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AUSTRALIAN LABOUR SUPPLY BULLETIN

Rising trend in participation despite ageing population

Key points

- It is usually assumed that an ageing population means a shrinking workforce relative to total population. In many advanced economies, though, the opposite is true. Participation rates are on multi-decade upward trends in many economies, including Australia.
- Policy responses to ageing, such as raising pension ages, have helped offset the ageing effect, but are only part of the story. More important is that population ageing happens because people are living longer, healthier lives and having smaller families. Higher participation in the 55–64 age group and women aged 25+ has more than offset the rising share of older people.
- The US is an outlier, though. There, the participation rate for these groups have seen no upward trend in the past quarter-century. Moreover, participation of males aged 25–54 is lower than at the turn of the century, in contrast to peer economies where downward trends have ceased. This divergence is probably because the US has had worse trends in health and life expectancy.
- These cross-country demographic differences imply different conclusions for macro policy. In Australia, RBA (and Budget) forecasts assume no upward trend in participation from here. If it instead continues, labour market slack will rise more than these forecasters expect. By contrast, the US is developing a singular long-run labour supply issue, irrespective of current migration policies.

Live long and boost labour supply

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Population ageing spurs concerns about a shrinking workforce and calls for policy action to forestall this. For these concerns to be borne out, labour force participation rates would need to decline. In fact, for many advanced economies including Australia and New Zealand, overall participation rates are on a multi-decade rising trend. Australia's participation rate is close to the highest rate since records began in 1910. Economies further along the ageing journey such as Germany and Japan have likewise seen rising trends in participation over the past 20 years, though of course the overall rate is lower than in Australia or New Zealand.

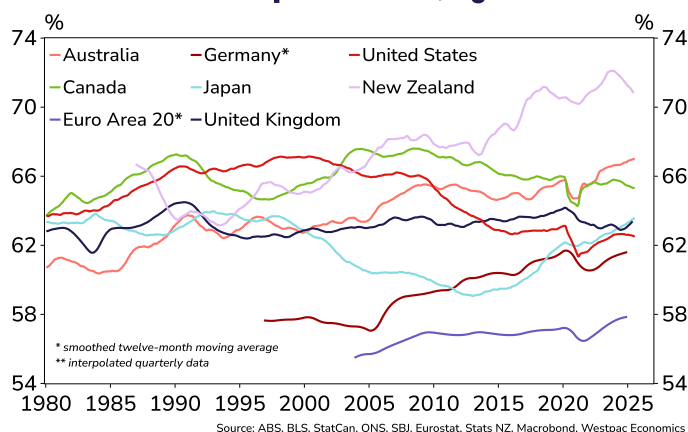
The COVID-19 pandemic arrested these trends for a time as lockdowns and other restrictions took many people out of the workforce. Participation bounced back almost immediately in Australia and New Zealand, though the latter is now seeing a cyclical decline. Even in the UK, a sharp recovery is now evident after a considerable slump.

Policy responses to population ageing have gone some way to offsetting the effect that a higher share of (low-participation) over-65s has on overall participation. Pension eligibility ages have been raised in many countries including Australia. In a number of European countries, the eligibility age is indexed to life expectancy. While retirement is typically not compulsory at this age, pensions are an important income source for low- and middle-income workers after they retire. The eligibility age also represents a kind of 'permission' to retire for those not reliant on government pensions. As a result of these policy changes, participation rates of over-65s have increased greatly from a low base.

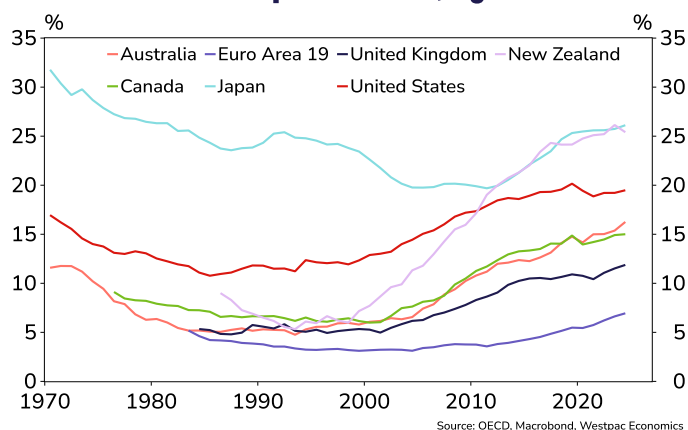
The extent of the increase has varied across economies, partly driven by the adequacy of pension incomes, and partly by the details of pension systems. For example, one of the reasons why participation rates for over-65 New Zealanders are higher than those in Australia is that the age pension system there is [not means tested](#). Older New Zealanders can therefore continue working without losing any pension income.

Participation has not only risen for the over-65s, though. The participation rates of people aged 55 and over of both sexes and of women aged 25–54 have risen noticeably over the past two decades in many advanced economies. This follows a downward trend in the 1980s and 1990s that has since reversed. The turning point was around the turn of the century: in some countries, a little earlier and others a little later. In many cases, including Australia, these within-group changes in participation have more than offset the increase in the share of the population in older age groups, who participate less than the population average. In a few countries, such as Canada, the within-group increases have not quite been enough to generate an overall upward trend, but the within-group behaviour has been similar.

Labour Force Participation Rates, Age 15/16+

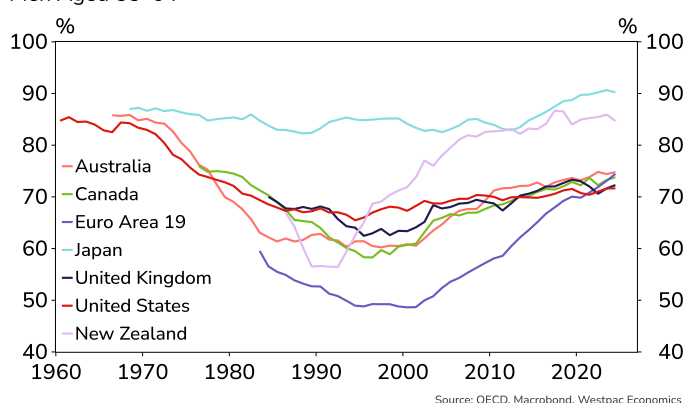


Labour Force Participation Rates, Age 65+



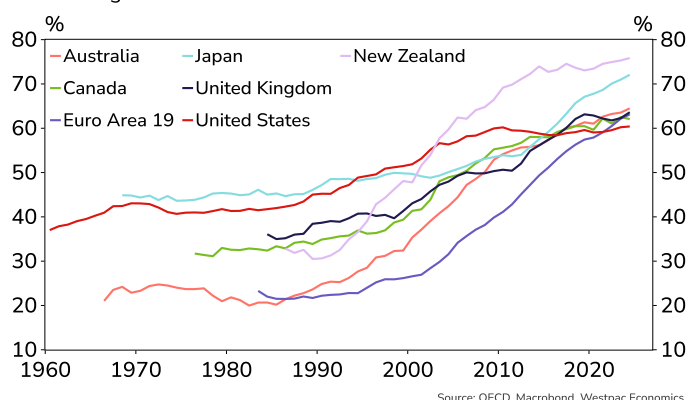
Labour Force Participation Rate

Men Aged 55–64



Labour Force Participation Rate

Women Aged 55–64



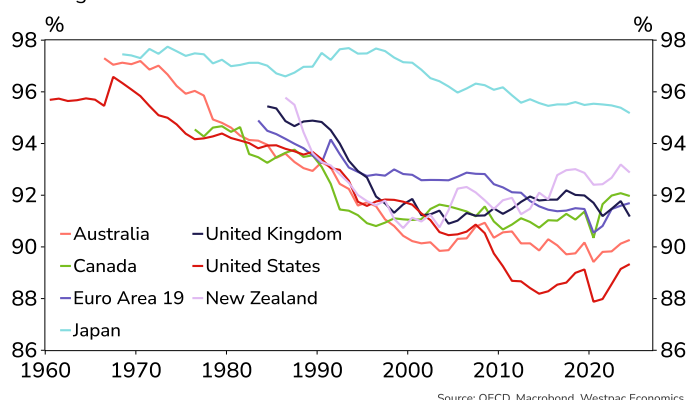
The increase in participation by the 55–64 age group makes intuitive sense (and indeed one of us pointed this out in a [speech back in 2019](#)). Population ageing happens because people are living longer, which necessarily implies that they are on average also healthy for longer. Fewer people therefore retire early due to ill health than they used to. Trends in flexible work and work-from-home will have contributed to this, though not for the whole multi-decade period over which participation rates have increased for these age groups.

There is also a choice aspect to this shift. If people expect to live longer than previous generations, they will often choose to retire later. Partly this is because people can stay active in the workforce for longer. However, it is also because they do not expect that they could fund such extended periods of retirement from savings accumulated over the same number of years in work as previous generations had.

Another aspect of the population ageing story is that people are having smaller families. The historical pattern of mothers staying out of the workforce to care for the children they do have has also become less common. Both social changes have meant that participation rates of women aged 25–54 have increased drastically over the past decades, especially in the countries where it was previously the lowest.

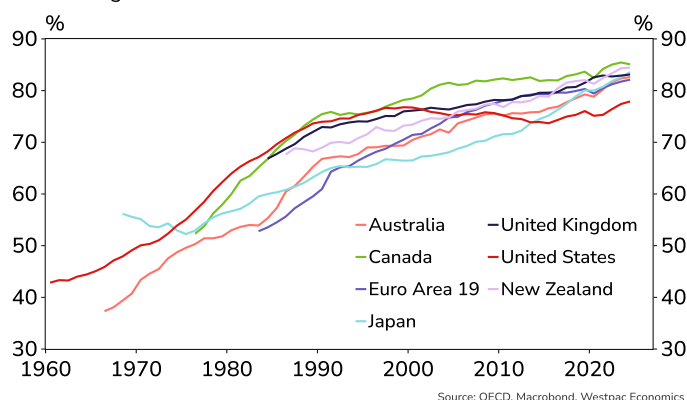
Labour Force Participation Rate

Men Aged 25–54



Labour Force Participation Rate

Women Aged 25–54



The wrong kind of US exceptionalism

The US is an outlier to these trends in a number of respects. This might help explain why the belief that population ageing is weighing on labour supply persists, even though it is not the case in most other advanced economies. Because the United States and its data are so dominant in economic discourse, many observers under-appreciate trends that are not evident there.

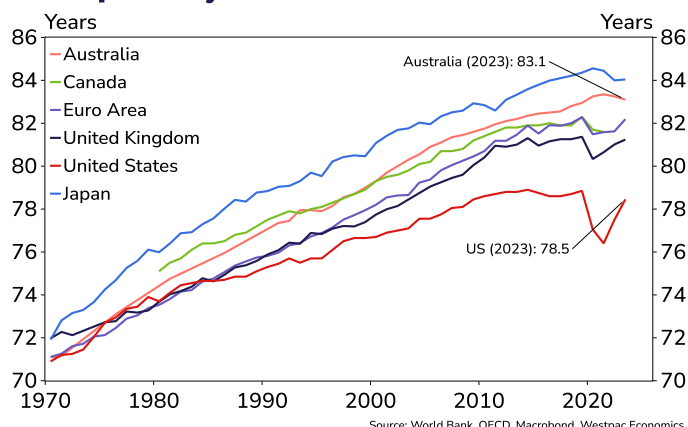
Since 2000, the US has recorded the smallest increases in participation rates for older workers (55–64) and women aged 25–54 and have declined the most for men aged 25–54. Across all four demographic groups, the US now has the lowest participation rates of any of these seven peer economies, and noticeably so for the 25–54 age group. While over-65s participation is higher in the US than the median of this group, the pace of increase has slowed recently, lagging the increases seen in peer economies over the past decade.

Participation rates for males aged 25–54 have trended down in many economies. Part of the reason for this is that more younger adults are undertaking university studies. Thus they enter the workforce later than those with non-university qualifications. But as some [recent analysis from the San Francisco Fed](#) shows, the participation rates of American males without any college education have been falling through time as well; this gap is evident at all ages in this cohort, but especially for men in their 40s and 50s.

Why has the US lagged so much on labour force participation? The answer, we suspect, stems from the drivers of population ageing. The reality is that Americans, unlike their advanced-economy counterparts, have not been living longer, healthier lives over the past 15 or so years. Life expectancy has not increased there for more than a decade and is now well below levels in peer economies, even before the out-sized hit from the COVID-19 pandemic.

Moreover, this is not simply a matter of whether someone makes it to, say, 85 versus 80 years old, which would have limited implications for participation of younger age groups. Premature death rates are much higher in the US than other advanced economies. The burden of disability on capacity to work [has also mattered](#).

Life Expectancy at Birth



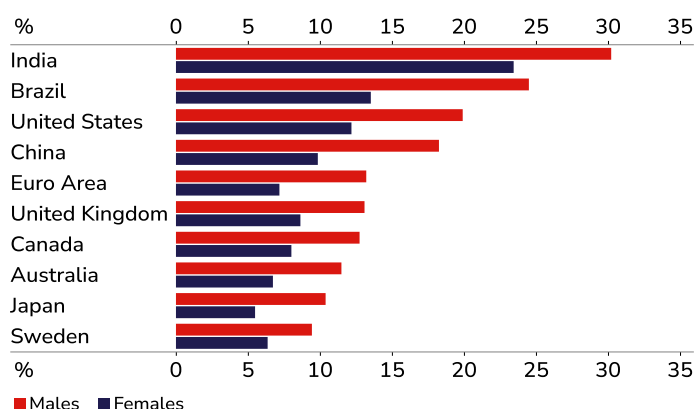
To take one metric as illustrative, even using 2019 data to abstract from the pandemic, almost one in five American men would not make it to age 65. That is worse than the rate in China and almost double the rate in Australia.

A detailed analysis of the reasons for the US's under-performance on life expectancy is beyond the scope of this note. We observe, however, that much of the divergence is accounted for by avoidable premature deaths. The US does worse than many advanced economies on deaths from road accidents, cardiovascular conditions brought on by differences in diet and lifestyle, as well as so-called 'deaths of despair' from opioid and other substance abuse, as well as suicide. We cannot rule out that the introduction of semaglutides and similar drugs, along with policy changes, narrow the US longevity gap. So far, though, we have seen little improvement.

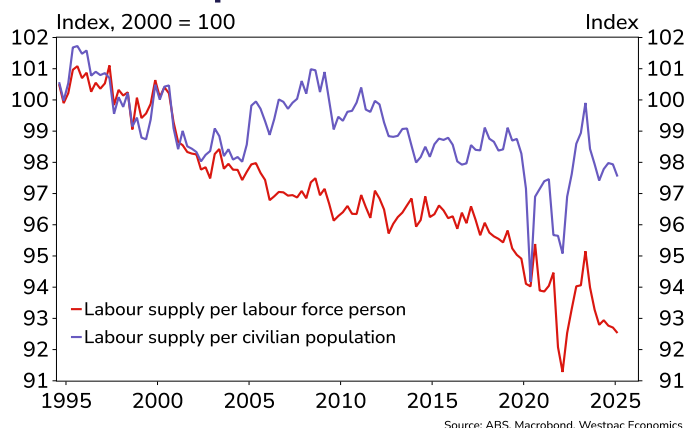
Diverging policy implications

For countries such as Australia where participation is still rising in net terms, policy needs to take this trend into account. Labour supply in heads terms is rising faster than the population. Average hours worked per employed person has been falling. But even on an hours basis, labour supply is stronger than it would appear at first glance. Because of the rising trend in participation, hours supplied by the working-age population – including those outside the labour force and so supplying zero hours – has been reasonably steady for the past quarter-century.

Chance of dying before age 65 (2019)



Available Hours per Person



Rising trend participation has implications for expectations about potential output growth, fiscal revenues and even estimates of neutral interest rates. It also has implications for RBA and Treasury forecasts, which currently assume that both participation and unemployment rates remain relatively constant for the next few years. While 'flat spots' in the overall upward trend in participation have been seen before, such as in the mid-2010s, typically these are periods where labour market slack is rising – which is not the presumption behind the official sector forecasts. If we are right that the upward trend in participation is still operating, policymakers could be surprised by emerging labour market slack over coming years.

At some point, this upward trend in participation might eventually be overwhelmed by the changing composition of the population. The experience of New Zealand, [Japan](#) and some Nordic countries not shown here, suggests that there is probably a limit to how far participation within each age/sex cohort can rise. It is also debatable whether Australia would reach the same heights on these within-group participation rates as Japan and New Zealand, especially for the older age groups. Means-tested public age pensions keeps Australia's welfare system very targeted, but also reduces the incentive for those aged over 67 to remain in the workforce, as many do in New Zealand.

Once those limits are reached, the picture would start looking more like Canada, with its downwards trend in participation despite similar outcomes in the age/sex-disaggregated participation rates. That said, current data suggest that the underlying upward trend could have further to run in Australia.

The policy implications for the US are very different. There, the trend is to deficient labour supply, in ways not seen in peer economies. This suggests the US is more likely to see rising labour costs and skills shortages than its advanced-economy peers, at least for the time being. Migration has obscured this underlying trend, but given the current administration's deportation policies, this might be less help in coming years.

The broader point here is that demographic influences on labour supply go beyond simple assumptions about population ageing. Health outcomes matter, and can differ greatly across countries. The future for Australia is a workforce that is bigger than many assumed – and also older and more female than in the past.



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