

Geriatric Deadbeats

Old folks may be less willing to repay sovereign debts

Ali Alich

AS THE NUMBER of older voters relative to younger ones increases around the globe, the creditworthiness of borrowing countries could decline—resulting in less external lending and more sovereign debt defaults.

Because lenders cannot easily confiscate a government's assets in the case of a default, they must rely almost completely on the creditworthiness of a sovereign in deciding whether to make a loan. To the many factors affecting a nation's creditworthiness—such as macroeconomic strength and past debt-payment record—lenders must add aging.

Studies have shown that a country's willingness to repay is as important as whether it has the resources to repay. This willingness deteriorates as voters age because they have a shorter period to benefit from their country's access to international capital markets and become more likely to opt for default on current debt. Moreover, older voters generally benefit more from public resources—such as pension and health care benefits—which could shrink if debt is repaid. If the old are a majority, they might force default, even if it is not optimal for the country as a whole. Lenders will take this into account and reduce new lending to an aging country.

There is some empirical support for the notion that aging increases the probability of default on sovereign debt, but more work is needed to draw strong conclusions. Alich (2008) uses a panel of about 75 countries that have had at least one episode of sovereign default during 1975–2003 and shows that, on average, younger countries (those with a higher percentage of people ages 15 to 59 years) are less likely to default.

Now if the old are altruistic and care about their children as much as themselves, they will not vote for default with its negative consequences for future generations. But Altonji, Hayashi, and Kotlikoff (1997) have shown that altruism does not hold at the overall level in the United States—although there are few studies of this sort for most other countries.

How can countries with aging populations improve their credit profile? They can collateralize more of their debt, using assets in the lending country or a third country; lower the external debt ceiling, which would reduce the incentive to default; or move toward a fully funded structure and reduce the dependence of social security and old-age health benefits on public resources.

They should do so as soon as possible—before their populations age! ■

Ali Alich is an Economist in the IMF's Asia and Pacific Department.

References:

Alich, Ali, 2008, "[*A Model of Sovereign Debt in Democracies*](#)," IMF Working Paper 08/152 (Washington: International Monetary Fund).

Altonji, Joseph G., Fumio Hayashi, and Laurence Kotlikoff, 1997, "Parental Altruism and Inter Vivos Transfers: Theory and Evidence," *Journal of Political Economy*, Vol. 105, No. 6, pp. 1121–66.