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The cost of growing old frugally

By Merryn Somerset Webb

Are you an average FT Weekend reader (aged about 44)? Have you noticed that your parents spend rather less money than you do? If so, it is possible that you have more of an insight into the growth patterns of the UK than all the City's economists put together.

It is increasingly clear that trend GDP growth rates are strongly influenced by how many people of any particular age live in any one country. In the UK, for example, we tend to think that constant growth at 2-4 per cent is normal simply because, for as long as we can remember, any dip has been followed by quick recovery.

But look at our demographic profile and you get a glimpse of a very different future. According to figures from Paul Hodges at consultancy International eChem, births in the UK rose 15 per cent between 1946 and 1970 compared with the previous twenty-five years. This gave us an extra 3m babies (the current population of Wales). That was nice for families but it was also brilliant for the economy.

Those babies grew up to create what Hodges calls the "growth supercycle" of 1982 to 2007: the period in which they reached their peak spending age range (46 is the average top spending age) and the one in which the credit markets developed to make sure they had the cash to make the most of it.

In the early part of peak spending – say 25-39 – people tend to work hard and productively and to invest in housing. As they hit 40 they become slightly less productive and move on to investing any surplus in bonds and equities. At 65 they stop work, cut consumption and downsize both their housing and stocks. It makes sense that when we have large groups of the young we should see rises in asset prices and GDP – this makes particular sense if you think of GDP as being the number of workers times the productivity of those workers.

The problem now? That despite my generation of working mothers doing our best to keep things going we don't have large groups of the young these days. Births between 1971 and 2000 were 17 per cent lower. The result is that over-55s are now the only growth cohort in the UK. That might be good for travel agents – recreation is the only area of major household spend that rises post 50. But it isn't going to help us with the GDP equation.

Worse, our Boomers are uncomfortably aware that the savings they have entrusted to the state and financial industry might not have been husbanded carefully enough to provide the retirement they want. So they might even spend less than the historical average for their group.

Anyone who thinks demographics is irrelevant nonsense might glance to Japan. It experienced a baby boom slightly earlier than we did, says Hodges. Japan's Boomers hit the peak wealth creating age between 1977 and 1994. The Nikkei peaked in 1989 with government bond yields at 8 per cent and growth at 4 per cent. It has been around 1 per cent since – regardless of the government's stimulus efforts.

The implications, said the governor of the Bank of Japan earlier this year, are "profound." There will be "differences in timing and magnitude" but eventually all developed countries should expect "a decline in growth potential, a deterioration of the fiscal balance and a fall in housing prices." Hmm. Look around you. See any of that?