

This PDF is a selection from an out-of-print volume from
the National Bureau of Economic Research

Volume Title: Fiscal Policy and Management in East Asia,
NBER-EASE, Volume 16

Volume Author/Editor: Takatoshi Ito and Andrew K. Rose,
editors

Volume Publisher: University of Chicago Press

Volume ISBN: 978-0-226-38681-2

Volume URL: http://www.nber.org/books/ito_07-1

Conference Date: June 23-25, 2005

Publication Date: October 2007

Title: Comment on "Population Aging, Fiscal Policies, and
National Saving: Predictions for the Korean Economy"

Author: Shigeki Kunieda

URL: <http://www.nber.org/chapters/c0902>

Korea's saving by properly treating the country as a small open economy. It considers each cohort's remaining lifetime resources in each future year and multiplies those resources by the cohort's propensity to consume. Since older cohorts have higher consumption propensities, a shift toward an older population leads to more aggregate consumption and lower national saving, other things equal. Korea is slated to age very dramatically. Indeed, by the end of this century, Korea could be the oldest country in the world. The authors suggest a very dramatic decline, indeed a true collapse, in the country's national saving rate, albeit one that can be mitigated to some degree with more generationally responsible fiscal policy. This is a very carefully done study and should serve as a model for future analyses of national saving.

Comment Shigeki Kunieda

The Chun chapter analyzes the effects of aging and fiscal policy on the national savings in Korea using a life-cycle model. Despite the seemingly sound current Korean fiscal situation, this chapter and another paper by the author and Auerbach (Auerbach and Chun 2006) show that rapid aging will have significant effects on national savings and intergenerational equity in Korea in the near future. Especially, the maturation of PAYGO public pension system and the expansion of medical expense will reduce the national savings significantly. In addition, the chapter points out possible negative effects of annuitization of wealth. I would like to raise three issues that might be relevant for the future analysis and the Korean fiscal policy reform.

Desirability of Dynamic General Equilibrium Analysis

As Chun admits in the chapter, the analysis in it is partial equilibrium analysis, since wage rate and discount rate are exogenously determined. In order to include possible effects of factor price changes, dynamic general equilibrium analysis such as Auerbach-Kotlikoff's model is desirable for further research.

Bequest Motives and the Effects of Annuitization

Chun argues that the annuitization of wealth will reduce national savings further in Korea. However, the claim that annuitization of wealth, especially introduction of reverse mortgage, will reduce savings crucially de-

depends on the assumption of no or weak bequest motives. For example, if pure altruistic bequest motive is the most important bequest motive, reverse mortgage business cannot attract a large number of customers since the real estate under reverse mortgage contract cannot be left to children. In fact, the recent Annual Report on Japanese Economy and Public Finance (2005) points out that the most important reason why Japanese people do not have reverse mortgages is their desire to leave their real estate as bequest. Thus, I believe that a more detailed study about the most important bequest motives in Korea is desired in order to discuss the possible effects of annuitization of wealth in Korea in a more realistic setting.

Constitutional Rule of Intergenerational Equity

According to the results in this chapter, immediate drastic policy reforms such as tax increase and pension benefit cut are urgent in order to prevent the negative effects of aging in Korea. However, politicians in most democratic countries tend to postpone necessary reforms even when coming “intergenerational exploitation” is clearly predicted. Thus, after realizing the necessity of drastic policy reforms, we should also discuss how to make politicians take necessary policy actions to avoid “intergenerational exploitation” in the real world. One repeatedly proposed remedy is the constitutional constraint on budget deficit such as the balanced budget rule. However, this chapter’s result, that the current Korean fiscal situation seems apparently sound even when coming intergenerational inequity is expected, implies that the constitutional constraint on budget deficit may be ineffective for securing intergenerational equity.

In the case of Japan, who is facing the similar political difficulty, I (Kunieda 2004) propose the constitutional rule of intergenerational equity instead of balanced budget rule. If securing intergenerational equity is defined as the constitutional responsibility, politicians cannot postpone politically unpopular, but necessary policy reforms for securing intergenerational equity. However, in political reality, it may be very difficult to amend the existing constitution in order to add a new constitutional article of intergenerational equity rule. Still, if we can establish a new constitutional interpretation claiming that serious intergenerational fiscal inequity is not allowed even under the currently existing constitution, then we can force politicians to take necessary actions to recover intergenerational equity. I believe that it is possible to establish such constitutional interpretation under the current Constitution of Japan. If the constitutional interpretation is widely accepted, we should clarify the government responsibility of securing intergenerational equity by introducing the new “Fundamental Law of Securing Intergenerational Equity,” and establish an independent government agency for securing intergenerational equity. The agency calculates and submits the generational accounts annually, and

recommends necessary reforms to avoid constitutionally unaccepted intergenerational inequity. While my proposal is based on the current Japanese fiscal and political situation, it may also contribute to prevent “intergenerational exploitation” in Korea.

In conclusion, after reading the Chun chapter, Korean policymakers are strongly expected to start serious discussions of policy alternatives for preventing intergeneration inequity immediately.

References

- Auerbach, A. J., and Y. J. Chun. 2006. Generational accounting in Korea. *Journal of Japanese and International Economy* 20 (2): 234–68.
- Cabinet Office of Government of Japan. 2005. *Annual report on Japanese economy and public finance*. [in Japanese]. Tokyo: Cabinet Office Government of Japan.
- Kunieda, S. 2004. Fukouhei Zesei he Kihonhou Seitei (New Fundamental Law for Securing Intergenerational Equity). *Nihon Keizai Shinbun*. [in Japanese]. October 8, 2004.