Savings, Pensions, and Work," http://www.aarp.org/issues/dividedwefail/about_issues/divided_we_fail_platform_savings_pensions_and_work.html.

[14] Author's calculations from U.S. Census Bureau, Historical Income Table H-10.

[15] U.S. Census Bureau, Table POV01 and Historical Poverty Table 3.

[16] A paper by Gary Engelhardt and Jonathan Gruber estimates that a $1,000 increase in Social Security benefits is associated with a 2 to 3 percentage point reduction in poverty rates for elderly households. Applying this estimate to the change in Social Security benefits between 1967 and 2000 suggests that the increase in benefits can explain all of the 17 percentage point decline in poverty that occurred during this period. Source: Gary V. Engelhardt and Jonathan Gruber, "Social Security and the Evolution of Elderly Poverty," NBER Working Paper No. 10466, May 2004. According to the CBPP, without Social Security, the elderly rate of the poverty would be much closer to 50 percent. Source: Arloc Sherman and Isaac Shapiro, "Social Security Lifts 13 Million Seniors Above the Poverty Line: A State-by-State Analysis," Center on Budget and Policy Priorities, February 24, 2005.

[17] U.S. Census Bureau, Current Population Survey, 2007 Annual Social and Economic Supplement, Table PINC-02.

[18] Felicitie C. Bell and Michael L. Miller, "Life Tables for the United States Social Security Area 1900–2100," Actuarial Study No. 120, Table 10, August 2005.

[19] See James F. Fries, "Measuring and Monitoring Success in Compressed Morbidity," Annals of Internal Medicine, 139(5), September 2, 2003, p. 455–459.

[20] Edward B. Fiske, "A Nation at a Loss," The New York Times, April 25, 2008.

[21] Julia Isaacs, "Economic Mobility of Men and Women," Getting Ahead or Losing Ground: Economic Mobility in America, February 2008.

[22] Child Well-Being in Rich Countries, UNICEF Report Card No. 7, 2007.

[23] First Focus, "Children's Budget 2008," April 2008.

[24] Ibid.

[25] Author's calculations from CBO, "An Analysis of the President's Budgetary Proposals for Fiscal year 2009," data from Baseline Projections of Mandatory Outlays, March 2008.

[26] Ibid.

[27] Note that the expenditure of a full extra 0.5 percent of GDP on children, would leave roughly $55 billion to allocate toward other programs or initiatives compared with what is detailed here.

[28] William T. Dickens, Isabel Sawhill, and Jeffrey Tebbs, "The Effects of Investing in Early Education on Economic Growth," The Brookings Institution, April 2006.

[29] Author's calculations from Adam Carasso, C. Eugene Steuerle, Gillian Reynolds, Tracy Vericker, and Jennifer Macomber, "Kids' Share 2008," data from Figure 14, June 2008 and Julia Isaacs, "Cost-Effective Investments in Children," Budgeting for National Priorities, January 2007.

[30] After a detailed study of this issue for the Center for Retirement Research at Boston College, John Turner concludes: "The question of whether more workers could work past age 62 has two parts. First, how have older workers' capabilities changed? Second, how have job requirements changed? Overall, individuals in their fifties and sixties are effectively younger than people the same age 25 years ago in terms of life expectancy, disability rates, and self-reported health. These findings are consistent across gender and racial/ethnic groups. Along with health, employment has become less physically-demanding, except for those with relatively little education." John A. Turner,

"Promoting Work: Implications of Raising Social Security's Early Retirement Age," August 2007. Also, see Gary Burtless and Joseph P. Quinn, "Is Working Longer the Answer for an Aging Workforce?" Center for Retirement Research at Boston College, December 2002.

[31] This increase in GDP is the authors' "preferred estimate." See Isabel V. Sawhill, Jeffrey Tebbs, and William T. Dickens, "The Effects of Investing in Early Education on Economic Growth," Brookings Policy Brief #153, April 2006.

[32] The authors calculate that the extra GDP will produce approximately $400 billion extra in revenue in 2080. The net cost of the program is estimated to be $59 billion in 2080, producing a fiscal surplus of $341 billion in that year. See Sawhill, Tebbs, and Dickens (2006).

## Appendix A

**Chart 1: Today's Baby Boom Generation Will Be the Wealthiest Generation in History**

| Age | Early Silent (Born 1925 - 1934) | Late Silent (Born 1935 - 1944) | Early Boomers (Born 1945 - 1954) | Late Boomers (Born 1955 - 1964) |
|---|---|---|---|---|
| 25 | | 31.1 | 36.7 | 35.6 |
| 26 | | 36.0 | 39.2 | 37.7 |
| 27 | | 36.4 | 41.5 | 39.7 |
| 28 | | 38.0 | 43.5 | 42.9 |
| 29 | | 39.3 | 44.2 | 43.3 |
| 30 | | 40.7 | 43.5 | 45.4 |
| 31 | | 42.6 | 43.9 | 48.1 |
| 32 | 32.3 | 45.6 | 44.5 | 51.3 |
| 33 | 34.7 | 48.8 | 47.3 | 53.8 |
| 34 | 37.7 | 49.0 | 53.2 | 57.9 |
| 35 | 39.1 | 50.1 | 55.2 | 56.5 |
| 36 | 42.1 | 51.7 | 59.2 | 58.3 |
| 37 | 44.7 | 53.7 | 62.2 | 59.5 |
| 38 | 46.5 | 56.3 | 60.1 | 67.5 |
| 39 | 47.9 | 57.9 | 64.8 | 71.5 |
| 40 | 48.9 | 56.0 | 64.5 | 75.7 |
| 41 | 51.0 | 54.1 | 65.0 | 75.2 |
| 42 | 52.7 | 54.1 | 65.8 | 78.1 |
| 43 | 57.2 | 56.8 | 67.8 | 78.9 |
| 44 | 55.9 | 62.0 | 68.4 | 85.4 |
| 45 | 54.9 | 62.5 | 66.4 | 85.4 |
| 46 | 55.8 | 65.6 | 69.9 | 87.0 |
| 47 | 57.1 | 65.3 | 72.3 | 88.3 |
| 48 | 58.9 | 66.3 | 74.8 | 89.2 |
| 49 | 59.4 | 66.2 | 78.3 | 89.8 |
| 50 | 56.5 | 67.6 | 84.7 | 90.9 |
| 51 | 56.1 | 70.2 | 82.8 | 92.4 |
| 52 | 58.1 | 72.7 | 87.1 | 94.1 |
| 53 | 58.7 | 70.7 | 84.1 | 95.9 |
| 54 | 62.0 | 69.9 | 82.5 | 97.2 |
| 55 | 64.1 | 73.6 | 81.2 | 98.0 |
| 56 | 61.1 | 76.0 | 81.6 | 99.0 |
| 57 | 59.1 | 78.5 | 82.3 | 100.1 |

| Chart 1 continued | | | | |
|---|---|---|---|---|
| 58 | 65.6 | 81.8 | 82.8 | 101.5 |
| 59 | 58.2 | 73.9 | 83.5 | 102.2 |
| 60 | 62.8 | 76.7 | 84.6 | 103.0 |
| 61 | 61.6 | 74.8 | 86.3 | 103.8 |
| 62 | 59.3 | 73.4 | 87.2 | 104.5 |
| 63 | 58.9 | 72.1 | 88.3 | 105.3 |
| 64 | 62.6 | 67.1 | 89.6 | 105.6 |
| 65 | 75.0 | 67.2 | 90.0 | 104.9 |
| 66 | 70.7 | 69.6 | 90.5 | 104.3 |
| 67 | 64.7 | 73.5 | 90.2 | 103.6 |
| 68 | 66.5 | 74.9 | 90.1 | 102.8 |
| 69 | 62.3 | 75.7 | 89.9 | 101.8 |
| 70 | 52.8 | 73.9 | 87.0 | 98.1 |
| 71 | 53.7 | 71.8 | 84.3 | 94.7 |
| 72 | 50.4 | 69.2 | 80.6 | 90.9 |
| 73 | 57.4 | 66.3 | 76.9 | 86.9 |
| 74 | 54.0 | 63.1 | 72.9 | 82.5 |
| 75 | 53.3 | 61.8 | 70.9 | 80.3 |

Note: Late Boomers born from 1955 through 1964; early boomers born from 1945 to 1954; late silent born from 1935 to 1944; early silent born from 1925 to 1934.

Source: Diana Farrell et al, "Talkin' 'Bout My Generation: The Economic Impact of Aging US Baby Boomers," Exhibit 2, McKinsey Global Institute, June 2008.

## Chart 2: The Average Number of Years Spent in Retirement Has Grown Dramatically

### Men

| | Average Age at Death[1] | Average Retirement Age[2] | Year Spent in Retirement |
|---|---|---|---|
| 1950 | 77.8 | 68.7 | 9.1 |
| 1960 | 77.9 | 66.8 | 11.1 |
| 1970 | 78.1 | 64.4 | 13.7 |
| 1980 | 79.0 | 63.9 | 15.1 |
| 1990 | 80.1 | 63.7 | 16.4 |
| 2000 | 80.9 | 64.1 | 16.8 |
| 2006 | 81.3 | 63.5 | 17.8 |
| 2020 | 82.2 | 63.5 | 18.7 |

### Women

| | Average Age at Death[1] | Average Retirement Age[2] | Year Spent in Retirement |
|---|---|---|---|
| 1950 | 80.1 | 68.0 | 12.1 |
| 1960 | 80.9 | 65.2 | 15.7 |
| 1970 | 82.1 | 63.9 | 18.2 |
| 1980 | 83.4 | 63.5 | 19.9 |
| 1990 | 84.1 | 63.5 | 20.6 |
| 2000 | 84.0 | 63.8 | 20.2 |
| 2006 | 84.0 | 63.4 | 20.6 |
| 2020 | 84.7 | 63.4 | 21.3 |

Note: Average age at death is equal to life expectancy at age 65 plus 65 years.

Note: Average age for benefits rewarded used for average retirement age.
See here for more: <http://www.ssa.gov/OACT/ProgData/awardDef.html>.

[1] Felicitie C. Bell and Michael L. Miller, Life Tables for the United States Social Security Area 1990-2100, Actuarial Study No. 120, Table 10, SSA, August 2005.

[2] Social Security Administration, "Annual Statistical Supplement to the Social Security Bulletin, 2007," Table 6.B5, April 2008.

**Chart 3: The Miracle of Compound Interest: A $1 Initial Investment**

| Initial investment = $1 | | |
|---|---|---|
| **Rate of Return** | **Years** | **Final Amount** |
| 5% | 10 | $1.63 |
| | 15 | $2.08 |
| | 20 | $2.65 |
| | 25 | $3.39 |
| | 30 | $4.32 |
| | 40 | $7.04 |
| | 50 | $11.47 |
| 7% | 10 | $1.97 |
| | 15 | $2.76 |
| | 20 | $3.87 |
| | 25 | $5.43 |
| | 30 | $7.61 |
| | 40 | $14.97 |
| | 50 | $29.46 |
| 10% | 10 | $2.59 |
| | 15 | $4.18 |
| | 20 | $6.73 |
| | 25 | $10.83 |
| | 30 | $17.45 |
| | 40 | $45.26 |
| | 50 | $117.39 |

Source: http://www.moneychimp.com/calculator/compound_interest_calculator.htm