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## YOUNG AND OLD COMPETING FOR PUBLIC WELFARE SERVICES

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## **Young and old competing for public welfare services**

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### **Abstract**

Generational conflict affects the supply of public welfare services, and the rising share of elderly is seen as a threat to educational spending. We offer an analysis of spending in child care, primary and lower secondary education, and care for the elderly related to the size of young and old voters. The age groups face possible disadvantages of being part of a large cohort, but also can gain political strength to crowd out services for the other groups. The decentralization of public services in Scandinavia allows for the simultaneous analysis of age related services. Using panel data from Denmark for the period 1989-1996, we find that the elderly are reducing spending in child care and education, but the young do not threaten services for the elderly. It is a disadvantage for both the elderly and the young to be part of a large cohort. The possible Tiebout-bias is handled with instrument variables predicting the relevant age composition variables.

JEL codes: H42, H72

Keywords: Public welfare services, group size, age composition of the population, generational conflict

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## 1. Introduction

Voter groups compete for shares of the public budget, and recently the focus has been set to the conflict between age groups in educational spending. The rising share of elderly voters is seen as a threat to educational spending. Poterba (1997, 1998) analyzes the negative correlation between the share of elderly and educational spending across US states. Fernandez and Rogerson (1997) report similar results, while the relationship is challenged by Ladd and Murray (2001). Harris et al. (2001) confirm that a growing share of elderly tends to depress spending in education analyzed at the school district level. Similar results are reported in European studies such as Borge and Rattsø (1995) for Norway and Grob and Wolter (2005) for Switzerland. Most of this literature links elderly voters to spending for schools. We extend this evidence to analyze the determination of child care, primary and lower secondary education, and care for the elderly taking into account both young and old. The decentralization of services for the young and the old in the Scandinavian welfare states, here Denmark, allows for the simultaneous analysis of several age groups and services.

Welfare states are first and for all about redistribution over time to finance public welfare services. In the short run this redistribution implies a conflict between generations. Public welfare services are redistributive and each of them has a client group typically defined by age. In the literature, these services are described as ‘concentrated benefits’, ‘directed spending’ and ‘particularistic goods’. The services can be understood in terms of congestion. With full crowding, the publicly provided services are private goods, and the degree of crowding is an empirical issue.

In the Scandinavian welfare states, the relevant public services are decentralized to local governments. The allocation of public welfare services between age groups is determined in the context of a local democracy. This is a challenge to the standard Musgrave-Oates-Tiebout model of local public finance assuming local public goods and benefit taxation. An understanding of the generational conflict must take into account the role of different voter age groups in the allocation of redistributive services.

Across the Scandinavian countries, the public debate has signaled worry about the provision

of public services to the growing number of elderly. Large cohorts now enter age groups with high demand for public care. Resources to expand services for the elderly must be financed by higher taxes or reallocation from age groups in decline. The resistance to higher taxes and conflicting claims from other groups may imply that the elderly lose out. They may experience the disadvantage of being many. Borge and Rattsø (1995) address this concern in an early study of Norway, and they find a clear negative effect of age group size on spending per client. Lotz and Aagesen (1997) offer a number of partial analyses of the relationship between size of age groups, measures of service output, and spending per client for Denmark. In this paper we integrate the partial relationships between age group size and spending in a full demand model of public welfare services. Strömberg (1998) separates between demand and political influence of the elderly in neighboring Sweden. He finds that a rising share of elderly increases their political influence, but the results are not inconsistent with a decline in the spending per elderly when the number of elderly goes up.

We have a dataset of local government service spending and age groups of the population for the period 1989-96 made available to us by the Danish Ministry of Finance. The panel allows an investigation of the relationship between shares of age groups and spending per inhabitant in the relevant age groups for three services: child care, education, and care for the elderly. We address the methodological challenge of Tiebout-bias by using historical measures of the age composition as instruments in line with Harris et al. (2001) and Ladd and Murray (2001). Our estimates indicate that the elderly reduce spending in child care and education, but the young do not threaten services for the elderly. The results furthermore support the hypothesis that it is a disadvantage for both the young and the elderly to be part of a large cohort.

Section 2 clarifies the understanding of generational conflict and (dis)advantage of large cohorts. The institutional setting in Denmark is described in section 3, and Section 4 presents data and empirical specification of the analysis. Section 5 discusses the results, and section 6 offers concluding remarks.

## **2. Understanding generational conflict**

The demand model for public services is the obvious starting point to understand

demographic shifts and conflicts between age groups. Different age groups have different demand for public services. The standard understanding of demographic shift is that the identity of the median voter changes, as suggested by Inman (1978). When the median voter gets older, public spending will shift from services to the young to care for the elderly. The budget constraint shows the disadvantage of being part of a large cohort. Given the available finances and service level, a larger client group will be more expensive to serve. The cost effect is likely to reduce spending per client when the number of clients goes up. The demand models consequently identify a tradeoff between political influence versus service costs. On the one hand increased size of a voter group means more political influence, but on the other hand spending must go up to keep the service level constant for the whole group.

Empirical analyses often have assumed a broader 'community preference' including demographic descriptives since the median voter assumes single dimensionality. Cutler et al. (1993) analyze the effects of demographic shift for local spending levels in this context. The normative implications of 'community composition' are worked out by Schwab and Oates (1991). The research has shifted towards the understanding of political institutions and an early contribution by Craig and Inman (1986) proposes a voter group decision model, where the actual outcome is a weighted average of each group's preferred allocation. More recent contributions apply probabilistic voting models as the foundation for fiscal demand analysis and Holtz-Eakin (1992) presents the linkages between median voter and probabilistic demand models. Borge et al. (1995) provide an empirical analysis of how reallocation of resources between different age groups is affected by interest group pressure.

Recent theoretical contributions have added arguments beyond this simple understanding of generational conflict. Strömberg (1998) argues that altruism may modify the conflicting claims. The selfish battle for age group influence does not capture the links between generations at any point in time and the intertemporal distribution over the life time for each individual. Duncombe et al. (2003) find in survey data that elderly with grand children are more likely to support school spending than those without. The cost effect of the size of the cohort may include economies of scale that will modify the cost effect. In this case, spending per client may go down with increasing size of an age group even when service level for each individual in the group goes up.

Dynamic intergenerational redistribution has been investigated in particular with respect to social security, and Grossman and Helpman (1998) have worked out an overlapping generation (OLG) framework to discuss political aspects. Holtz-Eakin et al. (2004) apply the OLG framework to analyze how aging affects school expenditures and economic growth. Their simulations imply that aging has a negative output effects through lower school expenditures, and that this dominates the positive effects of lower taxes. On the other hand, Gradstein and Kaganovich (2004) develop an OLG model where increased longevity has a positive effect on education funding and economic growth. The intuition is that working adults experience a higher probability of survival into retirement, and choose to increase their support for schooling to increase the returns on their savings for retirement.

Voting behavior of age groups reflects other factors than their own services. Brueckner and Joo (1991) show how homeowners have incentives to take into account the capitalization effect of public services. In our context elderly voters may support school spending to raise the value of their house. The finding of Harris et al. (2001) that the generational conflict is more severe for state financed school spending than for locally financed spending indicate that capitalization weakens the conflict between young and old at the local level. Brunner and Balsdon (2004) use survey data and find that support for school spending generally declines with age, but less so for local spending than for state spending. Their results are consistent with both capitalization of local spending into housing values and intergenerational altruism.

The relationships between age groups and age related public welfare services are complex and related to several adjustment mechanisms. Our data allow a reduced form investigation of the relationships and future work must address tests of alternative channels of effect.

### **3. Public welfare services and age groups in Denmark**

Denmark has 275 local governments<sup>1</sup> primarily producing child care, primary and lower secondary education, care for the elderly, and local infrastructure. Home care and institutionalized care (i.e. nursing homes) for the elderly represent about half of local

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<sup>1</sup> A reform implemented in January 2007 reduced the number of local governments to around 100.

government spending. Education and child care take another ¼ of the spending. The government is among the most decentralized in the world. The local governments produce about 20% of the national product and the full local public sector (including county level with hospitals) is about 30% of national product or 50% of total public spending. Lotz (1991, 1998) presents the rationale of the Danish design. Mouritzen (1991) offers a comprehensive evaluation of the functioning of the local political system.

The present study concentrates on child care, education, and care for the elderly. These services are publicly provided private goods directed towards specific subgroups of the population. The relevant 'client' group for child care is children aged 0-6 years and for primary and lower secondary education children aged 7-15 years. Care for the elderly covers only a share of the elderly population and elderly 80 years and above represent the main target group. Spending in care for the elderly is scaled by the share of the population 80 years and above. The development of spending per 'client' and the population shares of the client groups are displayed in Table 1. During the period under study (1989-1996) the major demographic shift occurred in the younger age groups. Children eligible for child care have increased their share of the population, whereas children eligible for primary and lower secondary education have been in decline. There has been a modest increase in the share of the population 80 years and above

Table 1 about here

The two younger age groups have experienced a similar development of spending per client. Child care spending care per child 0-6 years and educational spending per student both increased by 13% in real terms from 1989 to 1996, which is equivalent to an average annual growth rate of 1.8%. In the care for the elderly sector spending per inhabitants 80 years and above declined by 10% (or 1.5% per year).

The raw data in Table 1 do not provide any clear evidence regarding the relationship between group size and spending per client. In primary education and care for the elderly there seem to be a disadvantage of being part of a large cohort. An increasing share of elderly is associated with lower spending per elderly, whereas a declining population share for children 7-15 years

of age is associated with higher educational spending per student. On the other hand, spending on child care per child 0-6 years of age has increased in a period with a growing population share. Generational conflict and the disadvantage of being part of a large cohort must be investigated in the context of a model including other determinants of public welfare spending.

The local income tax is the main source of revenue for Danish local governments and amounts to nearly 70% of total revenue. The average annual growth of the income tax base (private income in Table 1) was 1.6% during the period under study. The equalization system is to large extent arranged as pure redistribution among the local governments. Transfers to local governments with high spending needs and/or low tax bases are financed by contributions from authorities with low spending needs and/or high tax bases. As a consequence, block grants from the national government only account for 10% of total revenue. The block grants have been quite stable during the period under study.<sup>2</sup>

Table 2 about here

The models estimated include community and year fixed effects, and the crucial issue is whether there is sufficient time series variation in the data. More precisely, do the local governments experience sufficiently different demographic development during the period under study? Information on the time series variation is provided in Table 2 where we report descriptive statistics for the change in population shares from 1989 to 1996. It is evident that the aggregate development in Table 1 masks substantial variation across local governments. The change in the share of children 0-6 years of age varies from a reduction of 1.4 percentage points to an increase of 3.5 percentage points, a sample range of nearly 5 percentage points. The interquartile range is 1 percentage point. The variation is equally large for the share of children 7-15 years of age, with a sample range of nearly 6 percentage points and an interquartile range of nearly 1 percentage point. It can also be seen that the variation is substantially less for the share of elderly 80 years and above. The sample range is only 2 percentage points and the standard deviation is less than half of that for the two younger age groups. A broader measure of the elderly, the share of the population 67 years and above,

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<sup>2</sup> The sharp decline from 1995 to 1996 is due to changes in the grant system.

shows slightly more variation than the two younger age groups. In the empirical analysis this broader measure of the elderly will be used as an alternative to capture generational conflict. Although the time span is short, we conclude that the data set is rich in the sense that it includes local governments with very different demographic development.

#### 4. Data and empirical specification

The analysis is based on a balanced panel data set covering all 275 Danish local governments during the period 1989-1996. The data are based on local government accounts and population statistics, and have been made available to us by the Danish Ministry of Finance. The dependent variable ( $E_{it}$ ) is real spending per client in child care, education, or care for the elderly in community  $i$  in year  $t$ . The following core empirical specification is applied for all three service sectors:

$$\log(E_{it}) = \beta_1 \log(TINC_{it}) + \beta_2 \log(CH06_{it}) + \beta_3 \log(CH715_{it}) + \beta_4 \log(EL80+_{it}) + \alpha_t + \eta_i + \varepsilon_{it} \quad (1)$$

The explanatory variables are per capita income ( $TINC_{it}$ ), the share of children 0-6 years of age ( $CH06_{it}$ ), the share of children 7-15 years of age ( $CH715_{it}$ ), and the share of the population 80 years and above ( $EL80+_{it}$ ).<sup>3</sup> Spending and total income are measured in real terms. A set of time dummies ( $\alpha_t$ ) capture time specific factors common to all local governments. Finally, ( $\eta_i$ ) is a community specific term and  $\varepsilon_{it}$  an error term. The specification is similar to Poterba (1997), but is generalized to a broader set of public welfare services.

We started out with private income and block grants as separate external sources of revenue, but in line with other studies of Danish local governments we have not obtained reliable estimates of the block grant effect. Block grants are partly selffinanced (see Section 3) and this may explain the unstable estimates. Below we report results using the sum of private income and block grant ( $TINC$ ) as income variable. The effects of the demographic variables

are robust to alternative specifications of the income variables.

All equations estimated take account of community specific fixed effects. The statistical inference is then based on the time series variation in the data, how changes in the age composition of the population over time affect the composition of services. The model is estimated with the least squares dummy variable method and by differencing out the community specific effect. The main methodological challenge is the importance of mobility. If the client groups move from local governments with low spending per client to local governments with high spending per client, population shares and spending per client are jointly determined, and Tiebout-bias is a potential problem. The direction of the Tiebout-bias is likely to differ between the direct effects and the cross effects.<sup>4</sup> To see this, suppose that both the direct effects and the cross effects are negative. Since the Tiebout-effect produces a positive correlation between the relative size of the client group and spending per client in their own sector, the true direct effect is likely to be underestimated (in absolute value) when the simultaneity problem is not taken into account. On the other hand, since the different population groups compete for resources, the Tiebout-effect produces a negative correlation between the relative size of a client group and spending per client in other sectors. Then the true cross effects are likely to be overestimated (in absolute value). The potential Tiebout-bias is handled by use of instruments. We follow Harris et al. (2001) and Ladd and Murray (2001), and use historical measures of the age composition as instruments. In addition we utilize that business cycle effects on population growth and age composition vary between urban and rural communities.

## 5. Estimation results

The core panel data model with data for 1989-1996 and using community specific fixed effects is presented as the first set of estimates (fixed effects, baseline) in Table 3. The direct elasticities are significantly negative, i.e. *CH06*, *CH715* and *EL80+* come out with negative signs for child care, education, and care for the elderly respectively. The disadvantage of being part of a large cohort is strongly supported. Spending per client tends to be reduced

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<sup>3</sup> Description and summary statistics for the variables are reported in the appendix Table A1.

<sup>4</sup> The direct effects refer to the (dis)advantage of being part of a large cohort, while the cross effects refer to

when relative group size increases. The elasticities range from -0.64 in care for the elderly to -0.79 in child care, and are of roughly of the same magnitude in the three sectors.

The cross effects capture generational conflict. The main effect identified is that an increased share of elderly has a significant negative effect on spending in child care and education, i.e. the elderly crowd out spending for the young. The crowding out effect is stronger for child care than for education. There is no evidence of the opposite effect that the younger age groups contribute to lower spending in care for the elderly.

Table 3 about here

In the second set of estimates we include some additional controls. These are population size (*POP*), the share of socialists in the local council (*SOC*), and female work participation (*FWORKP*).<sup>5</sup> Female work participation is associated with higher resource use in all three sectors (reflecting demand for child care and day care services for younger school children, and less family based care for the elderly) and that growing communities are able to exploit economies of scale.<sup>6</sup> The impacts of relative group size are very robust to the inclusion of additional controls. The main difference is that the impact of the share of children 0-6 years in child care is somewhat reduced in magnitude, making the direct elasticities even more similar across sectors.

The community specific effects can alternatively be eliminated by differencing, and the final set of estimations in Table 3 is based on the development from 1989 to 1996. By increasing the frequency from one to seven years the length of the time period also becomes similar to the US studies by Poterba (1997), Harris et al. (2001), and Ladd and Murray (2001) that use data for every 10th year. The direct effects of relative group size come out highly significant also in this case, but the quantitative effects are somewhat reduced compared to the baseline estimates. The main generational conflict is still that the elderly impose lower spending for the younger age groups, but the impact in education is not statistically significant in this case.

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generational conflict.

<sup>5</sup> Female work participation is measured as the fraction of women 20-44 years that is employed.

<sup>6</sup> The weak effect of the share of socialists may reflect that the time series variation is limited as we only have data from two local elections.

The estimated income elasticities in Table 3 show that spending in child care is most responsive to changes in total income, whereas care for the elderly is least responsive. The lower elasticities for child care and education in the fixed effects specification may reflect that these estimates to a larger extent are affected by transitory changes in income.

We now turn to the handling of the possible simultaneity problem due to Tiebout sorting. Our point of departure in addressing the simultaneity problem is Harris et al. (2001) and Ladd and Murray (2001), who use the age composition 10 years before as instruments. Based on the same reasoning we use the share of children 0-6 years lagged 10 years as instrument for *CH715* and the share of the population 67-79 years as instrument for *EL80+*. The share of the population 20-44 years did not perform well as instrument for *CH06*,<sup>7</sup> probably reflecting high mobility among younger adults. Our chosen instrument for *CH06* captures the fact that business cycle effects on population growth and age composition vary between urban and rural communities. The idea is that booms are associated with migration from rural to urban areas, and that this effect is particularly strong for younger adults with children below school age. We measure booms and busts by the change in the national unemployment rate (*dU*), while the urban-rural dimension is captured by the log of the population density (*DE*) measured as the number of inhabitants (lagged 10 years) per square kilometer. As instrument we use the product of the change in the unemployment rate and the log of population density.

Table 4 shows the estimation results when Tiebout sorting is taken into account. The results from the first stage regressions are reported in the left panel. The instruments perform well in the sense that they are significantly correlated with the relevant variables. Ten years lag of the share of children 0-6 years of age and the share of the population 67-79 years of age are as expected positively correlated with respectively *CH715* and *EL80+*. Moreover, the interaction term between the change in the unemployment rate and population density is significantly correlated with *CH06*. The interpretation of the negative coefficient is that the share of children increases more in urban areas than in rural areas in periods where the rate of unemployment is reduced.<sup>8</sup>

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<sup>7</sup> The variable was insignificant in the first stage regression.

<sup>8</sup> Although the first stage regressions explain more than 90% of the variation in the variables to be instrumented,

Table 4 about here

The second stage regressions in the right panel of Table 4 reveal that the direct effects of relative group size are negative and highly significant also when they are instrumented.<sup>9</sup> The estimates of the share of children 7-15 years in education and the share of elderly 80 years and above in care for the elderly are quite similar to the baseline fixed effects estimates. On the other hand the estimate of the share of children in child care increases substantially in absolute value. The absolute value is above unity, indicating that total spending in child care is reduced when the share of children 0-6 years increases.<sup>10</sup> Also the IV estimates indicate that the main generational conflict is that the elderly impose negative effects on spending for the young. The quantitative effects are stronger than in the baseline fixed effects models, but the coefficient for educational spending is less precisely estimated. The two younger age groups impose negative effects on each other, but not on the elderly.

In Tables 3 and 4 the generational conflict between the young and the elderly were identified using the share of the population 80 years and above as a proxy for elderly voters. The main motivation for this formulation is that the elderly 80 years and above is the main target group for care for the elderly. However, most elderly voters are below 80 years of age and they may also crowd out spending for the young.<sup>11</sup> In Table 5 we identify the generational conflict using the share of the population 67 years and above as proxy for elderly voters. This definition of the elderly is also more in line with the US studies of generational conflict that use the share of the population above 65. It turns out that the generational conflict in most cases becomes stronger with this broader definition of the elderly. Moreover, in this case the negative impact of elderly in education is statistically significant also with differencing and instruments.

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overfitting is not a problem. The reason is that only the variation beyond fixed effects and time dummies are used to estimate the parameters of interest. When this is taken into account, the first stage regressions explain 20-45% of the relevant variation in the variables to be instrumented.

<sup>9</sup> Also Harris et al. (2001) and Ladd and Murray (2001) find that the impacts of demographics are not much affected by the use of instruments.

<sup>10</sup> The elasticity remains above unity in absolute value also when we include additional controls or remove the community specific term by differencing.

<sup>11</sup> In 1996 the elderly 67 years and above made up 13.4% of the population, whereas elderly 80 years and above made up 3.9%.

Table 5 about here

It is of interest to compare our findings with those from other studies. Since the international literature has focused on educational spending, the explicit comparison of estimates must be restricted to this sector. US studies have focused on generational conflict, and the results vary substantially across studies. Poterba (1997) finds strong evidence of generational conflict using state level data. He estimates the elasticity of school spending with respect to the share of elderly to be -0.26. Much weaker effects are found on lower level data. Harris et al. (2001) estimate elasticities of up to -0.10 using school district data, while Ladd and Murray (2001) find no evidence of generational conflict using county level data. Our estimates range from -0.10 to -0.15 when elderly is measured as the share of the population 67 years and above, and are most similar to the findings of Harris et al. (2001).<sup>12</sup> In addition, we document that this generational conflict is even more severe for child care, but that the younger age groups do not contribute to lower spending in care for the elderly.

Consistent with other studies, we find that there is a disadvantage for school children to be part of a large cohort. The direct elasticities are in the order of -0.6 to -0.7, and they are all significantly less than 0 and significantly larger than -1. Educational spending increases when the number of pupils increases, but not sufficiently to avoid a reduction in spending per pupil. The estimated disadvantage is somewhat larger than in US (Harris et al., 2001; Ladd and Murray, 2001) and German (Kempkes, 2007) studies using local government data, but less than in Poterba's (1997) study of the US states.<sup>13</sup> Also Grob and Walter (2005), analyzing Swiss cantons, find that educational spending per student decreases when the number of students increases. Our analysis clearly shows that the disadvantage of being part of large cohort extends to child care and care for the elderly, and that the order of magnitude is roughly the same as in the educational sector.

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<sup>12</sup> Grob and Wolter (2005) use data for Swiss cantons (not local governments), and do also find evidence of generational conflict. They do not report a comparable elasticity, but we have calculated it to -0.23. Their finding seems to confirm that analyses of higher level government tend to find stronger generational conflict.

<sup>13</sup> Poterba (1997) estimates the elasticity to be close to -1, which means that total educational spending remains unaltered when the number of pupils increases.

## **6. Concluding remarks**

The Scandinavian local governments arrange public welfare services for the young and the old, and demographic shifts affect the political influence of the different age groups and the costs of providing the services. Whereas earlier contributions analyzing generational conflict and the (dis)advantage of being part of a large cohort have focused on educational spending, the decentralization of public welfare services in Scandinavia allows for a simultaneous analysis of services for the young and the elderly.

The econometric analysis is based on a panel data set for local governments in Denmark during the period 1989-1996, and focuses on child care, education, and care for the elderly. In line with earlier European and US studies, we find evidence of generational conflict in the sense that a larger share of elderly voters reduces educational spending. We also identify disadvantage of being part of a large cohort as a larger share of students in the population reduces educational spending per student. The extension to include services for the elderly and child care offers some new results. Elderly voters also reduce spending in child care, the young do not threaten services for the elderly, and both the young and the elderly have a disadvantage of being part of a large cohort.

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Table 1

Year	Population shares (%)			Spending per client			Private income	Block grants
	0-6	7-15	80+	Child	Educat.	Elderly		
1989	7.5	11.3	3.6	1.00	1.00	1.00	1.00	1.00
1990	7.6	10.9	3.7	1.00	1.01	0.96	1.00	1.04
1991	7.9	10.5	3.7	1.01	1.04	0.93	1.00	0.95
1992	8.1	10.2	3.8	1.04	1.05	0.91	1.01	0.98
1993	8.3	9.9	3.9	1.08	1.09	0.90	1.02	1.09
1994	8.5	9.8	3.9	1.13	1.10	0.90	1.08	1.05
1995	8.8	9.7	3.9	1.10	1.12	0.87	1.08	1.03
1996	9.0	9.7	3.9	1.13	1.13	0.90	1.12	0.73

Note: All figures are weighted averages. Spending per client, private income and block grants are in 1996 prices and measured as an index where the average value for 1989 equals unity. Private income and block grants are measured per capita.

Table 2

Descriptive statistics for the change in population shares (%-points), 1989-1996

Age group	Min	1. quart.	Median	3. quart.	Max	St.dev.
0-6 years ( <i>CH06</i> )	-1.4	0.7	1.3	1.7	3.5	0.74
7-15 years ( <i>CH715</i> )	-5.1	-2.2	-1.7	-1.3	0.7	0.87
80 years and above ( <i>EL80+</i> )	-0.4	0.2	0.4	0.6	1.6	0.32
67 years and above ( <i>EL67+</i> )	-4.4	-0.1	0.3	0.8	3.4	0.95

Note: The figures are based on data for 275 local governments.

Table 3  
Regression analyses

Variable	<u>Fixed effects, baseline</u>			<u>Fixed effects, additional controls</u>			<u>Differencing</u>		
	Child care	Education	Elderly care	Child care	Education	Elderly care	Child care	Education	Elderly care
log( <i>TINC</i> )	0.914 (7.79)	0.269 (5.00)	0.049 (0.56)	0.777 (6.53)	0.212 (4.41)	-0.036 (-0.43)	2.059 (8.20)	0.480 (4.48)	-0.015 (-0.08)
log( <i>CH06</i> )	-0.792 (-7.19)	-0.191 (-4.62)	-0.016 (-0.25)	-0.686 (-6.05)	-0.158 (-3.68)	0.012 (0.18)	-0.724 (-6.20)	-0.161 (-3.15)	-0.022 (-0.26)
log( <i>CH715</i> )	-0.042 (-0.32)	-0.680 (-12.96)	-0.012 (-0.15)	-0.037 (-0.29)	-0.689 (-13.13)	-0.018 (-0.23)	-0.070 (-0.44)	-0.595 (-8.70)	-0.071 (-0.76)
log( <i>EL80+</i> )	-0.231 (-3.07)	-0.049 (-1.73)	-0.641 (-10.78)	-0.217 (-3.14)	-0.059 (-2.12)	-0.660 (-11.18)	-0.191 (-2.00)	-0.027 (-0.69)	-0.510 (-7.28)
log( <i>POP</i> )				-0.428 (-1.47)	-0.313 (-2.20)	-0.448 (-2.12)			
log( <i>SOC</i> )				0.029 (0.79)	-0.000 (-0.02)	-0.039 (-1.70)			
log( <i>FWORKP</i> )				0.995 (6.89)	0.157 (2.32)	0.226 (2.18)			
Observations	2200	2200	2200	2200	2200	2200	275	275	275
$R_{adj}^2$	0.951	0.931	0.920	0.955	0.933	0.921	0.443	0.284	0.203

Note: Dependent variables are log of spending per client for the three public services, time dummies are included in the fixed effects regressions, and a constant term in the differenced equations. The t-values in parentheses are based on robust standard errors.

Table 4  
Fixed effects IV analysis

<u>First stage regressions</u>				<u>Second stage (IV) regressions</u>			
Variable	log(CH06)	log(CH715)	log(EL80+)	Variable	Child care	Education	Elderly care
log(DE) <sub>t-10</sub> x dU	-0.817 (-7.94)	-0.113 (-1.56)	-0.111 (-0.93)	log(CH06)	-2.105 (-6.95)	-0.601 (-4.84)	0.401 (1.97)
log(CH06) <sub>t-10</sub>	-0.176 (-4.97)	0.456 (17.06)	-0.030 (-0.78)	log(CH715)	-0.436 (-2.06)	-0.701 (-8.60)	0.146 (0.96)
log(67-79) <sub>t-10</sub>	0.049 (1.18)	0.041 (1.48)	0.627 (13.57)	log(EL80+)	-0.498 (-2.70)	-0.067 (-1.03)	-0.570 (-4.54)
Observations	2200	2200	2200	Observation	2200	2200	2200
$R^2_{adj}$	0.927	0.973	0.990	$R^2_{adj}$	0.933	0.918	0.914

Note: Dependent variables in the right panel are log of spending per client for the three public services. Time dummies and log of total income are included in all equations. The t-values in parentheses are based on robust standard errors.

Table 5  
Alternative measure of the elderly

Variable	<u>Fixed effects, baseline</u>		<u>Differencing</u>		<u>Fixed effects IV</u>	
	Child care	Education	Child care	Education	Child care	Education
log( <i>TINC</i> )	0.766 (6.47)	0.219 (4.14)	1.854 (7.20)	0.402 (3.63)	0.279 (1.38)	0.064 (1.02)
log( <i>CH06</i> )	-0.845 (-7.63)	-0.207 (-4.94)	-0.786 (-6.62)	-0.180 (-3.49)	-2.313 (-7.97)	-0.584 (-4.82)
log( <i>CH715</i> )	-0.125 (-0.95)	-0.707 (-13.52)	-0.140 (-0.89)	-0.622 (-9.08)	-0.467 (-2.13)	-0.723 (-9.16)
log( <i>EL67+</i> )	-0.528 (-4.31)	-0.152 (-3.29)	-0.397 (-3.20)	-0.107 (-2.29)	-0.334 (-1.69)	-0.127 (-1.93)
Observations	2200	2200	275	275	2200	2200
$R^2_{adj}$	0.953	0.932	0.457	0.294	0.933	0.921

Note: Dependent variables are log of spending per client for the public services, time dummies are included in the fixed effects regressions, and a constant term in the differenced equations. The t-values in parentheses are based on robust standard errors. In the Fixed effects IV specification the share of the population 57-66 years of age lagged 10 years is used as instrument for log(*EL67+*). The instruments for log(*CH06*) and log(*CH715*) are the same as in Table 4.

Table A1  
Descriptive statistics

Variable	Description	Mean (st.dev.)
Expenditure per client in child care	Child care expenditures per child 0-6 years, Danish kroner (DKK), fixed 1996 prices	28779 (10055)
Educational expenditure per client	Educational expenditures per youth 7-15 years, DKK 1996	34510 (4381)
Care for the elderly expenditures per client	Care for the elderly expenditures per inhabitant 80 years and above, DKK 1996	112570 (23906)
Total income ( <i>TINC</i> )	The sum of private income per capita and block grants per capita, DKK 1996	90188 (14837)
The share of children 0-6 years of age ( <i>CH06</i> )	The share of the population 0-6 years, January 1	0.086 (0.010)
The share of children 7-15 years of age ( <i>CH715</i> )	The share of the population 7-15 years, January 1	0.115 (0.015)
The share of elderly 67 years and above ( <i>EL67+</i> )	The share of the population 67 years and above, January 1	0.135 (0.033)
The share of elderly 80 years and above ( <i>EL80+</i> )	The share of the population 80 years and above, January 1	0.037 (0.012)
Population size ( <i>POP</i> )	Total number of inhabitants, January 1	18826 (36482)
The share of socialists ( <i>SOC</i> )	The share of socialist representatives in the local council	0.514 (0.146)
Female work participation ( <i>FWORKP</i> )	The share of women 20-44 years that is employed	0.772 (0.046)

Note: Unweighted averages based on data for all 275 local governments during the period 1989-1996.