

## FOREWORD

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Cathy E. Minehan

This year's conference topic, "Seismic Shifts: The Economic Impact of Demographic Change," at first glance may seem of less than immediate relevance to the Federal Reserve System. As a central bank, we usually focus on developments that take place in the short and medium run and directly affect our role in conducting monetary policy or supervising banking and financial institutions. But the ultimate goal of the Federal Reserve System is to provide an economic and financial environment that is conducive to economic growth and rising living standards. It is important that we occasionally take a step back and look at longer-range developments that have broad economic impacts. This year's conference topic definitely falls in that category.

Demographic and economic forces are closely intertwined, although economists often take demographic variables as givens or ignore them altogether. And demographic trends seem likely to restructure the global economy fundamentally over the next half century. In coming decades, low fertility rates will result in slow growth, in many cases actual declines, in the native-born working-age population across the developed world. This trend, combined with increases in life expectancy, will result in a substantial rise in the ratio of retired workers to those still working. In many ways, these demographic trends are to be welcomed. Increased life expectancy, with its gift of several more years of active life, is unambiguously good news. And decreased fertility has come by choice, as enhanced labor market opportunities and improved birth control have led many couples to opt for smaller families. Still, many policymakers worry about how living standards will be affected as each worker has to provide for the consumption needs of a growing number of elderly dependents. It is certainly not a foregone conclusion that the aging of the population will have negative consequences for living standards. But it is

important for us to better understand this phenomenon so that appropriate policy adjustments can be made.

While many developing countries will also experience aging of their populations, population growth will generally be more rapid there than in more developed countries. A substantial shift in the distribution of the world's population will result. Because developed countries will have largely stable labor forces, their need for new investment will be modest relative to that of developing countries, whose more rapidly expanding labor forces will need to be equipped with capital goods. If developing countries are not able to attract this capital, then increases in global inequality may well follow.

Migration will undoubtedly be another important phenomenon in coming decades. Slow labor force growth in developed countries will likely exert upward pressure on wages at the same time that population crowding negatively affects many developing countries. The result is likely to be increased migration, with important consequences for both source and destination countries. Depending on the education levels of the migrants, this flow may result in a "brain drain" from source countries and boost economic growth in destination countries, or it may alleviate both surpluses of low-wage labor in the source countries and shortages of less-educated labor in the destination countries while aggravating income inequality within the destination countries.

Although many of the effects of demographic change will influence central banks here and elsewhere only in the long run, some demographic developments may already be having an impact. The ability of the U.S. economy to sustain both low inflation and low rates of unemployment in recent years probably has been due at least in part to the aging of the labor force. Older workers are less likely to be entering the labor force for the first time or switching jobs, and they are less likely to suffer spells of unemployment when they do switch. The acceleration of labor productivity growth in the late '90s may also be partly attributable to demographic forces. A slowly growing labor force creates incentives for firms to implement labor-saving production techniques, leading to faster productivity growth.

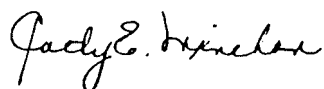
A key element of how developed countries adapt to the aging of their populations will likely be a better utilization of their human resources. Work-life policies that facilitate the continued contributions of older workers are one way in which employers may respond to labor shortages. Nontraditional schedules and telecommuting options may make work effort by the younger elderly more attractive than it has been in the past. As a result, the sharp demarcation between working and retirement may give way to workers gradually reducing the amount of time they spend at work as they grow older. At the Boston Fed, we have seen many examples of how valuable the contributions of older individuals can be. Eddie McCarthy, a long-time Bank employee, was a source of wisdom

and insight into his mid eighties. And Paul Samuelson and Franco Modigliani are vibrant contributors to our Academic Advisory Council at ages well past those when most people retire.

The need to use human resources effectively extends beyond encouraging labor force participation by the elderly. At the Federal Reserve Bank of Boston, we have found success in retaining employees who have experienced increased family responsibilities, such as the need to care for young children, by allowing schedules to be adapted to employees' personal needs. We believe that it is also important to encourage people to acquire the skills needed to succeed at work. Older adults must continually renew their skills in order to maintain their viability in the labor market. And entry-level workers, who increasingly will come from groups that historically have had below-average levels of educational attainment, must have access to the skills needed for successful careers. At the Bank, we offer extensive training opportunities to our staff, and we are also involved in promoting education and skills development in the wider community through our involvement with the Boston Private Industry Council.

This conference brought together a distinguished group of presenters, commentators, and panelists whose global reach matched the scope of the conference topic. The result was lively and insightful discussion that provided us with more informed perspectives on the coming demographic shocks, a better understanding of their economic consequences, and some fresh ideas regarding possible policy responses.

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A handwritten signature in cursive script that reads "Cathy E. Minehan".

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