Aging and Declining Birth Rates: Economic Impact and Coping Strategies

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Abstract: *Recently, the China Finance 40 Forum and the China Center for International Economic Exchanges jointly held the 6th Bund Summit, where discussions focused on topics such as the economic impact and coping strategies for Aging and declining birth rates, as well as how pension finance can meet the diverse needs under the silver economy.*

Experts at the summit pointed out that Aging is rapidly accelerating in Asia, and China has already entered a "moderately aging" society. The combined effects of population Aging and low birth rates leading to a shrinking total population will significantly impact trends of long-term economic growth.

Experts suggested that the elderly could serve as a driving force for modernization to improve development quality with the current demographic structure. Solutions could involve expanding the workforce and enhancing productivity to cope with aging. The government should also increase investment to ensure the well-being of the elderly.

The experts emphasized the importance of developing "pension finance," promoting financial services for the elderly, accelerating the transformation of the pension system, strengthening the results of the third pillar pension insurance system, and deepening capital market reforms to address the challenges posed by aging.

I. Trends of Population Aging and Its Economic Impact

Albert Park, Chief Economist at the Asian Development Bank, highlighted that aging is accelerating across Asia, yet many countries are ill-prepared. By 2050, the percentage of the population aged 60 and above in Asia is expected to double, reaching 25%. The elderly population will total 1.2 billion. Although different countries in Asia are at varying stages of demographic transition, the aging is generally faster compared to traditional developed countries, and many face the challenge of "aging before becoming wealthy."

Cai Fang, Chairman of the CF40 Academic Committee and Chief Expert of National Think Tank at the Chinese Academy of Social Sciences, pointed out that as of 2023, 15.4% of China's population is aged 65 or older, which marked the enter of the "moderate aging" stage. By 2032, this proportion is expected to rise to 21%, entering a phase of "deep aging." Simultaneously, China is facing challenges from declining birth rates, as the fertility rate is dropping rapidly. The seventh national census showed that China's total fertility rate was 1.3%, and according to the World Bank, it further decreased to 1% in 2022.

Masaaki Shirakawa, former Governor of the Bank of Japan and Distinguished Professor at Aoyama Gakuin University, noted that aging populations and low birth rates that lead to overall population decline will have a significant impact on long-term economic growth.

First, aging will lead governments to allocate more funds to social welfare programs, thus reducing investment in basic research and education, which can slow productivity growth.

Second, aging also affects the speed at which societies adopt new technologies. Economic productivity largely depends on a society's ability to embrace new technology, but older populations are slower to adapt to technological changes.

Third, population decline weakens economies of scale, which are critical to productivity. In cities with shrinking populations, maintaining the public infrastructure (such as roads, hospitals, and schools) becomes more expensive once the population falls below a certain threshold. Private sector services face similar challenges.

II. Strategies for Addressing Population Aging

Cai Fang emphasized the importance of the current demographic structure, and he viewed the elderly as a driving force for modernization to improve development quality. Rather than a burden, he advocated for regarding the elderly as workforce and consumers to support Chinese modernization. The challenge of "aging before becoming wealthy" presents not only obstacles but also opportunities with potential latecomer advantages. China's potential productivity is much higher than other countries at similar levels of aging, because of a solid material foundation for modern development. To tackle aging, Cai stressed the need to enhance the supply of elderly care services to meet the growing needs. At the same time, efforts should be made to improve public services, reduce the costs of childbirth, childcare, and education, thus encouraging higher fertility rates.

Masaaki Shirakawa highlighted that addressing aging through labor force expansion and productivity improvement is essential. First, increasing labor force participation. The most direct approach is to raise the labor participation rate. While Japan has a high labor participation rate among older populations, there is room for improvement in female participation, especially in leadership positions. A significant reason for Japan's lower female participation is that few women play managerial roles. Second, attracting foreign workers or immigrants. Embracing more foreign employees or immigrants can help mitigate labor shortages. Third, raising birth rates. Creating a favorable environment for young couples to raise children is crucial. International comparisons show that birth rates are positively correlated with the share of men contributing to household chores and child-rearing.

Albert Park suggested that governments should invest more in the health security of the elderly and improve their well-being. This would not only enhance their quality of life but also reduce health problems and medical costs, helping governments avoid higher expenditures in the future. While China has made significant strides in expanding basic healthcare and pension systems, the support remains insufficient, as disparities are prominent in health conditions among elderly individuals based on gender, region, and occupations.

Park also proposed that delaying retirement could effectively alleviate labor shortages and increase elderly labor participation. He outlined three ways to ease the implementation of delayed retirement policies: First, plans are announced in advance to raise the retirement age years for more time to adapt. Second, people are allowed to retire at the legal age while encouraged to work further through incentive policies. Third, ensuring that the design of pension system do not stimulate productive workers to retire early. In addition, providing lifelong learning opportunities for the elderly is a vital investment.

Masaaki Shirakawa believed that while artificial intelligence (AI) and robotics could alleviate some impacts of population decline, they are not a solution once for all. AI and robotics represent capital investments. With the increasing capital investment, the rate of return on capital will gradually diminish, eventually weakening productivity growth. Additionally, as populations shrink, the sources of capital supply itself will face challenges.

III. Developing "Pension Finance" to Address Population Aging

Zhang Xiaohui, CF40 Non-Resident Senior Fellow and former Assistant Governor of the People's Bank of China□emphasized that elderly finance should cover three key areas: pension finance, elderly industry finance, and elderly service finance. Among these, elderly service finance is particularly critical as individuals require financial services at every stage of life. Financial institutions must adhere to a "people-centered" approach, reforming the supply side to meet the evolving needs of the elderly. This involves providing tailored financial services to offer comprehensive financial security for older adults.

Jin Luo, Vice Chairman of thethe National Council for Social Security Fund, highlighted two prominent trends in pension system design from international experience. First is the shift from a single-pillar system to a multi-pillar one, especially by increasing the share of the second and third pillars. Second is the transition from defined benefit (DB) plans to defined contribution (DC) plans. The design should consider several factors, such as coverage, gender equality, benefit adequacy, management efficiency, and cost. Financial sustainability and actuarial balance must also be taken into account. The design must be dynamic, in line with the national context, and adaptable to better address the challenges posed by aging populations.

Zheng Bingwen, Director General of the Center for International Social Security Studies at the Chinese Academy of Social Sciences stressed the need to consolidate the achievements of China's third-pillar pension insurance system. While this system has only been in place for two and a half years, its coverage has exceeded expectations. However, only 22% of account holders actively contribute, reflecting a mismatch between account openings and contributions. One reason for this may be the poor investment returns of third-pillar products. Among the four product types—savings, bank wealth management, pension insurance, and public funds—only insurance and savings products have had positive returns, while the rest have frequently experienced negative returns. Publicly offered funds have generally fallen below their net value, with overall returns performing poorly. If this continues, the third pillar may fail to fulfill its intended role.

Zheng further pointed out that reforming the capital market is essential to restoring confidence in the third pillar. A a package of policies to revitalize the capital market and boost investor confidence since the last year is crucial for enhancing the third pillar's attractiveness. Besides external reforms, internal adjustments are also necessary. For instance, the current range of products is limited, and homogeneous competition exists. Expanding product diversity and offering more options could improve the system.

Liu Zhihui, President of Industrial Securities, suggested that securities firms can provide support for wealth management in the pension sector. Given the long investment cycle, significant capital requirements, and uncertain returns in the elderly care industry, its funding mainly relies on government and insurance support. In this context, securities firms can contribute through innovative financing tools such as asset-backed securities (ABS), real estate investment trusts (REITs), and specialized bonds for the elderly care industry, thereby unlocking more financial resources for the sector.

Li Jing, Deputy General Manager of Changjiang Pension, noted that there are significant structural differences in pension reserves among different income groups. The coverage of basic pensions should be further expanded and strengthened, particularly for workers in emerging industries. Drawing from international experiences, such as Germany's "Riester Pension," where the government provides financial subsidies to encourage individuals to save for retirement, could enhance the overall level of pension security in China.