# To save capitalism we must help the young

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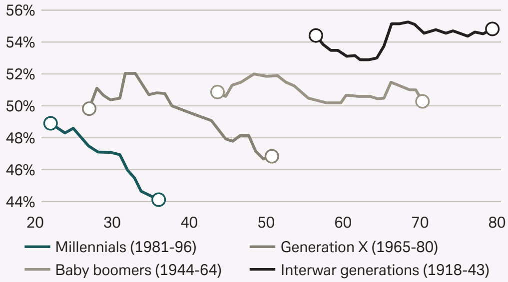
"If you're not liberal when you're 25, you have no heart. If you're not a conservative by the time you're 35, you have no brain".

This quote has been attributed to Winston Churchill and is a blunt way of saying that as people age, and acquire income and wealth, they have a higher propensity to want to protect it. Essentially, they become more absorbed in the capitalist and democratic model or, at least, become more tolerant of the system.

Yet, that is not the case with today's young people. They are the most dissatisfied with democracy of any generation born in the last 100 years. Covid has only made things worse as the economic crash has disproportionately hurt younger workers. They have been more likely to work in industries such as retail or hospitality where working from home isn't possible, job hunting has become impossible for graduates, and most have little in the way of savings.

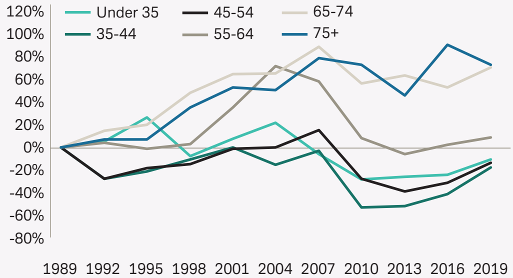
This problem will not go away after the pandemic recedes. The evidence shows that people who graduate in a recession see lower earnings than they otherwise would have for years after the recovery. That is an alarming prospect for young people given that the past 12 years have witnessed the two biggest economic shocks in almost a century.

### Satisfaction with democracy by age




Source: Centre for the Future of Democracy, University of Cambridge

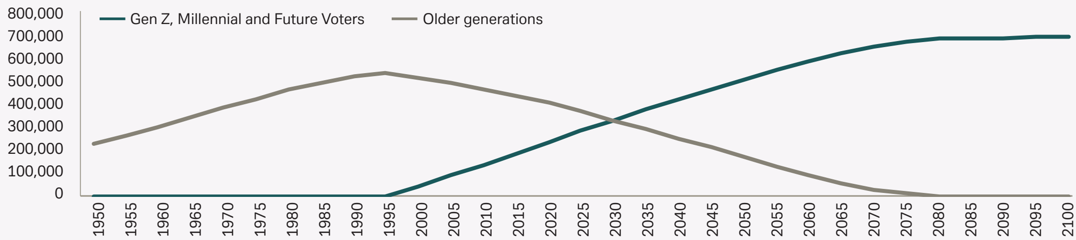
### Percentage change in US median family net worth by age of head of family




Source: Federal Reserve Board, Haver Analytics, Deutsche Bank

The covid crisis should be the catalyst that policymakers use to level up the generations. In fact, if we do not act now, there is a serious risk that over the coming decade, when the younger generation of voters begins to outnumber the older generation, a populist politician could corral the anger of the young. That could lead to sudden and seismic shifts in the established capitalist order.

### Millennials, Generation Z and younger cohorts will have nearly as many voters as those in older generations in the G7 by the end of this decade




Source: United Nations, Haver, Deutsche Bank. *Using midpoint of 15-20 age range to proxy voting age.

Of course, some may cheer a shake-up of capitalism. After all, the system is far from perfect. But it is the best system we know for human advancement. Over the last century, the spread of capitalism has coincided with life expectancy almost doubling after centuries of stagnation. Global poverty rates have collapsed and, over the last 40 years, global extreme poverty has fallen from 42 per cent to under 10 per cent. Child mortality has fallen from over 40 per cent in 1800 to under 5 per cent today. capitalist-driven economic growth has also coincided with decreasing inequality. From the second Industrial Revolution up until 1984, the share of wealth in the UK owned by the top one per cent fell from 70 per cent to 15 per cent.

The stalling and, in some areas, reversal of the decrease in inequality is one of the great problems of today. This phenomenon began in the 1980s and, thus, younger generations have been hit particularly hard while older folk have reaped the benefits.

In a liberal society, we should not over-engineer redistribution policies. They should incentivise work and the effective allocation of resources while providing an appropriate cushion to those who experience hard times. Yet, we must realise and accept the risk of a politician harnessing anger and upending capitalism such that it is detrimental to the lives of everyone in society. To reduce this risk, we must distribute to the young, even if it means cleaving away some of the assets of the old.

### The gains we should redistribute from the old to the young

So, what is a ‘fair’ way to redistribute? For starters, we should avoid a simple age-related tax. A blunt instrument makes no sense. Similarly, we must acknowledge that many older people have worked hard for the wealth they have acquired. So, in order to assess what wealth should be redistributed, we must first identify where the older generation has made gains through mere luck of timing and forces outside their control or expectations. The following is a list of five things that fit this criteria and have helped generate outsized gains.

*Low interest rates:* The ultra-low interest rates seen in recent years are the product of the authorities' attempt to prop up capitalism when it has over reached rather than allowing creative destruction. As such we artificially, and inadvertently, propped up the value of assets that the older generation are much more likely to own. Free markets would likely have now seen higher interest rates, less debt and lower asset prices.

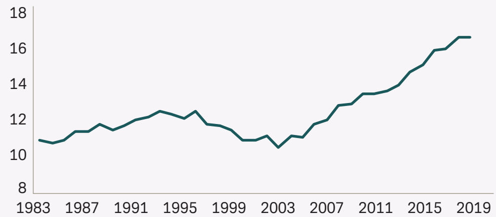
So given that much of the growth in this wealth has been an unintended side effect of this monetary stimulus, it could be argued that older people who happen to own assets are at an unfair advantage relative to the younger generation that is, and will likely continue to, struggle to muster the wealth to buy them.

Even if the concept of 'fair' is subjective, the inability of young people to afford houses is bad for the overall economy as it stalls economic engagement and family formation. The following charts show just how the problem has grown over the past two decades.

### Percentage of UK 25-year olds living with their parents


Source: ONS, Detusche Bank

### Percentage of US 25-34 year olds living with their parents



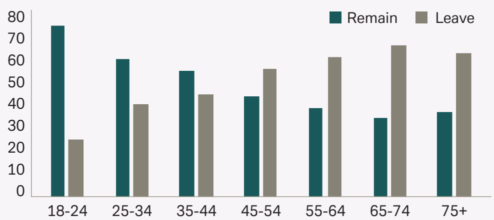

Source: Haver Analytics, Detusche Bank

*Urbanisation:* This is another factor that has inflated house prices, and its effects have been amplified by the inability of governments to encourage sufficient supply for newcomers. Over the last four decades, the proportion of the population who live in cities in the US has increased nine percentage points to 83 per cent. In the UK, it has increase six percentage points to 84 per cent, and in Germany four percentage points to 77 per cent. Excessive planning restrictions in many cities, combined with a lack of infrastructure investment in rural areas have combined to give a substantial boost to urban house prices.

*Pollution:* Harming the environment has been profitable for the companies in which the older generation invest. Cleaning up the mess will be costly for the young. It is true that overall carbon emissions in the US and many European countries have been falling for some years, however, a good chunk of these reduced emissions have merely been 'exported' along with manufacturing to China and other Asia countries. As the global consensus on green investment steadily builds, the cost of it will increasingly burden the young.

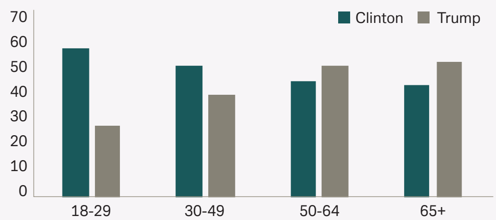
*Size of cohort:* The outsized weight of the baby boomer generation means they generally win the democratic process. This is illustrated by the following chart which shows the massive skew in age-based preferences for the Brexit referendum and the 2016 US presidential election. It is no wonder the young are disillusioned with democracy given their numbers make it impossible for them to win a vote.

### Brexit referendum vote by age




Source: Ipsos MORI, Deutsche Bank

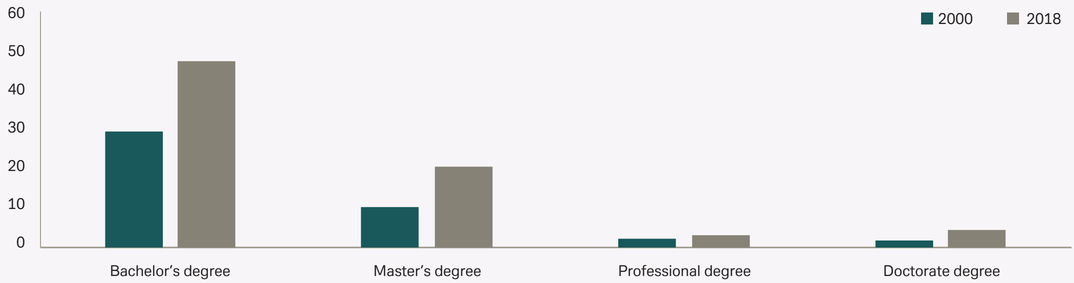
### US 2016 Presidential election vote by age




Source: "For Most Trump Voters, 'Very Warm' Feelings for Him Endured. Also: A detailed look at the 2016 electorate, based on voter records." Pew Research Center, Washington, D.C., August 9 2018

*Education:* Quite simply, the young have to pay far more for their education than the older generation. Not only that, but they increasingly require more education than their parents did to do the same jobs. In the US, over 13 per cent of Americans now have an advanced degree, well up from the nine per cent that had one in 2000. Young people's financial and time commitment to education, therefore, is far higher than that of their predecessors.

Number of degree holders: 2000 and 2018 (in millions)




Source: U.S. Census Bureau, Annual Social and Economic Supplement to the Current Population Survey, 2000 and 2018.

## Policies to consider

If we are to level the generational divide with regard to these five forces, there are several policies that should be considered. Some of these policies are more realistic than others, however, we will discuss some more radical and innovative ideas with a view to starting the conversation. Some of the policy ideas overlap so thus not all will be needed, however, they should form part of the conversation in how best to deal with a fair redistribution from the old to the young.

A tax on primary residence: Few countries employ such a measure, however, the extraordinary gains made on residential housing over the last few decades make a tax on them a necessity. And there are several ways to do this sensibly. First, a capital gains tax could be implemented. This could be enacted on houses above a certain value to avoid hitting lower-wealth groups, while acknowledging that richer, older groups have done doubly well from their house by virtue of the leverage involved. Fairness could be ensured by allowing house sellers to index the cost of their house to inflation. And if capital gains taxes on primary residences are not politically viable, then countries might consider a move to have sellers pay stamp duty rather than the current system in many countries where buyers pay and, for mortgage applicants, it is effectively an enormous tax on their deposit.

Additional taxes may also be needed on financial assets, such as stocks and bonds, due to their gains from loose monetary policy. This is particularly the case as the baby boomers begin to sell down non-pension assets into their retirement. Consider that in the 30 years to 2019, the S&P 500 gained over 800 per cent, two-thirds more than the return seen in the three decades before. A sizable portion of those gains have come from policy makers and their stimulus packages.

Of course, the details of a more appropriate capital gains tax system for financial assets is a complex country-by-country discussion. However, one technique that should be considered is to base the tax on unearned income. That will catch those who wait until they leave work, have a lower income, and then sell their assets in a drip-feed way that lowers their lifetime tax bill. Alternatively, countries can remove capital gains tax discounts for specific financial assets, such as stocks and bonds. Other countries can do away with flat rates and base the tax on the investor's marginal tax rate which can be higher than the flat capital gains tax rate. This will acknowledge that many older investors see their non-pension financial assets as future income.

A 'super tax' on stocks will also go some way to providing recompense for the gains these companies have made through pollution. This pollution may be direct or indirect but it is near impossible for any company to argue they have not benefited over the last four decades of globalisation from the ability of their supply chain to harm the environment in ways we now acknowledge should be cleaned up. This 'super tax' could help fund massive investment in climate change.

In the end, our desire for more tax to be generated from capital gains is derived from the idea that we should avoid much higher income taxes. These can be an invasion on hard work and, should they rise, there is a risk that work will be disincentivised.

Policies that level the playing field for urbanisation will be highly sensitive but if there is ever a time to discuss them, it is now. These can be achieved either through taxation, such as that described above, or through lowering house prices. Pushing for the latter may be desirable in areas where overly-restrictive planning policies have led to a dearth of house building and thus an extraordinary run-up in house prices. There are serious questions to be asked about the extent to which industrial parks are needed in cities.

The answer may be more centralised control of city planning. This is a dramatic step, and one that will be very controversial. But given the consistent failure of cities to build enough homes for its residents, it is hard to argue than anything other than a massive shake up of existing rules is needed. In fact, if this is not done now, it is likely that policies such as these will become some of the first to be implemented when the younger generation tips the voting scales. Consider that in Ireland this year, Sinn Féin saw a swell of support behind its housing policies which included the promise to build 100,000 new houses on public land.

Housing policies that focus on making land available can be better than ones that merely push developers to build quicker. The last thing cities need are cheap tower blocks being thrown up as quickly as possible. Experience from the 1950s and 1960s shows cities end up regretting these decisions. Rather, it is the availability of land that is the key thing. The construction will flow from there.

Finally, there is the issue of education and that young people are far more burdened by its cost, both time and money, compared with the older generations. Among the ideas that must be considered are dramatic government subsidies for higher education. Another idea is for countries in which university fees have grown quicker than have graduate salaries. The government could give new graduates a top-up grant for the first few years of their working life. This could be equivalent to, say, five or ten per cent of their salary and funded from the housing tax mentioned earlier.

Over time, this subsidy could be slowly rolled back until the market for graduates adjusts for the debt they carry. Grants could be increased for those with graduate degrees to compensate them for the additional time they have spent studying, and attempt to reduce the inevitable delay that will occur in their family formation – something desperately needed in an age of demographic decline.

If we do not recognise the increased time and financial debt of education, two things will happen. First, when young people come to power, blunt policies to write off debt or shake up university funding could be enacted as a knee-jerk reaction. Second, as baby boomers retire, and companies find there are not enough qualified people to take their place in the smaller generations, salaries for younger people could suddenly shoot up. This will violently upend business models. To soften this blow, it is preferable to either see salaries for young people rise gradually or to reduce the cost of their education.

The problem of the imbalance in the size of generations, and their effects on elections is a difficult one to mitigate. Our liberal democracies are based on the concept of one-person-one-vote. More powerful youth advisory councils may be an answer. Many countries and organisations already have these, including the Council of Europe, however, they must be given better access to power. Their meetings must be regularly chaired by the country's leader and their representatives should be given 'observer' or 'shadow' membership in parliaments and the right to participate in panels.

Even if some in the older generation wish to exercise their right to remain self-interested, they should still accept a simple fact. They wish to retire into an economy that supports their pension, healthcare, and wellbeing. Yet declining demographics means younger people will have to support an increasing number of older people. Thus, the older generation is entirely reliant on the goodwill of young people, the fruits of their education, and their willingness to form larger families.

Currently, that goodwill does not exist. If we do not enact substantial change now, then a generation of young people will soon take power. When they do, all indications are that they will enact policies that not only forcibly redistribute in blunt ways, but also upend the very foundations of capitalism. This will be a detriment to everyone. It would be a great shame if the older generation realises too late that its size – the source of all its power over the last four decades – has become its biggest liability.