

Demographics, Inflation, Immigration, Capital, and Social Harmony

Aging populations are associated with lower levels of inflation. According to James Bullard's November 2012 article in Federal Reserve Bank of St. Louis *Review*, workers like inflation when they are young, but dislike it when they are old. An optimal level of capital exists for every social distribution. When the young have more influence, wages are high and the return from capital is low; when the old have more influence, this is reversed.

So it is that **the drop in fertility rates in the wealthy countries for the last several decades has been a powerful depressant on inflation and interest rates**, a force which seems to elude some of those seeking to explain or influence inflation expectations. Bond yields are low, even in countries without a Fed to talk them down, with real policy rates projected to be negative for years in Japan, Britain, and the Eurozone. Despite profit margins near record levels and rock-bottom interest rates, business investment has been sluggish and productivity growth has slowed to 1% since the recovery began, half its long-run average. This may be partially due to related, weak upward pressure on labor costs. In addition to weak investment, a global savings glut also presses down on natural long-term interest rates. Bernanke has credited a global saving glut originating in China and other emerging markets with holding down long-term interest rates. Although China's current-account surplus has shrunk in the past 5 years, Goldman Sachs reckons that the proportion of emerging-market populations in their prime saving years (aged 35-69) is climbing, and won't peak until 2032.

When central banks adopted "quantitative easing" (printing money to buy financial assets) policies several years ago, many feared runaway inflation. Asset prices have certainly soared. But consumer prices have not. Indeed the growing fear is that rich countries may be entering a twilight zone of ultra-low inflation or worse. Eurozone inflation has fallen to 0.7%, the lowest ever for the unified currency, raising fears about the prospect of deflation. If an economy with high unemployment grows too slowly for too long, prices and wages may start to fall. The immense difficulty that successive Japanese governments have encountered in trying to escape deflation serves as a warning of the danger of letting inflation fall too low. Workers tend to resist nominal cuts in pay more fiercely than the subtler erosion of their income through inflation, and debt becomes more onerous in real terms.

The aging population in the rich world is testament to the best birth control device in the world--money. With increased wealth and a universal desire to launch their children into life,

the exploding cost of raising and educating children has depressed birth rates throughout wealthy nations to much less than the self-sustaining rate of 2.2 births per household. Those experiencing the most spectacular wealth gains and academic achievement are most at risk of depopulation, with Korea and Japan now experiencing 1.3 births per household. Their only viable alternative to a sustained slide in economic health is **more immigration**. This will be an increasing pressure and unpopular cultural change to those countries most resistant to it--and in need of it. Both legal and illegal migrants are often entrepreneurs, not victims, as they bring their human capital with them. History shows that **urban areas receiving the most immigration are among the best positioned for success in the generations that follow, i.e. Geneva, London, New York, Hong Kong, Singapore.**

These combined and related forces are also increasing the gap between rich and poor in America. Scholars have said that changes in marriage patterns — as opposed to changes in individual earnings — may account for as much as 40% of the growth in inequality. Long a nation of economic extremes, the US is also becoming a society of family haves and family have-nots, with marriage and its rewards evermore confined to the fortunate classes. "It is the privileged Americans who are marrying, and marrying helps them stay privileged," said Andrew Cherlin, a sociologist at Johns Hopkins University. About 41% of births in the US occur outside marriage, up sharply from 17% three decades ago. But equally sharp are the educational divides, according to an analysis by Child Trends, a Washington research group. Less than 10% of the births to college-educated women occur outside marriage, while for women with high school degrees or less, the figure is nearly 60%. Long concentrated among minorities, motherhood outside marriage now varies by class about as much as by race.

Compounding the **class and income gap** are forces that increase the strength of **capital** in the historic "capital v labor" trade-off. During the 20th century factories grouped workers together, allowing them to organize and improve their conditions by holding fixed assets of heavy industries hostage to their demands. But now the internet seems to be atomizing the workforce, shifting control to owners of capital. Cheaper and more powerful equipment in robotics and computing has allowed firms to automate an ever larger array of tasks. The cost of investment goods, relative to consumption goods, has dropped 25% over the past 35 years, contributing to a 5% decline in the labor share of the economy. Corporate profits are now at a post WW2 high as a share of American GDP.

All of this brightens the outlook for the global economic future, while clouding it for social harmony.