Will We Be Healthy Enough to Work Until We are 70?

Professor Laurie Brown
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Acknowledgements

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• Drs Riyana Miranti and Jinjing Li, IGPA
• David Cullen, Chief Economist, DoH & Adjunct Prof at IGPA
Outline

1. Policy Context
   - History of age pension in Australia
   - 2014 Budget Measure to increase the age pension eligibility age to 70 years

2. Why? Demographic and fiscal challenges

3. Labour economics 101 – who forgot about the demand for labour?

4. A health capital approach

5. Discussion & concluding remarks
History of Age Pension in Australia

- 1909 introduction of a Commonwealth Government means-tested flat-rate age pension
- available to men at 65 years of age and women at 60 years of age
- residence qualification of 20 years
- financed through general revenue
- no distinction between single or married persons
- early 1960s the residence requirement for the pension was reduced to 10 years and a new standard rate of pension was introduced to provide single pensioners a higher payment
Age Pension in Australia

- provides income support and access to a range of concessions for eligible older Australians
- a social safety net with the objective of providing security for older Australians who are unable to support themselves in their retirement. Older Australians with the resources to fund their own retirement should do so (NCoA)
- the three pillars of retirement income
  - age pension
  - compulsory superannuation funded from employer contributions
  - private savings
- access to the pension remains dependent on when a person was born, their income and assets (excluding the family home), and meeting residence requirements
- pension rates indexed twice a year using a wages benchmark (combined couple rate of pension at 41.76% of male total average weekly earnings)
# Increases in the Qualifying Age for the Age Pension

<table>
<thead>
<tr>
<th>Date of Birth</th>
<th>Qualifying Pension Age</th>
<th>Date Pension Age Changes</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 July 1952 to 31 December 1953</td>
<td>65 years and 6 months</td>
<td>1 July 2017</td>
</tr>
<tr>
<td>1 January 1954 to 30 June 1955</td>
<td>66 years</td>
<td>1 July 2019</td>
</tr>
<tr>
<td>1 July 1955 to 31 December 1956</td>
<td>66 years and 6 months</td>
<td>1 July 2021</td>
</tr>
<tr>
<td>1 January 1957 onwards</td>
<td>67 years</td>
<td>1 July 2023</td>
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<tr>
<td>1 July 1958 onwards</td>
<td>...</td>
<td>...</td>
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<tr>
<td></td>
<td>70 years</td>
<td>1 July 2035</td>
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</table>
Why Increase the Age Pension Age?

We should celebrate the fact that Australians are living longer but we must prepare for the adjustments in our society.

People should work as long as they can.

What we are going to do is to deliver a fairer system for the aged pension that is going to focus on the sustainability of the system with a reasonable quality of life.

The aged pension needs to be a safety net by 2035, not a cargo net.
Why Increase the Age Pension Age?

- Government’s largest single social security program
- 2.4 million Australians are recipients of the age pension
- about 70% of people of Age Pension age receive the Age Pension
- around 60% receive a full rate pension
- 2013-14 the Australian Government spent $39.4 billion on the age pension with a budgeted expenditure of $42 billion in 2014-15
- expenditure growing at ≈7% per year
- currently 2.9% of GDP rising to 3.6% of GDP ($165bn in today’s dollars) by 2054-55
Why Increase the Age Pension Age?

- Hadn’t increased for men since its inception
- Increases in life expectancy
- Other countries are doing it (Iceland & Norway at 67; US, Germany & Denmark moving to 67; UK increasing to 68)

Living much longer than when the Age Pension was devised and on current trajectories it isn’t financially unsustainable

So the cost of the Age Pension remains sustainable and affordable and well targeted to those in genuine need
Dep Ratio is the dependency ratio measured as the number of persons aged 15-64 years per 10 persons aged 65 years and over.
# Growth of Australia’s Older Population (aged 65 years and over)

<table>
<thead>
<tr>
<th>Year</th>
<th>Male (m)</th>
<th>Female (m)</th>
<th>Total (m)</th>
<th>Growth (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2015</td>
<td>1.662</td>
<td>1.906</td>
<td>3.568</td>
<td></td>
</tr>
<tr>
<td>2035</td>
<td>2.889</td>
<td>3.301</td>
<td>6.190</td>
<td>74</td>
</tr>
<tr>
<td>2055</td>
<td>4.016</td>
<td>4.518</td>
<td>8.534</td>
<td>38</td>
</tr>
</tbody>
</table>
Increases in (Residual) Life Expectancy for Australians at age 65 years

In 2035 Australian men aged 65 years can expect to live to 87.7 years and women to 89.4 years (84.8 & 87.4 in 2015)
An International Comparison of Employment Rates

Source: OECD, Older Workers Scoreboard, 2014
Laurie’s Labour Economics 101

wages, employment and income

The Labour Market
Demand For Labour

Decisions to hire & deploy = f(MR vs MC)

- how productive a worker is or how hard they are working
- imperfect knowledge about worker ability
- price of labour
- working conditions & arrangements
- investment in training
- labour market regulation - rates of pay (minimum wages laws), regulation of Industrial Relations and employment conditions, dismissal-ending employment regulations.

Effective Age of Labour Market Exit (i.e. when do people retire in Australia?)

• Women retire at an average age of 62.9 years

• Men retire at an average age of 64.9 years
Why does NZ do so well?

- Qualifying age for the state pension (NZS) increased from age 60 to 65 between 1992 and 2001;
- Income-test on other earnings was removed in 1998 so that there was no longer a financial penalty on earning extra income;
- NZ’s recent economic recovery, following the GFC, increased job opportunities including drawing back into the workforce many older workers on the fringe of the labour market;
- Technological changes reducing the manual intensity of some types of work;
- An increased share of work that is knowledge- and skill-intensive rather than being manually intensive; and
- An ongoing skill shortage that has increased older workers’ bargaining power
- **Better health and the recognition among older people of the benefits of keeping active** (RPRC Pension Briefing, 2014-4).
Country differences in health status and life expectancy matter

Proportion of people reporting good, very good or excellent SAHS, 2011-2012

<table>
<thead>
<tr>
<th></th>
<th>45-64</th>
<th>65+</th>
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<tbody>
<tr>
<td></td>
<td>Males</td>
<td>Females</td>
</tr>
<tr>
<td>Australia</td>
<td>82.7</td>
<td>84.2</td>
</tr>
<tr>
<td>New Zealand</td>
<td>88.8</td>
<td>89.1</td>
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</table>

Source: OECD Health Statistics Database
Concept of Health Capital (Michael Grossman)

• **Good health** = commodity that is demanded (direct utility & determines the total amount of time available for market and nonmarket activities)
• Health is a durable capital stock
• Individuals inherit an initial stock of health that depreciates over time at an increasing rate (at least after some stage in the life course) and can be increased by investment
• Death occurs when health stock falls below a certain level
• Investments in health capital are produced by household production functions and generally increase with age
Employment of 60-69 year olds by Occupation (%), 2013

Source: NATSEM calculations from HILDA, wave 13 unit record data
Employment of 60-69 year olds by Industry (%), 2013

Source: NATSEM calculations from HILDA, wave 13 unit record data
Proportion employed either full or part-time by health status (2011-12)

Source: ABS Tablebuilder 2011-12 National Health Survey
Modelling Health Transitions as People Age and Future Workforce Participation
Modelling Health Transitions as People Age and Future Workforce Participation

Δs in Health stock, depreciation and return on investment
Modelling

A) Changes in health status of Australians as they age from 60 to 70 years

- Used the longitudinal data available in the HILDA survey, a cohort of individuals aged 60 years in 2001-2003 were pooled, the cohort was followed for 10 years, and changes in health status identified.

B) Projected health status of mature-aged Australians in 2035

- Using the shifts in health status experienced by respondents in waves 1 to 13 (2001-2013) of the HILDA survey, the likely transitions in the health status of 40-54 year olds in 2015 over the next 20 years was modelled based on their age, gender and health status in 2015.

- The proportion of 40-54 year olds in 2015 who are likely to be working in 2035 when they are 60-74 years of age was estimated based on their health status in 2015, survival to 2035, and taking into account recent trends in workforce participation and health status.
# Health Status Projections

## Future health stock

<table>
<thead>
<tr>
<th>Health status in 2015 (Years)</th>
<th>Health Status in 2035 (age 60-74 Years)</th>
<th>Excellent</th>
<th>Very Good</th>
<th>Good</th>
<th>Fair</th>
<th>Poor</th>
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<tbody>
<tr>
<td>Excellent</td>
<td></td>
<td>30.8</td>
<td>36.2</td>
<td>22.2</td>
<td>8.2</td>
<td>2.6</td>
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<td></td>
<td>28.9</td>
<td>36.9</td>
<td>23.0</td>
<td>8.5</td>
<td>2.7</td>
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<tr>
<td></td>
<td>24.2</td>
<td>38.0</td>
<td>25.3</td>
<td>9.5</td>
<td>3.0</td>
<td></td>
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<tr>
<td>Very Good</td>
<td></td>
<td>22.4</td>
<td>34.4</td>
<td>26.9</td>
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<tr>
<td></td>
<td>20.5</td>
<td>34.5</td>
<td>27.8</td>
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<td>16.7</td>
<td>34.1</td>
<td>29.9</td>
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<td>Good</td>
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<td>Poor</td>
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</table>

**Current health stock**

**Net effect of depreciation and investment**
### The Propensity of 60-74 year olds in 2035 to Work

<table>
<thead>
<tr>
<th></th>
<th>Males</th>
<th>Females</th>
</tr>
</thead>
<tbody>
<tr>
<td>40-54 year olds in 2015</td>
<td>2.39m</td>
<td>2.43m</td>
</tr>
<tr>
<td>How many working in 2035</td>
<td>847,300</td>
<td>609,000</td>
</tr>
<tr>
<td>Percent</td>
<td>35.5</td>
<td>25.1</td>
</tr>
</tbody>
</table>

**Scenario – 10% improvement in health transition rates**

<table>
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<tr>
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<tr>
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<td>2.39m</td>
<td>2.43m</td>
</tr>
<tr>
<td>How many working in 2035</td>
<td>868,200</td>
<td>623,500</td>
</tr>
<tr>
<td>Percent</td>
<td>36.4</td>
<td>25.7</td>
</tr>
<tr>
<td>△</td>
<td>0.9 (2.5%)</td>
<td>0.8 (2.4%)</td>
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<tr>
<td></td>
<td>21,000 workers</td>
<td>14,500 workers</td>
</tr>
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</table>
Discussion

• Raising Age Pension qualifying age is a simplistic solution to complex social and economic issues
• The change in the Age Pension eligibility age from 65 to 70 years is estimated to add around 0.8 percentage points to the total participation rate in 2054-55
• Small investment in health capital could easily achieve same outcomes and in a shorter period of time
• Little correlation between official and effective ages of retirement
• Australia currently has the 4th lowest level of public pension spending of any OECD country and is projected by 2050 to have the 3\textsuperscript{rd} lowest level of pension spending.
Discussion

• Major equity concerns
  – unfair to delay retirement from laborious jobs
  – expect older workers to cope with a labour market that discriminates and employers who don’t want to invest in them
  – who wants to work
  – one single pension age doesn’t fit all people
    • some disadvantaged groups have lower levels of life expectancy (LE)
    • at age 60 years the difference between LE for those in the highest income quintile and the lowest income quintile was 5 years for men and 5.4 years for women (Clarke & Leigh)

– years of pension receipt
Concluding Remarks

• Is increasing the pension age an effective way of addressing current and future Government budget challenges? (NCoA recommended age pension age increase to 70 by 2053)

• And will we be healthy enough to be able to work until we are 70?

Wait for the upcoming release of the next AMP-NATSEM Income-Wealth Report

_Federal Treasurer Joe Hockey is open to the idea of automatically increasing the pension age to keep it in line with growing life expectancy_
Thank you

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