

Show Us the Money!

Public Finance Explained

MIND - O P E N E R # 2 :

The Future

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The goal of this session is to give citizens an understanding of the demographic and economic changes that Minnesota is undergoing, some estimates of what this means for the future, and the framework for some of the choices we face.

Minnesota is in a position of strength

Minnesota invested in education 50 years ago and it paid off; these are the good times. We rank among the national leaders in many economic and social indicators.

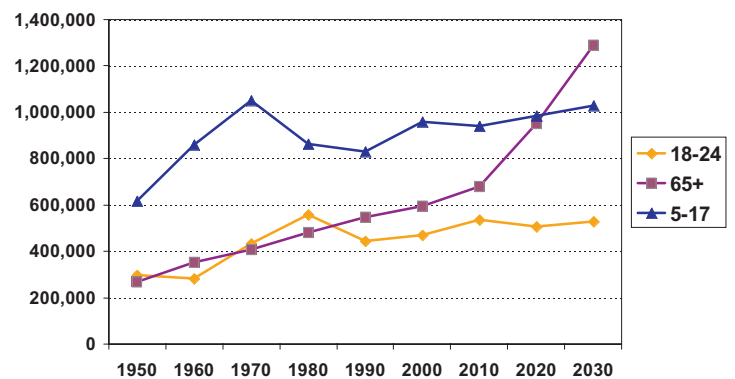
- 1st in percent of population with health insurance
- 2nd lowest poverty rate
- 2nd in percent of population with high school education
- 2nd in percent of population working
- 2nd in home ownership
- 6th in median family income
- 9th in percent of population with college education

We are aging as a society and facing a rapid transition

Nations around the world are aging for the first time in history. In particular, nations in Europe, Japan and the U.S. are facing rapid transitions. We cannot fully anticipate the changes. Aging in Minnesota is combining with:

- growth in population – about half a million people per decade
- change in age distribution of population
- increased migration and diversity

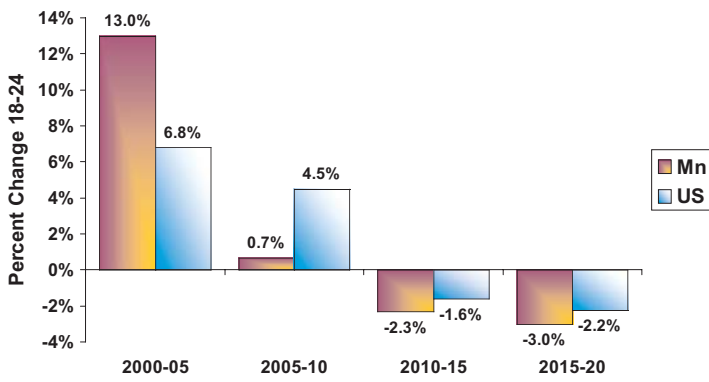
Chart 1



The change in population distribution is not somewhere off in the future; it is happening now. Growth in retirement-age population will start to increase in 2008 and the first wave of the baby boom generation will start to retire in 2011. After 2011, the difference between that 65 and older population and the college-age (18-24) population widens dramatically and by 2020, the 65 and older population will surpass the K-12 school-age (5-17) population (see Chart 1 above).

The slowing in growth in the college-age and K-12 populations means slowing growth in the workers and inventors of tomorrow. They are the ones who will take care of us as we age. The national competition for the “best and the brightest” will increase dramatically as Minnesota and the nation see declines in the number of 18-24 year olds as a percentage of the population (see Chart 2, next page).

Chart 2



In the future, our overall labor force will depend increasingly on migration from other states and nations. Minnesota is currently one of the least diverse states in the nation, but over half of our population growth from 2000-2010 will be people of color. Minnesota has been singled out as a health care and education leader and yet there are large disparities in these areas between minority and white populations that will threaten our future success if not addressed.

In the decades to come, Minnesota will see a dramatic slowing in the growth of the labor force, which will threaten to slow economic growth unless we counter it with an increase in per-worker productivity. Per-worker productivity increases come from things like innovation, invention, new machines, new techniques and a higher-qualified, better educated workforce – it goes right back to the issue of growing disparities in education with young children of color. It becomes a key issue in the economic future of our state.

Borrowers, savers and dissavers

The Household Wage Cycle has three basic stages: borrower, saver and dissaver (see Chart 3, right). As a whole, younger households consume more than they earn and are “borrowers.” Once income begins to exceed consumption, the household becomes a “saver” with the desire to save increasing up to the point of retirement. After retirement, income drops below consumption and the household becomes a “dissaver.”

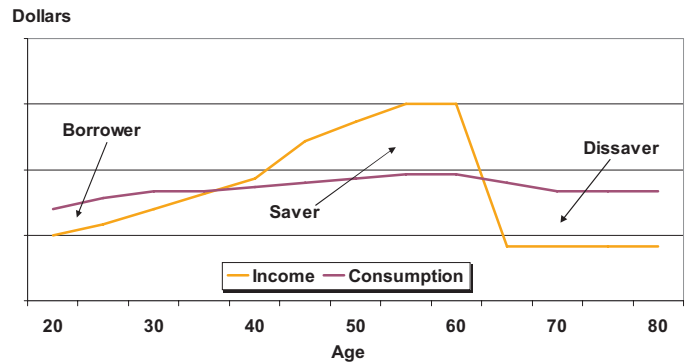
As more people get closer to dissaver status, they want to maintain current consumption and increase savings. The only way to do that is to cut taxes.

This is part of the reason that Minnesota has been experiencing pressure for low taxes. The indicator called Price of Government – which calculates the cost of state and local government as a percent of personal income – was 17.9 percent in 1993 and was down to 15.5 percent in 2002. That’s almost a 2.5 percent change on \$180 billion in personal income, which is about \$4.5 billion dollars. Does that figure sound familiar to anyone? (It is about the size of the 2003 budget deficit.)

The proportion of personal income that we are willing to spend for publicly provided goods and services has gone down. There is nothing wrong with the decision we made, but it is very important to recognize that we as a state – as a society – have made that decision.

The pressure for tax relief is likely to increase over the next decade as more baby boomers seek to save for retirement and more people retire. The economic reality is that when households go from saver to dissaver status, revenue for state and local government goes down. Why does this happen? It’s because of the progressive nature of our income tax, special benefits that we provide to people over 65, and that fact that when you retire you don’t buy as many of the things that are part of our sales tax base.

Chart 3



Can we afford the future? Yes.

Income after taxes is expected to grow 27 percent by 2014. We are going to have to increase spending on health care and save more for retirement, but even with that, about two-thirds of that additional income will be available for other uses. These are the good times.

We are in a period now where the dependency ratio is as favorable as it has ever been going back to 1940. The dependency ratio is a measure of workers to the rest of the population. When the dependency ratio is 50 percent, there are 2 workers for every dependent. We currently have about 2 workers for every one dependent (see Chart 4, right). As the dependency ratio increases, there are fewer workers per dependent. By 2030, Minnesota will only have 1.5 workers per dependent.

We must make choices

Minnesota's rapid transition looks something like this:

- 1990 – over 65 population passed college-age population (see Chart 1)
- 2008 – retirement rate starts to rise
- 2010 – dependency ratio at its lowest going back to 1940 (see Chart 4)
- 2010 – rate of new workers that are Minnesota natives begins to decline (see Chart 5)
- 2011 – first wave of baby boomers turn 65
- 2011 – gap between over 65 and college-age population begins to widen rapidly (see Chart 1)
- 2020 – over 65 population passes K-12 school-age population (see Chart 1)
- 2030 – dependency ratio returns to highest levels since the 1970s and continues at that level for several decades (see Chart 4)

We have the resources and flexibility to make choices now. The question will be what we choose to do. We can spend this increased income on:

- private consumption,
- investment,
- increasing savings,
- new plants and equipment,
- public infrastructure, or
- human capital.

Chart 4

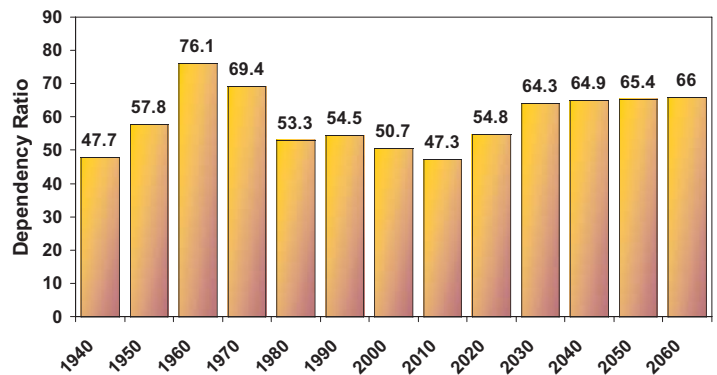


Chart 5

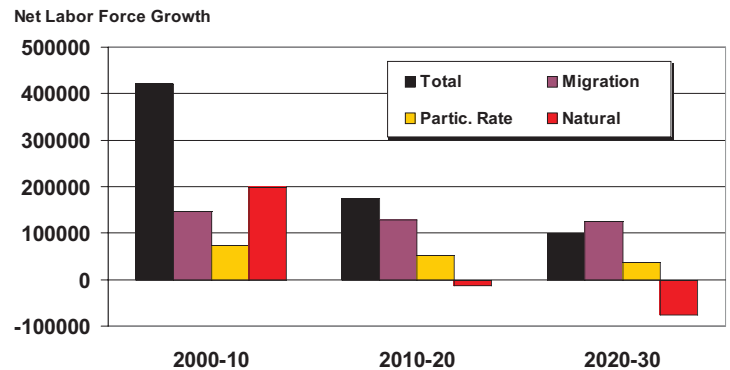
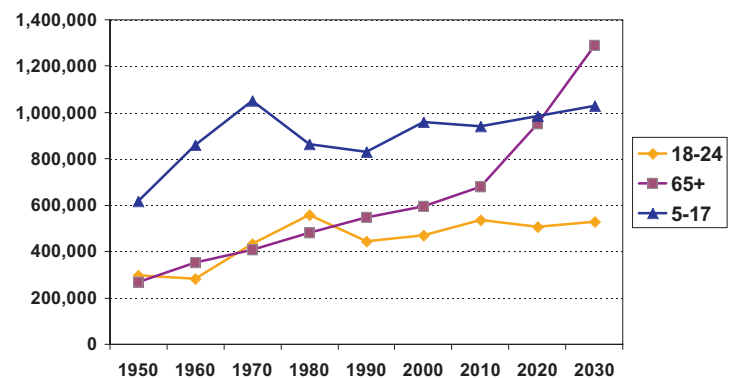


Chart 1



These are the choices that we have to start thinking about. The data is clear that K-12 investment was the big decision 50 years ago, but that was an easier decision to make at the time. What do we invest in now? Even if we were to presume to invest in human capital, where do we invest?

- early childhood,
- K-12 education,
- higher education,
- the incumbent workforce, or
- all of the above?

These decisions are complicated by population growth and change in distribution, migration and diversity.

Minnesota is in a critical period of rapid transition and must make decisions now that will determine what Minnesotans say about our stewardship in 50 years.

Mind-Opener Schedule

Thursday, August 18

The Feds

Tim Penny

Co-Director, Humphrey Institute Policy Forum

Dave Durenberger

Chair, National Institute of Health Policy

How will spending on Medicare and Medicaid affect Minnesota's budget for the next generation?

Wednesday, August 31

The 800-Pound Gorilla in Minnesota: Health Care

Dan McElroy

Chief of Staff to Governor Tim Pawlenty

Jan Malcolm

Chief Executive Officer, Courage Center

Lynn Blewett

Director, Public Health Administration Program
University of Minnesota

How can the state address the demographic time bomb of providing our aging population high-quality health care at a price we all can afford?

Wednesday, September 14

The 800-Pound Gorilla in Our Backyards

Karen Anderson

Mayor of the City of Minnetonka

Matt Smith

Director of Financial Services, City of Saint Paul

How do we meet post-9/11 homeland security demands facing local governments? How can we provide greater public safety with limited resources?

Late September (date to be announced)

Wrap-up Mind-Blower (evening)

Join the Citizens League and reform-minded policy makers to review what we learned in the previous sessions and discuss ideas for how we can most effectively serve the public good.

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