

EMPLOYMENT AND THAT MAGICAL YEAR, 2008

Everyone knows that 2008 promises to be a bellwether year, rife with dramatic changes already glimpsed. Some harbingers of change are obvious. A new president will be elected—though campaigns hide as much as reveal what that president will choose or be forced to do. The subprime mortgage market also portends dramatic changes in the financial markets in 2008 and beyond. But perhaps the biggest change of all is a sleeper so far—the first year of a scheduled drop-off in employment growth that will last for some 30 years running. If this decline is left unchecked, the net impact on employment will be far greater and longer lasting than the temporary employment dip during the Great Depression.

Suppose that the economy was about to suffer the equivalent of an increase in the unemployment rate of about 3/10 of 1 percent every year for the next 30 years. Further suppose that in many of those years, the number of workers declined rather than rose. Meanwhile, suppose that the rate of revenue growth declined along with employment growth—at the very same time that the rate of government spending starting rising rapidly because more and more people qualified for "elderly" benefits.

If you were an official in charge of economic policy, would you be worried? If you're an investor in stocks and bonds, should you be concerned?

Well, you should be. These ominous trends and more are now at the starting gate. The unprecedented mega-transition scheduled for the U.S. economy stems from both demographics and public policy. The rise and coming fall in employment of the baby boom generation—those born between 1946 and 1965—provides much of the demographic impetus.

Tracing the impact of the baby boomers on the economy over the years has often been likened to following a pig swallowed by a python. First, the boomers affected their parents' demand for post-World War II housing. Then their ranks swelled enrollment in primary and secondary schools. From the mid-1960s to the mid-1980s, college enrollment ballooned. Lately, the baby boomers have been stocking away retirement assets, adding to the national total, and, through increased demand, driving up the prices for second and vacation homes.

So how does the swallowed pig affect the national employment picture? When the Reaganites and the Clintonites brag about job growth during the 1980s or 1990s, they are mainly trying to claim personal credit for the number of human eggs fertilized from 1946 through 1965. Those embryos became babies who became workers and swelled the labor markets a few decades later.

Two other demographic factors added to labor market buoyancy and lack of fiscal pressure during the period that boomers stocked the workforce. First, these boomers came on the heels of a baby bust population born during the Depression and World War II, so growth in the ranks of the elderly was restrained. Also, women entered the labor market in droves, eventually reaching employment levels close to men's.

One net result was that U.S. employment grew 12 percent in the 1950s, 20 percent in the 1960s, 26 percent in the 1970s, 20 percent in the 1980s, and 15 percent in the 1990s. From 2000 to 2007, the growth was roughly 7 percent.

Public policy adjusted to the pig in the belly of the snake partly by taking advantage of the additional revenues provided by the new workers. Occasionally, elected officials increased subsidies for housing, education, and retirement saving to accommodate this generation. They also offered more and more years of retirement support and higher annual benefits to each succeeding generation of retirees.

But that was then. If higher employment growth spurred economic demand and growth, as well as government revenues and spending, in the past, what is lower employment growth likely to mean for the future?

We often read statistics about when Social Security funds will become inadequate to pay promised benefits. But the current system's obligations aren't confined to giving bigger benefits to more people. Besides that tall order, policymakers will have to deal with the projected decline in revenue growth rates as close to one-third of the adult population moves onto Social Security.

We can hold off on the hand-wringing only if we believe that demand for older workers will swell and that many boomers will stay in the workforce. I, for one, think that can happen and that many of the doomsday scenarios for this new labor market are wrong. Yet, the supply of older workers will be crimped as long as public and private employment policies stay rooted in the 1970s—or even the 1990s. How fast and well employers and government officials adjust will determine whether demographic changes poised to unfold starting in 2008 bolster or drag down the economy. Among the tallest of orders is to move away from private and public policies that now encourage retirement in middle age—a subject for another time.