

The Impact of the Baby Boomers' Retirement in Japan

By Kono Ryutaro

JAPAN'S baby boomer generation, born between 1947 and 1949, is fast approaching the age of 60. Although this population segment does not really stand out from others in terms of employment habits or consumption/saving patterns, the fact that it accounts for 5.4% of the entire population, or 6.9 million out of a total population of 126.9 million (National census of 2000), gives it substantial demographic clout. Thus, whenever they go through changes in their lifestyles, the socio-economic consequences are significant.

For instance, when the baby boomers started attending elementary school in the 1950s, problems of insufficient classrooms and teachers arose. Then when they went on to high schools and colleges, the competition in the entrance exams became intense. There were concerns that job hunting would also prove difficult, but this was fortunately averted because the economy at the time, namely during the late 1960s through the early 1970s, was still in the period of rapid expansion. Even so, after landing jobs, the baby boomers found that their real wages tended to be lower than those of other population segments, and promotions were harder to come by. Then during Japan's decade-long economic slump in the 1990s, wage cuts were the most pronounced among the baby boomers; this was not just because the economy was weak, but it reflected the fact that the supply of university-educated white-collar managers had expanded sharply with the baby boomer generation. (Since the baby boomers are a demographic segment with a significantly high degree of university graduates, university-educated managers, still rare until then, became commonplace and even undermined the wages of the baby boomers.) Now, since most companies have set 60 years old as the mandatory retirement age, there will be major economic ramifications affecting things like corporate profits, labor supply-demand

and the savings rate when the baby boomers turn 60 during the period of 2007-2009. This paper will address the likely impact on the labor market and the savings rate.

ACCORDING to estimates from data compiled by the National Institute of Population and Social Security Research, the number of people turning 60, the mandatory retirement age, will be 2.15 million in 2007, 2.25 million in 2008 and 2.25 million in 2009. This, however, does not mean that all 6.65 million of these baby boomers will necessarily leave the labor market for permanent retirement when they become 60 years old. For one thing, the self-employed are not bound by a mandatory retirement age and they often continue working well beyond the age of 60. Then, many of those who reach the retirement age will probably opt to seek some form of re-employment. With respect to female baby boomers who are currently in their late 50s in particular, some 40% have already left the labor market.

To get a rough estimate of the baby boomers' retirement from the labor market, we could look at the labor participation rate data for 2004. For men, the participation rate was 93% for ages 55 to 59, falling roughly 20% to 71% for ages 60 to 64, and then declining a further 20% to 46% for ages 65 to 69. For women, the rate was 60% for ages 55 to 59, falling to 40% for ages 60 to 64, and then down to 24% for ages 65 to 69. Even though the data is given in five-year increments, and yearly estimates are impossible to make, we can expect, assuming that the baby boomers' behavior mirrors the labor participation rates described above, that their retirement will have a tremendous impact on Japan's labor market from 2007 through 2014. The impact on companies will be the greatest when the baby boomers retire in droves between 2007 and 2009,

but in terms of departure from the labor market, the impact will likely be prolonged to 2012-2014 when the boomers reach the age of 65.

Well then, how big of a labor market exodus will this be? To begin with, let's assume that the labor participation rates for 2004 remain constant. Of course, this is never the case in real life, as the rates will rise whenever the labor market gets tight or changes in the eligibility age for pensions prompt workers to prolong their employment. In any event, assuming the labor participation rates are constant, Japan's labor force in 2010 will be 1.78 million lower than in 2004 due to the retirement of the baby boomers between 2007 and 2009 (as well as the retirement of the preceding generation). Even if businesses do not completely replenish such losses, assuming employment remains constant at 2004 levels (i.e., businesses replenish their losses by hiring jobless workers), the ranks of the unemployed would shrink by 1.78 million. Since the jobless total in 2004 was 3.13 million, the total of unemployed would fall to 1.35 million, and the jobless rate would decline from 4.7% to only 2.1%. (NB. The unemployment rate of 2.1% equals the jobless rate during the bubble economy in 1990-1991, which could be construed as full employment. The Japanese economy will be suffering from a severe labor shortage.) Then when the baby boomers reach 65 during 2012-2014, Japan's labor force in 2015 will fall a further 1.99 million from the 2010 levels.

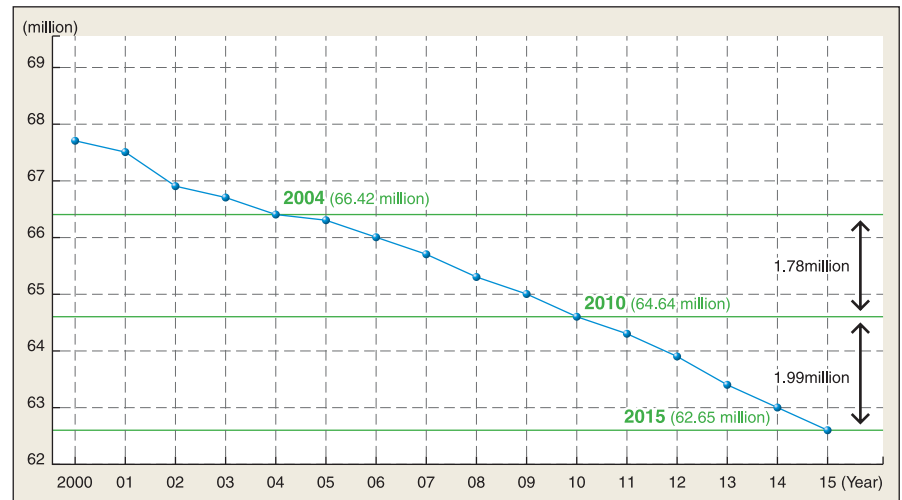
Although our projections are very mechanical, we can get an idea of just how rapidly Japan's labor market will tighten. Of course, not all of the job vacancies will need to be filled, as improved productivity can also compensate for some degree of labor deficiency. Once the labor supply becomes tight, real wages will gradually pick up, resulting in higher labor participation rates for other age groups.

MEANWHILE, since passing on skills has become such an urgent issue for many manufacturers, businesses faced with a labor shortage will probably come to realize the advantages of retaining senior workers who have reached the retirement age of 60. When the labor market clearly gets tight and businesses come to see the difficulty of hiring skilled outsiders, managers will probably realize that re-hiring retirees at substantially reduced wage rates is actually a very wise strategy to retain the valuable firm-specific skills and know-how of veteran workers. As a result, the labor participation rate for the 60-65 age group will likely rise.

What is more, the number of companies fully utilizing their female employees will naturally increase. Until now, the aggressive employment of women has been more rhetoric than reality, but once short-handedness becomes the norm for corporate Japan, companies will find themselves pressed to actively make the most of their human resources regardless of gender so as not only to prevent top-caliber staff members from being head-hunted by rival firms but also to be able to attract and secure outside talent as needed. This will greatly improve the way female workers are treated at the company level, something that will raise women's labor participation rate in the overall economy. Another trend likely to gain more popular support is tolerance for immigrant labor.

With these market mechanisms acting to raise labor participation rates, Japan's labor market might not get as tight as our estimates suggest. From a long-term perspective, we can expect that the demand for labor will decline alongside the diminishing labor supply. If real wages start to soar, businesses can always cope by switching production methods to relatively cheaper capital stock. In any event, although the unemployment rate in Japan today is still rather substantial, even with the steady improvements in employment and the declining number of jobless workers, it will not be long before

Figure 1 Changes in Japan's Labor Force (Both Genders)



Sources : MIC, National Institute of Population and Social Security Research, BNP PARIBAS

things change completely and Japan abruptly starts to become a labor deficient society from 2007.

THE retirement of the baby boomers will also have a tremendous impact on Japan's IS (investment and savings) balance, as the savings rate is sure to fall because the retired baby boomers will generally maintain a comparable level of spending but without the same income. Japan's savings rate has long been ranked first or second among the developed nations, but it has recently shown marked declines. After rising to 17.3% in 1980, Japan's household savings rate (93SNA basis) began a downward trek, slipping to 13.9% in 1990, then falling below 10% in 2000 and continuing down to 7.4% in 2003. The rapid aging of society is certainly one of the main factors depressing the savings rate. According to the life-cycle theory of consumption and savings, people save part of the income earned during their working years in order to finance their post-retirement consumption. If so, the savings rate for the overall household sector should naturally fall as the ratio of retirees in the population rises. Japan's population until the 1970s was relatively young, but since the 1990s aging has steadily accelerated, resulting in ever-growing numbers of people who must

tap into their accumulated savings (i.e., retirees). It was once said that Japan's high savings rate was due to the national character that valued hard work and frugality, so many dismissed the life-cycle theory as being inapplicable to Japan, but as recent trends show, Japan's savings rate is following a course that fully accords with this theory.

Looking ahead, we can expect the deceleration of Japan's saving rate will pick up during 2007-2009 when the baby boomers turn 60 years old and start retiring, and this rate of decline will further accelerate in 2012-2014 when they become 65 years old, the time of final retirement for most people. How low the savings rate will fall at that time is not clear (some say zero or lower), but what is certain is that the issue of how Japan should absorb the household sector's excess savings – a nagging question for more than 30 years since the end of Japan's rapid growth – will no longer be a problem. Thus, the retirement of the baby boomer generation will usher in a totally new macroeconomic situation for Japan in terms of the IS balance and the labor supply. **JS**

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