

# The Looming Budgetary Impact of Society's Aging

The federal budget-making process is near-term in nature, with rules and procedures that are applicable only five or 10 years into the future. As a result, the looming multidecade rise in government spending associated with society's aging is not in the budget picture on which the Administration and the Congress are required to act annually.

The relatively sanguine budgetary outlook for the next decade does not encompass the demographic shifts—emerging with the retirement of the post-World War II baby-boom generation—that will cause federal spending to begin rising sharply within the next 20 years (see *Figure 1*). At the same time, the near-term outlook offers an opportunity to introduce the necessary policies to mitigate the long-term pressures. Those policy changes affecting federal commitments to the elderly should be implemented far enough in advance to offer future recipients of Social Security and other entitlement benefits time to alter their savings and retirement plans.

For the President and the Congress, the immediacy of having to make year-to-year budgetary policy will always place heavy emphasis on the near term. However, it is critical for policymakers to begin addressing the long-term budgetary pressures associated with the aging of the U.S. population.

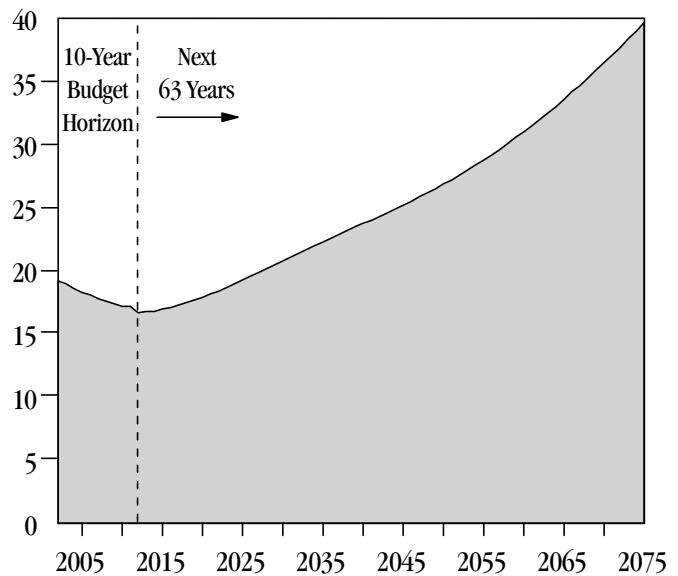
## The Near-Term Focus of the Budget-Making Process

Federal budgeting does not have a long time horizon. The Congress enacts annual budget resolutions that look no farther ahead than the next 10 years, and annual budget projections and updates prepared by the Congressional Budget Office (CBO) and the Administration's Office of Management and Budget (OMB) typically are limited to five- and 10-year periods. Appropriations similarly reflect a near-term perspective as they are made from year to year. This emphasis on the near term is set by precedent and long practice.

**Figure 1.**

## Federal Outlays, Fiscal Years 2002 to 2075

(As a percentage of GDP)



Source: Congressional Budget Office.

Note: For a discussion of these projections, see Congressional Budget Office, *A 125-Year Picture of the Federal Government's Share of the Economy, 1950 to 2075*, Long-Range Fiscal Policy Brief (July 3, 2002).

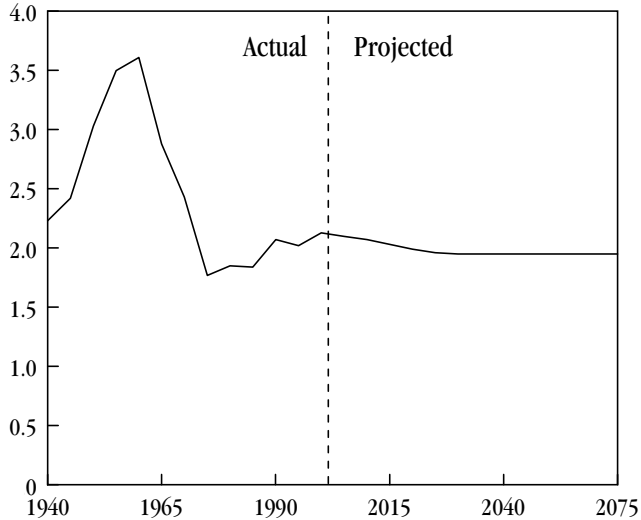
Although long-range projections are not part of the budget process, they have been made regularly for Social Security and Medicare, as well as for a number of other federal retirement and disability systems.<sup>1</sup> In Social Security's

1. The projections made for these programs routinely have been published in separate reports by agencies or trustees as long-range actuarial evaluations of the programs. They have not been published in a single report nor presented in a budget format. However, aspects of them have been consolidated as part of a required analysis of the federal government's financial statements and are now published annually in the Treasury Department's *Financial Report of the United States Government, 2001* (March 29, 2002). The underlying assumptions often are not consistent from program to program.

**Figure 2.**

**Birth Rates**

(Births per woman in her lifetime)



Source: Social Security Administration, *The 2002 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds* (March 26, 2002).

early years, the program’s trustees used a projection technique that employed an “infinite” period of valuation, and since 1965, they have used a 75-year period. For Medicare, long-range estimates have been a more recent phenomenon. For the Hospital Insurance portion of the program, 25-year projections were the practice until the mid-1980s. For the Supplementary Medical Insurance part of the program, only annual projections were routinely made.

In recent years, as attention has been drawn to the long-range demographic trends affecting the nation, both the Administration and CBO have been called on to make longer-term estimates. The trustees for both Social Security and Medicare now routinely make 75-year projections, and both OMB and CBO have been issuing long-range budget projections since the mid-1990s.

In a period of stable demographic trends and modest swings in the economy, a short horizon for budgeting may be sufficient as a framework for policymakers to operate in. But it does not provide a long enough perspective to address the very large and continuing rise in government spending that will occur 20 to 30 years from now. The outlook reflected in CBO’s baseline projections for fiscal

years 2003 to 2012 (the latest of which were issued in March 2002) and in the subsequent decade is relatively favorable, as modest surpluses are expected to arise within the next few years and to continue until the early 2020s (under the assumption that current policies are not altered). However, the first of the baby boomers will become eligible for Social Security in just six years, and the seeds for a long-term rise in federal spending begin to emerge shortly thereafter as more and more members of that generation draw on the government’s largest entitlement programs.

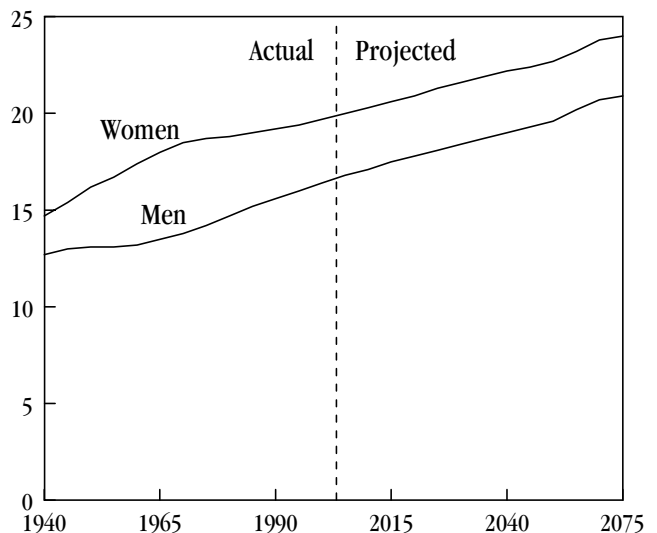
**Society’s Aging and Entitlement Programs**

Certainly, long-range projections are subject to unforeseeable economic and political events. In the short term, budget projections can change significantly (even from year to year, as recent experience has shown), and relatively small changes can have very large long-range effects as they are compounded through time. Therefore, skepticism about long-range estimates is justified.

However, a substantial portion of the demographic change underpinning the long-term budgetary outlook is in place. The “baby boom” and subsequent “baby trough” are events that have occurred; the subsequent uptick in

**Figure 3.**

**Years of Life Remaining at Age 65**

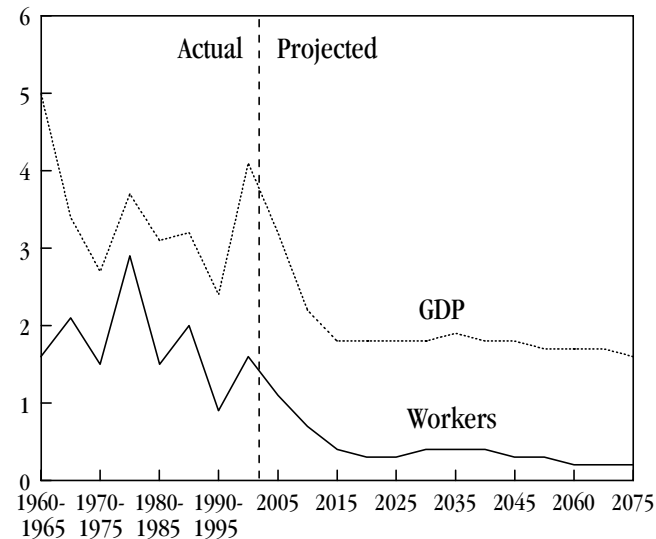


Source: Social Security Administration, *The 2002 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds* (March 26, 2002).

**Figure 4.**

## Growth in Real GDP and the Number of Workers

(Annual percentage)



Source: Social Security Administration, *The 2002 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds* (March 26, 2002).

Note: For the period prior to 2001, the figures represent five-year averages.

birth rates has not been substantial and may now have leveled off; and life expectancy continues to increase (see *Figures 2 and 3*). As a share of gross domestic product (GDP), spending for Social Security, Medicare, and Medicaid—the three entitlement programs most affected by the looming demographics—appears to be relatively stable over the next five years, growing only modestly. However, 10 years out, the outlook starts to change. The population age 65 or older will be growing rapidly. Although that segment constitutes 12 percent of the population today, according to the Social Security and Medicare trustees it is expected to grow to 18 percent in 2025, 21 percent in 2050, and 23 percent in 2075. At the same time, growth in the nation's workforce is expected to slow, resulting in a more slowly growing economy (see *Figure 4*). By 2035, the number of elderly will double, while the number of workers contributing to Social Security and Medicare will rise by only 17 percent. The ratio of the population ages 65 or older to the population in its prime working years (ages 20 to 64) will grow from 21 percent today to 32 percent in 2025 and 42 percent in 2075 (see *Figure 5*).

Exacerbating the population trends, Social Security benefits are automatically scheduled to rise in tandem with workers' wages, at a rate that is likely to exceed inflation. And the cost of medical care is expected to continue to climb at an even faster rate because of better technology and the demand for more and better medical services—a rate that for years has consistently outpaced the growth of GDP. As a result, national health expenditures, including those financed by Medicare and Medicaid, will absorb a rising proportion of the nation's production.

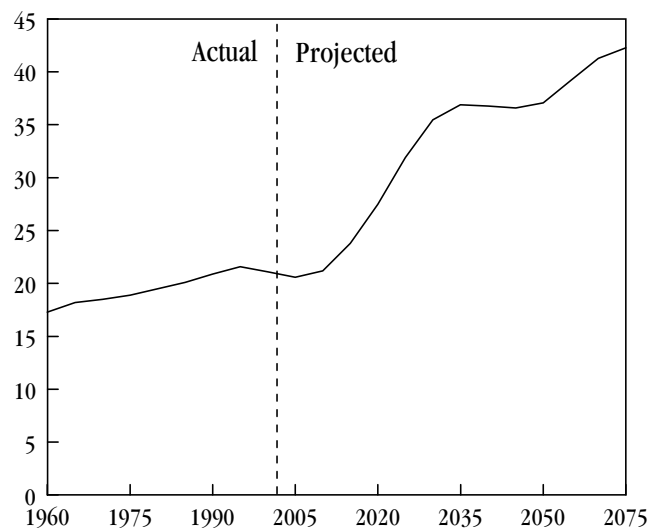
## The Necessity of Looking Beyond the Near-Term Budgetary Window

Although these demographic and budgetary trends are not new to fiscal policymakers, the budget process does not provide an effective means to address them. That said, the near-term focus of the process does not preclude a longer view. In the past, major reforms of entitlement programs have taken both near-term and long-range concerns about fiscal policy into account.

**Figure 5.**

## The Population Age 65 or Older as a Percentage of the Population 20 to 64

(Percent)



Source: Social Security Administration, *The 2002 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds* (March 26, 2002).

However, unlike the circumstances leading to earlier reforms, the situation today poses no imminent threat to anyone’s benefits. But the problem with waiting until the rapid escalation in costs falls within the budget window is that doing so may not leave sufficient transition time to deal with it in a gradual fashion.

Reform requires an awareness of the financial pressures that lie ahead and a consensus that legislative changes are necessary. The information presented here and in other long-term budget analyses is intended to help policy-makers acquire a fuller perspective about the issue and make prudent decisions. ■

**Supporting Tables**

**Economic Trends and Projections**

(Percent)

| Calendar Year | Average Annual Rate of Growth |                   |
|---------------|-------------------------------|-------------------|
|               | Real GDP                      | Number of Workers |
| 1960-1965     | 5.0                           | 1.6               |
| 1965-1970     | 3.4                           | 2.1               |
| 1970-1975     | 2.7                           | 1.5               |
| 1975-1980     | 3.7                           | 2.9               |
| 1980-1985     | 3.1                           | 1.5               |
| 1985-1990     | 3.2                           | 2.0               |
| 1990-1995     | 2.4                           | 0.9               |
| 1995-2000     | 4.1                           | 1.6               |
| 2005          | 3.2                           | 1.1               |
| 2010          | 2.2                           | 0.7               |
| 2020          | 1.8                           | 0.3               |
| 2030          | 1.8                           | 0.4               |
| 2040          | 1.8                           | 0.4               |
| 2050          | 1.7                           | 0.3               |
| 2060          | 1.7                           | 0.2               |
| 2070          | 1.7                           | 0.2               |
| 2080          | 1.6                           | 0.2               |

Source: Social Security Administration, *The 2002 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds* (March 26, 2002).

**Demographic Trends and Projections**

| Calendar Year | Life Expectancy at Age 65 <sup>a</sup> |      | Births per Woman | Population Age 65+ as Percent of Population 20 to 64 |
|---------------|--|------|------------------|--|
|               | Women                                  | Men  |                  |  |
| 1940          | 79.7                                   | 77.7 | 2.23             | 11.6   |
| 1950          | 81.2                                   | 78.1 | 3.03             | 13.8   |
| 1960          | 82.4                                   | 78.2 | 3.61             | 17.3   |
| 1970          | 83.5                                   | 78.8 | 2.43             | 18.5   |
| 1980          | 83.8                                   | 79.7 | 1.85             | 19.5   |
| 1990          | 84.2                                   | 80.6 | 2.07             | 20.9   |
| 2000          | 84.7                                   | 81.4 | 2.13             | 21.1   |
| 2010          | 85.3                                   | 82.1 | 2.07             | 21.2   |
| 2020          | 85.9                                   | 82.8 | 1.99             | 27.5   |
| 2030          | 86.6                                   | 83.4 | 1.95             | 35.5   |
| 2040          | 87.2                                   | 84.0 | 1.95             | 36.8   |
| 2050          | 87.7                                   | 84.6 | 1.95             | 37.1   |
| 2060          | 88.2                                   | 85.2 | 1.95             | 39.2   |
| 2070          | 88.8                                   | 85.7 | 1.95             | 41.3   |
| 2075          | 89.0                                   | 85.9 | 1.95             | 42.3   |

Source: Social Security Administration, *The 2002 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds* (March 26, 2002).

a. Projected age at death.

**Related CBO Publication:** *Social Security: A Primer* (September 2001) and *A 125-Year Picture of the Federal Government’s Share of the Economy, 1950 to 2075*, Long-Range Fiscal Policy Brief (July 3, 2002).

**Contacts:** This policy brief was prepared by Dave Koitz, Melissa D. Bobb, and Ben Page. It and other publications by CBO are available at the agency’s Web site: [www.cbo.gov](http://www.cbo.gov).