The Baby Boomers' Fiscal Policy Influence and Welfare

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Abstract

Did the baby boomers leverage their demographic and, hence, political clout to shape fiscal policy? If so, did this yield them higher welfare relative to other generations? I integrate electoral competition into an overlapping generations model to obtain fiscal choices that are consistent with empirical patterns: 1) when baby boomers are in the labor force, they benefit from low labor income tax rates and impose high capital tax rates on the elderly; 2) they support high education spending for their offspring, to ensure a larger future tax base from which old-age benefits can be funded during their retirement, and 3) when retired, boomers reap old-age transfers and benefit from low capital tax rates. The large cohort size is a double-edged sword for baby boomers. Although they shape fiscal policy to their advantage over their life cycle, the sheer size of the generation dilutes per-student education spending, curtails human capital accumulation, and leaves them worse off than neighboring generations.

Keywords— Demographics; Government spending; Social security; Education spending; Intergenerational conflict; Political economy; Probabilistic voting; Markov perfect equilibrium