

Demography and national debt: At what point is it “toxic”?

The most recent peak of the financial crisis, concerning the debt crisis in the EU states, has shown that borrowing is always dependent on the confidence of investors or rather, the outlook of speculators. As soon as their confidence in the security of debt repayment dwindles, funding sources quickly dry out and hefty risk premiums follow. Until now, the assumption has stood that national governments would always cover the outstanding debt in the system. But suddenly this basic trust is shattered. Now it is no longer clear whether or how countries, for example Greece, can reduce their deficits and their mountain of debt in the medium term.

The "if" and "how" of the debt problems have, until now, not addressed looming demographic changes including longer life expectancy, fewer workers, and continued low fertility rates. At the latest, by 2020, this will no longer be a scenario for many OECD countries, but rather the reality.

The level of debt a country can afford is largely determined by the growth and production potentials of its economy. Economic productivity, in turn, depends heavily on demographic development, specifically the following two key indicators:

- how large the work force is relative to the total population and
- how productive the work force is overall

Aging, health, and the retiring baby boomers generation will, in the coming years, cause dramatic shifts which will not necessarily be "deficit-friendly". On the contrary, the financial burden on the state will dramatically and inevitably grow as a result of increased demands on the social insurance systems from healthcare and pension payments, in conjunction with shrinking labor forces.

Take the current crisis-related deficits and add to that the increasingly demographically induced structural deficits in the future, and we come quickly to debt scenarios in which many OECD countries are suddenly very poorly positioned.

But which countries are we considering, and how are political systems reacting to this "bitter pill"? Regardless of how accurate these estimates are today, the demographic "structural problems" are already too deeply set, and will inevitably be reflected in future state finances. Soon the point will come, when the public starts to concern themselves with the following two questions: At what point do structural deficits become unsustainable? When will the debt become so high that any measures have no influence?

The attempt to null and void all state debt would have disastrous consequences: a "reset" of the financial systems would leave no stone unturned. The resulting scenario would likely include a collapse of the monetary system, economic order, and thus the state system (with all its consequences).

The necessary response is to take a visionary approach to demographics. Every state has to understand its own future demographic in order to be able to adapt quickly and accordingly its social and solidarity systems to the capability of its economy to create wealth.

Countries and economies that are particularly innovative and assertive in the activation of new productivity potentials will emerge as victors from the debt and confidence crisis.