

Rejoinder to Jan Pen's Comment

by

Hans-Werner Sinn

August 2005

Published in: De Economist, Volume 153, No. 4, December 2005, pp. 479-482

I took note of the fact that a Dutch author, who informs us that he is 84 years of age, mentions my German nationality four times in his short comment. Yes, I understand why Jan Pen is carried away by emotions. However, the misuse of population theories in the past cannot prevent Europeans of today from being concerned about a problem that more than anything else will give rise to fundamental frictions in their societies, destroy the dynamism of their economies and create extremely difficult fiscal problems. I felt young enough to free myself from the taboos of Jan Pen's generation when I presented my views in the Tinbergen lecture.

Jan Pen is moralising when he speaks of breeding premiums, not I. My article is not based on moral arguments of the kind he claims. On the contrary, the central argument is purely allocative. There are too few children because the paygo system expropriates parents from the fruits of their human capital investment. I even gave numbers on the size of the fiscal externality. Such expropriation can be defended as insurance against not being able to have children. However, every type of insurance has moral hazard effects, and the moral hazard effect in the case at hand is that more and more people rely on other people's children when old and collecting their paygo pensions instead of raising their own children. The moral hazard effect is not a moral

problem in the ordinary sense of the word. It is a technical term indicating a special type of welfare loss resulting from excessive insurance. To reduce the moral hazard effect I recommended curtailing the degree of insurance coverage in the paygo system. This is genuine economic reasoning, with very little value judgement. I am not moralising when I speak of moral hazard effects, despite the semantic similarities of these terms.

The child pension system I outlined helps to effectively reduce the amount of insurance coverage. The existing paygo pension systems should be converted from defined benefit to defined contribution systems with correspondingly meagre pensions when the lack of children will have doubled the old age dependency ratio in the 2030s. To prop up the pensions, only parents, not everyone, should get extra paygo pensions from their children, and the childless should have to save for an extra pension instead. Relative to the defined benefit systems that many European countries have, this effectively reduces the amount of redistribution from families with children to those without and limits the fiscal externality.

For reasons I explained, I find curtailing the primary state intervention carried out by the paygo system better than introducing countervailing secondary interventions such as taxes on the childless and child allowances. Countervailing secondary interventions typically have bad side effects that were not intended. Thus it is better to curtail the primary interventions instead.

I was aghast when I read how Jan Pen represents my views. He neither spends a word on my basic argument for why there are not enough children nor on the child pension system which is my basic policy recommendation. Instead he writes:

“The article culminates in the recommendation to boost the birth rate through financial stimuli, such as taxes on childless households – a new idea supported by the argument

that childless couples have lower outlays. Another proposal is for generous child allowances which increase progressively as more children are born to the family. If one wishes to be unkind, these could be called breeding premiums, ...”

This is a bizarre distortion, because these kinds of policy measures are exactly those that I (in section 6.1) declare inferior to the child pension system I propose because they are countervailing secondary interventions. I am afraid that I did not succeed in making my argument understood to Jan Pen and can only offer him my willingness to clarify the point in a personal conversation.

That being said, I share Jan Pen's concern for environmental problems resulting from uncontrolled population growth in the Third World. This is a serious issue that needs to be addressed. I understand why Jan Tinbergen was alarmed.

However, Europe does not belong to that part of the world. It does not have a problem of uncontrolled population growth but one of uncontrolled shrinkage, and I doubt that Europeans find relief in the statement that their shrinkage is balanced by the growth of other populations.

Moreover, when it comes to Europe, the allocative argument is not as simple as Jan Pen puts it. Pointing out that there are 373 people per square kilometre in The Netherlands and 222 in Germany is no valid argument. I could counter with the statement that there can hardly be overcrowding in Germany when only 5% of the country's surface is covered by man-made objects. From an economic perspective, such arguments lead nowhere since they lack a welfare base in terms of externalities, public goods and so on.

As long as land is privately owned rather than a common property resource there are no externalities from land use as such, and it cannot be expected that people's

individual fertility choices are distorted. A newly born child will have to buy the land it wants to use when adult, and the land that is given to him by his parents is not an externality either.

To the extent that there are common property resources, things are different of course. Free access to such a resource involves negative externalities of fertility decisions that imply excessive birth rates, a point already made by Malthus (1803, book II, p. 16) when he spoke about excessive population growth in seafaring nations. However, how important is this effect in the Europe of today? The common pool problem in fishery has been reduced and fishery accounts for only 0.5 permille of GDP even in The Netherlands. Dikes and other pure public goods are not a problem since there is no rivalry in consumption and hence there are no negative externalities of births. Roads, bridges and other public facilities that involve congestion externalities may seem a problem at first glance, but they have to be financed and maintained. By and large, the taxes necessary to cover the expenses can be seen as appropriate entrance fees for new people that want to use them, so there is no obvious externality either that could distort the fertility decision. (Note that even head taxes would impose a marginal tax burden when it comes to fertility choices.)

What remains is the natural environment, and here Jan Pen may have a point. However, Europe has already very intensive environmental regulation that largely avoids marginal externalities. Take the new system of CO₂ licenses for example. A country will not receive more licenses simply because more people are born. Thus a new person entering society by birth will have to pay for the additional environmental resources he or she uses.

All in all, I therefore fail to see a noteworthy negative externality that an additional child would place on society such that the assumption of excessive private fertility incentives could be justified. The decisive externality remains the one via the paygo pension system and other publicly organised intergenerational transfer systems such as public debt, tax relief for the elderly or public health insurance. It implies that there are not enough children if people optimise their private fertility plans. This externality is the justification for corrective policy actions.

To conclude, let me say that I read with interest what Jan Pen said about Tinbergen and his personal relationship with him. Jan Pen confirms, however, that Jan Tinbergen has not written on the subject of population growth, and this is what I stated in my introduction after having consulted the literature and a number of Dutch scholars. Unfortunately, I cannot make a contribution to the question of what Tinbergen would have said had he written on the subject. Here Jan Pen is indeed the expert. I am happy to admit that.

Reference

Thomas R. Malthus (1803), *An Essay on the Principle of Population*, reprint of the sixth (1826) and second (1803) editions, William Pickering: London, 1986.