Have we achieved adequate, safe and sustainable pensions?

Axel Börsch-Supan

Munich Center for the Economics of Aging (MEA) at the Max Planck Institute for Social Law and Social Policy (MPISOC)

Conference on „The future of pensions in Europe: Taking stock and looking ahead two years after the White Paper”, Brussels, 26 March 2014
Have we achieved adequate, safe and sustainable pensions in the EU?

- Not yet
- No surprise: history, short-term political costs vs. long-term gains, conflicts between aims
- Still: much progress has been made

- Develop very simple analytical framework, dominated by the force of demographic change
- Fill framework with examples: can be done, has been done
Dependency will roughly double

Thus equal burden for young and old means:
~40% higher contributions and ~40% lower benefits

Conflict between adequacy and sustainability

Resolve by separate systems ("pillar 0" vs. other "pillars")

Political economy issues:
- detach pillar 0 from demography
- index other pillars as much as possible to demography
Three Demographic forces

1. \(2000\)
2. \(2025\)
3. \(2050\)
4. \(2100\)
Three Demographic forces

- BabyBoom/Bust
- Fertility -
- Fertility +
Need at least three different policy instruments to tackle demography *(sustainability)*

- *Baby boom/bust: pre-funding*
- *Longevity: retirement age*
- *Fertility: quantity/quality (education & health)*

In addition: separate fourth policy to tackle *adequacy*

*Where do we stand on these four issues?*
Gross replacement rate of pensions:

40% 67%

Median earner
(OECD pensions at a glance 2013)
Share of 65+ individuals with income below 50% median income

Source: OECD Pensions at a Glance 2013
Pensions as %GDP and the resulting implicit debt

Source: EU Commission 2011
Explicit and implicit debt
[\%GDP, as of 2012]
Figure 21: Sustainability gap “S2” in selected European countries (% GDP)

Source: Balassone et al.
Force of ageing:
Annual percentage loss in working age individuals per population
The power of structural reform

Living standard [Consumption per capita] relative to a non-aging population

- **1: Status Quo**
- **2. Labor Market Reform**
- **3. Labor Mkt & Pension Reform**

If resemble...

Source: Börsch-Supan and Ludwig 2010
Key unsustainability

Labor force participation (Men 60-64)
Expected healthy life after age 65
(no limitations in daily activities), men
Myth: Health age 60-69 in Europe

Self rated: percent excellent, very good and good

Functional: percent with no ADL limitation

Objective: grip strength kg with std deviation
Can be done, has been done:

Tailwind through employment gains in spite of demographic headwind
Can be done, has been done:

### Contribution rate by labor force participation (LFP)

**LFP pre-reform (2007)**

**LFP post-reform (2011)**

**LFP Denmark**
Pre-funding

Riester private
Occupational
Other private

Copyright: Axel Börsch-Supan @ MEA
### Synopsis of pension reform elements in Europe, 1980-2010

<table>
<thead>
<tr>
<th>Country</th>
<th>Retirement age</th>
<th>Link of benefits to contributions</th>
<th>Indexation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>women → 65</td>
<td></td>
<td>+</td>
</tr>
<tr>
<td>Germany</td>
<td>all → 67</td>
<td>(universal point sys)</td>
<td>sustainability</td>
</tr>
<tr>
<td>France</td>
<td>all → 62</td>
<td>Basis of point system</td>
<td></td>
</tr>
<tr>
<td>Italy</td>
<td></td>
<td>NDC</td>
<td>NDC</td>
</tr>
<tr>
<td>Spain</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Greece</td>
<td></td>
<td>Partially</td>
<td></td>
</tr>
<tr>
<td>Denmark</td>
<td>all → 67 rev</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sweden</td>
<td>DI</td>
<td>NDC</td>
<td>NDC</td>
</tr>
<tr>
<td>Norway</td>
<td></td>
<td>point</td>
<td>life expectancy</td>
</tr>
<tr>
<td>Finland</td>
<td>UI tunnel</td>
<td>scale factors</td>
<td></td>
</tr>
<tr>
<td>Netherlands</td>
<td>EEA, DI</td>
<td></td>
<td></td>
</tr>
<tr>
<td>UK</td>
<td>all → 68</td>
<td></td>
<td>price → wage</td>
</tr>
<tr>
<td>US</td>
<td>all → 67</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Have we achieved adequate, safe and sustainable pensions?

Have we achieved adequate, safe and sustainable economic conditions for the young?