Trends in pension systems around the world

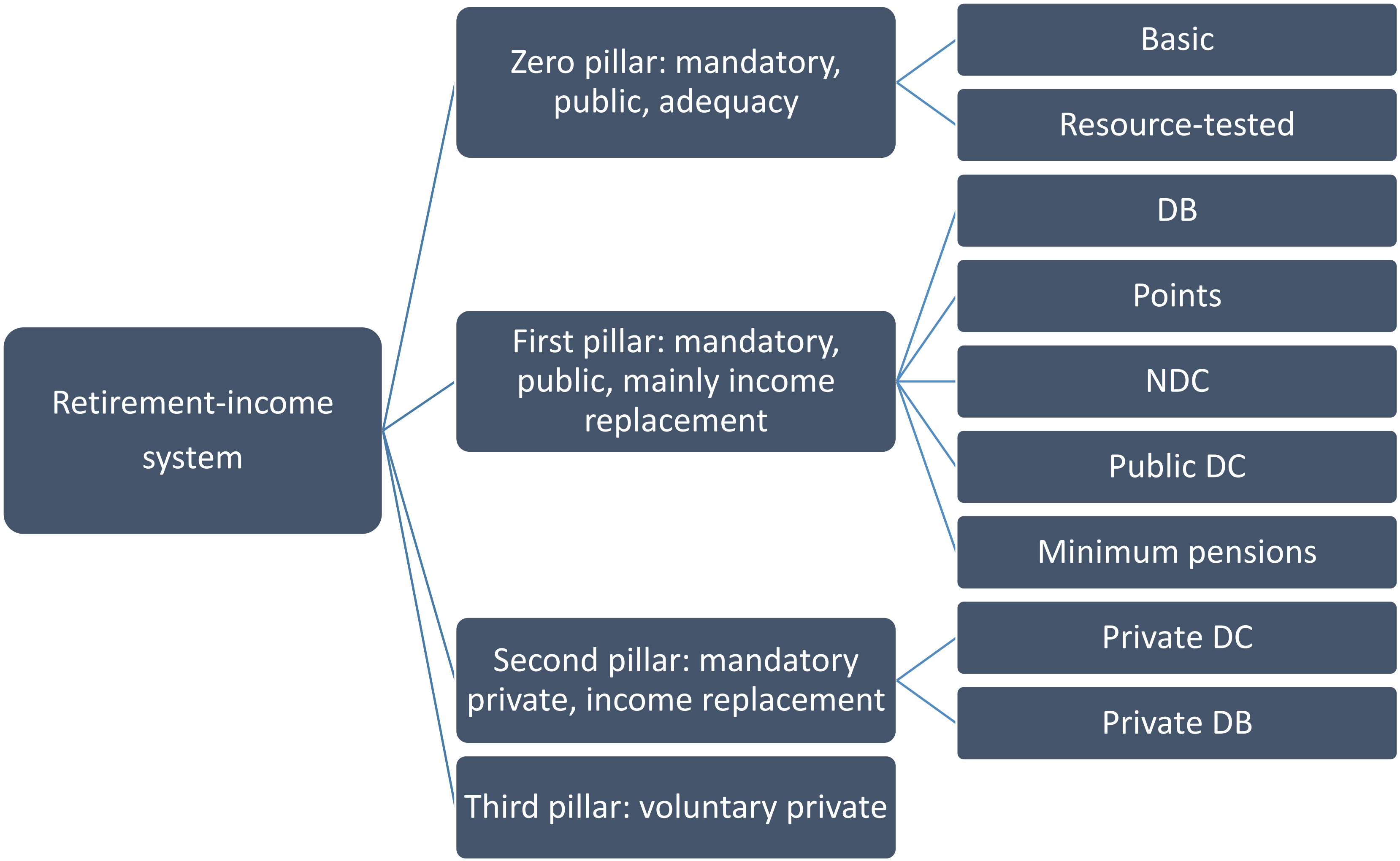
PENSIONS

GLOBAL SYSTEMS AND KEY DYNAMICS

WASHINGTON DC, MAY 2018

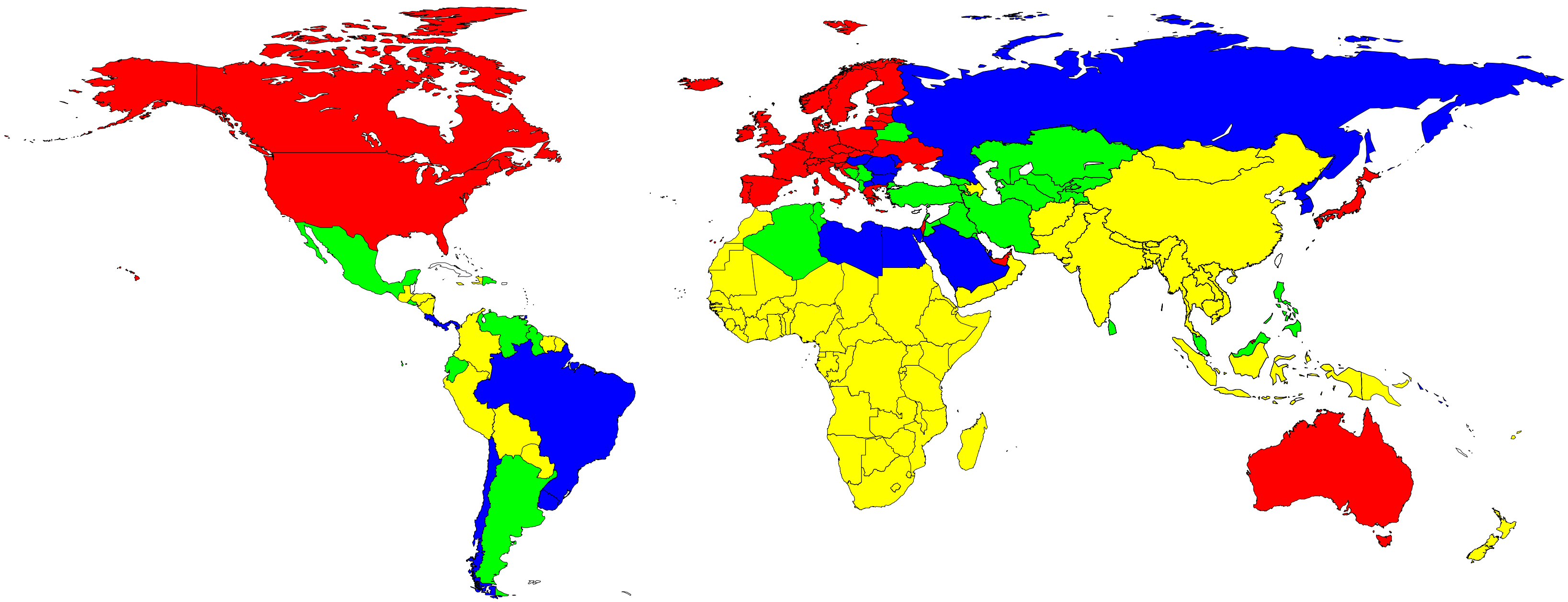
MONTSERRAT PALLARES-MIRALLES
EDWARD WHITEHOUSE

Multi-pillar framework



Coverage

Active members of mandatory pension systems
per cent of labor force

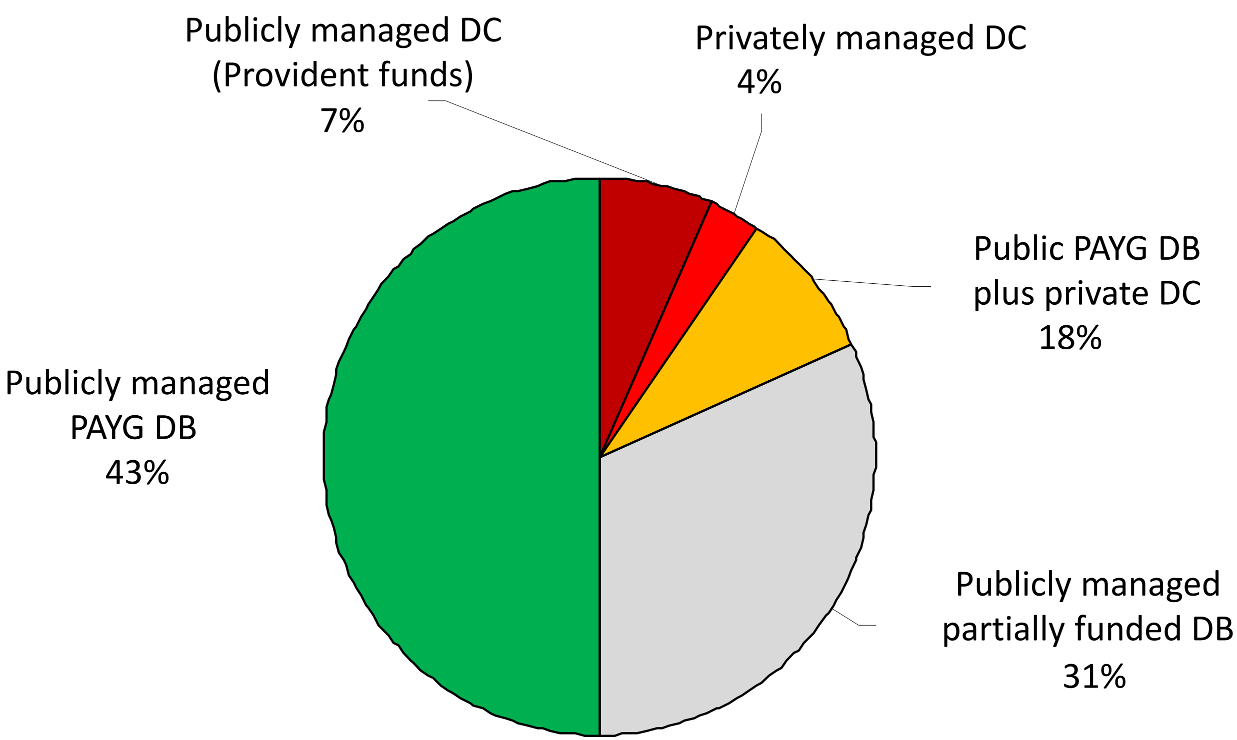


Coverage (active members / labor force)

0 to 25
25 to 50
50 to 75
75 to 100

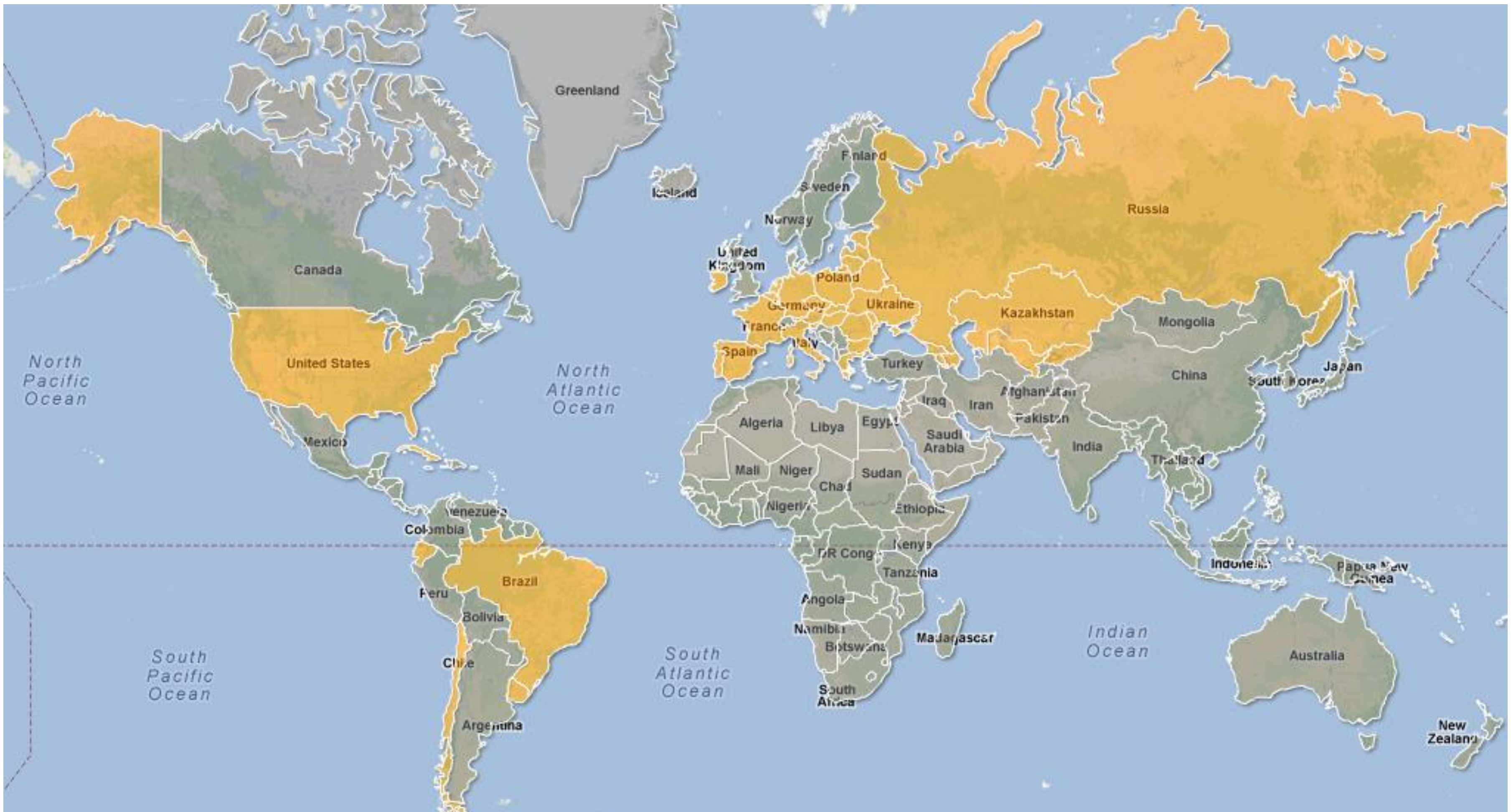
Mandatory pensions today

- Insitutional arrangements:
  - Public or private?
  - Defined benefit (DB) or defined contribution (DC)?
  - Prefunded (fully or partially) or pay-as-you-go financed?

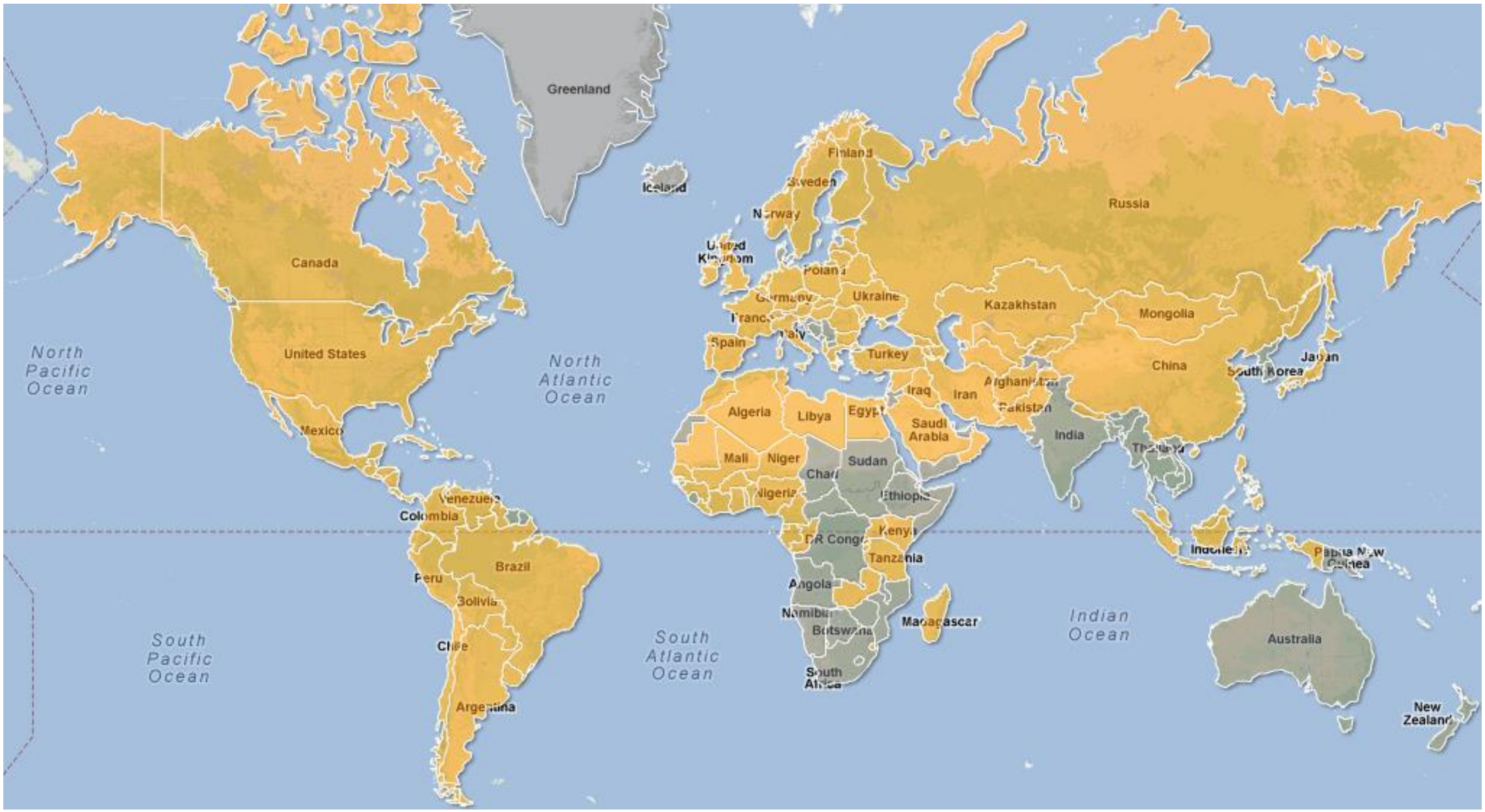


per cent of countries

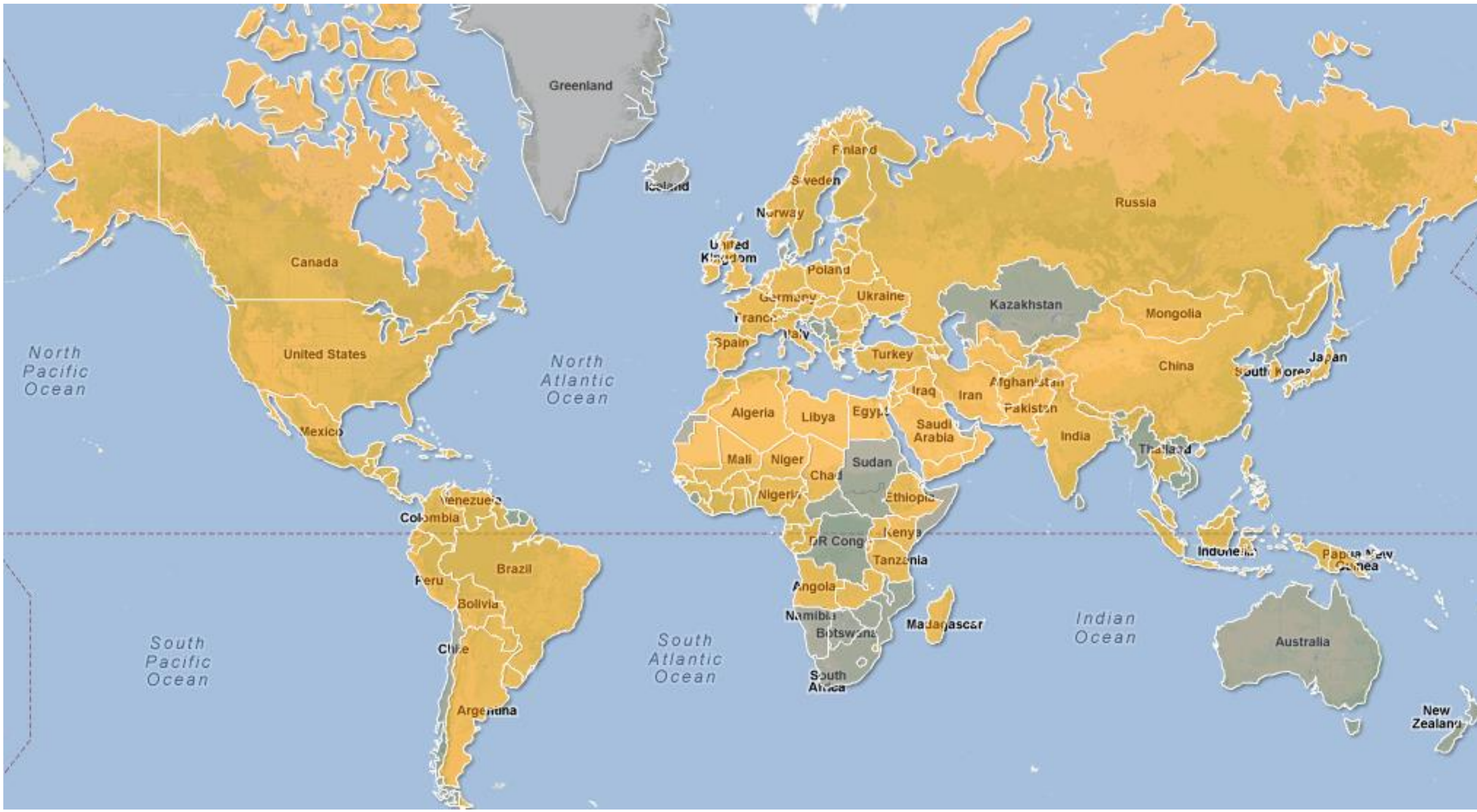
Defined-benefit public schemes in 1935



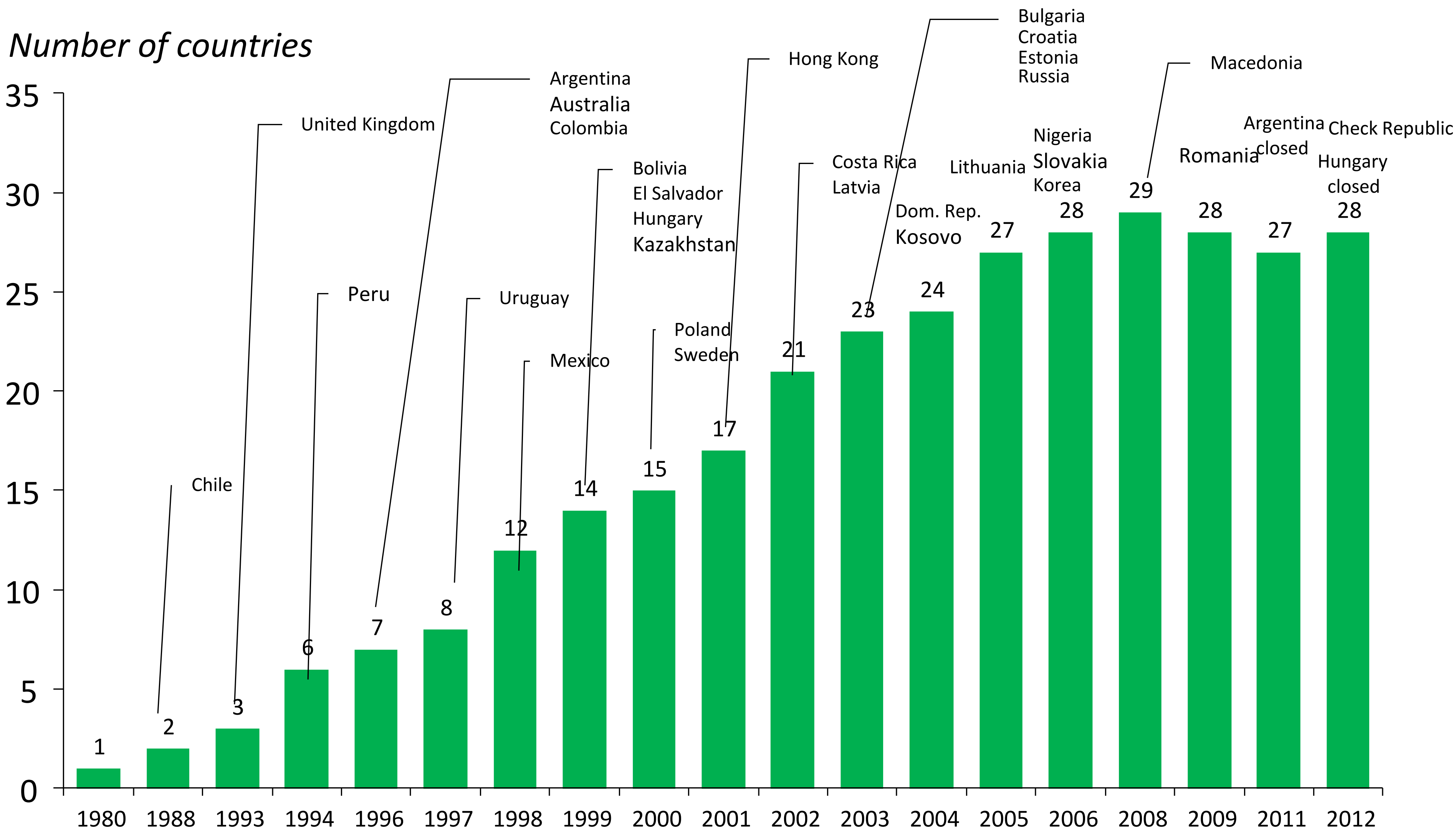
Defined-benefit public schemes in 1975



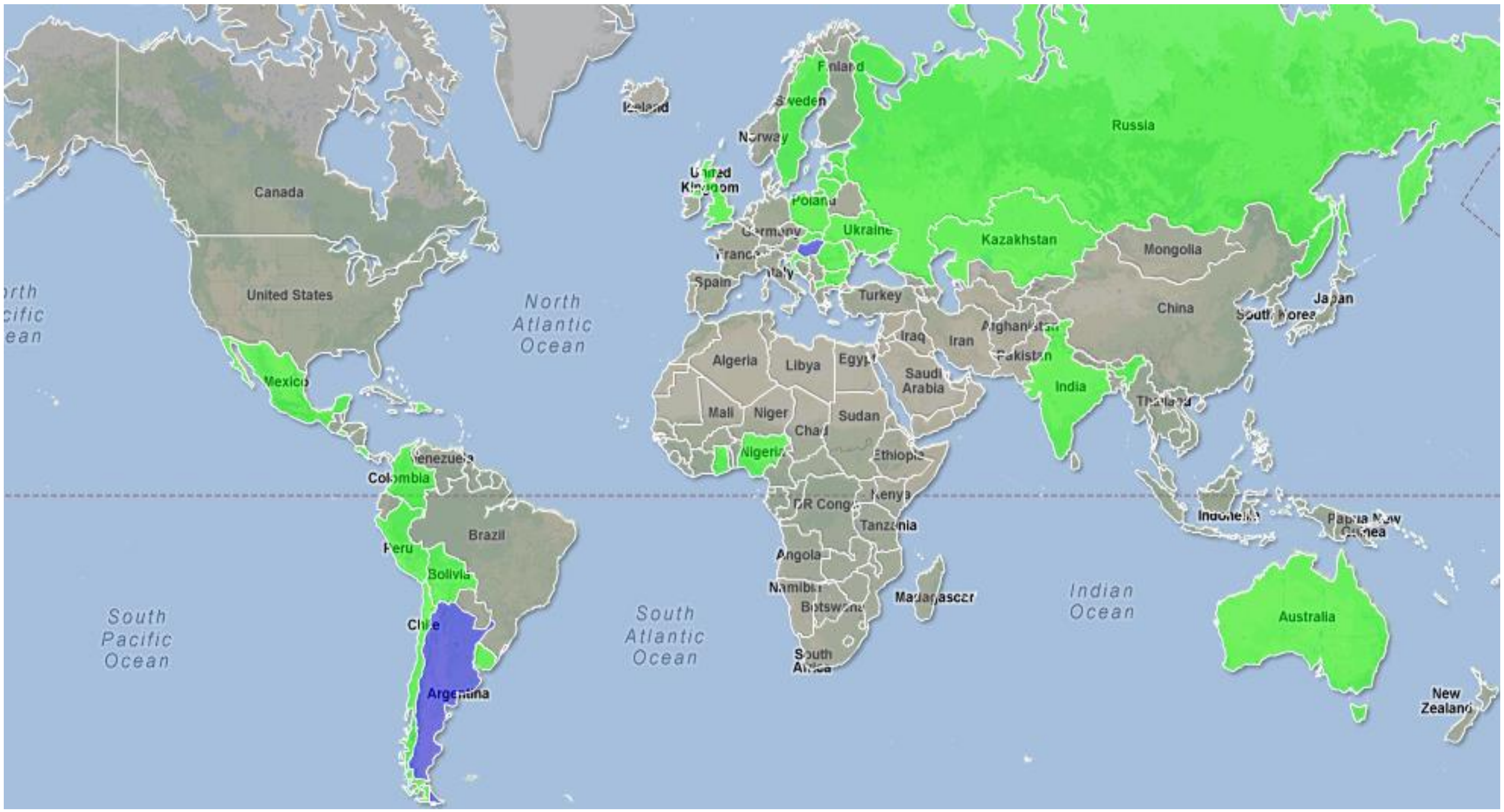
Defined-benefit public schemes in 2012



Growth of mandatory DC plans



Mandatory DC plans in 2012



Conclusions

- Public defined-benefit plans spread across the globe and dominated until the 1990s
- But, pension promises are proving difficult to keep as scheme mature and populations ages
- Defined contribution plans play a growing role
- This raises new issues such as costs, investments, payouts and regulation/supervision
- There is no single World Bank blueprint to apply to all countries
- Nevertheless, there are important best-practice principles that apply to all different retirement-income arrangements

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MANAMA, BAHRAIN, OCTOBER 2016

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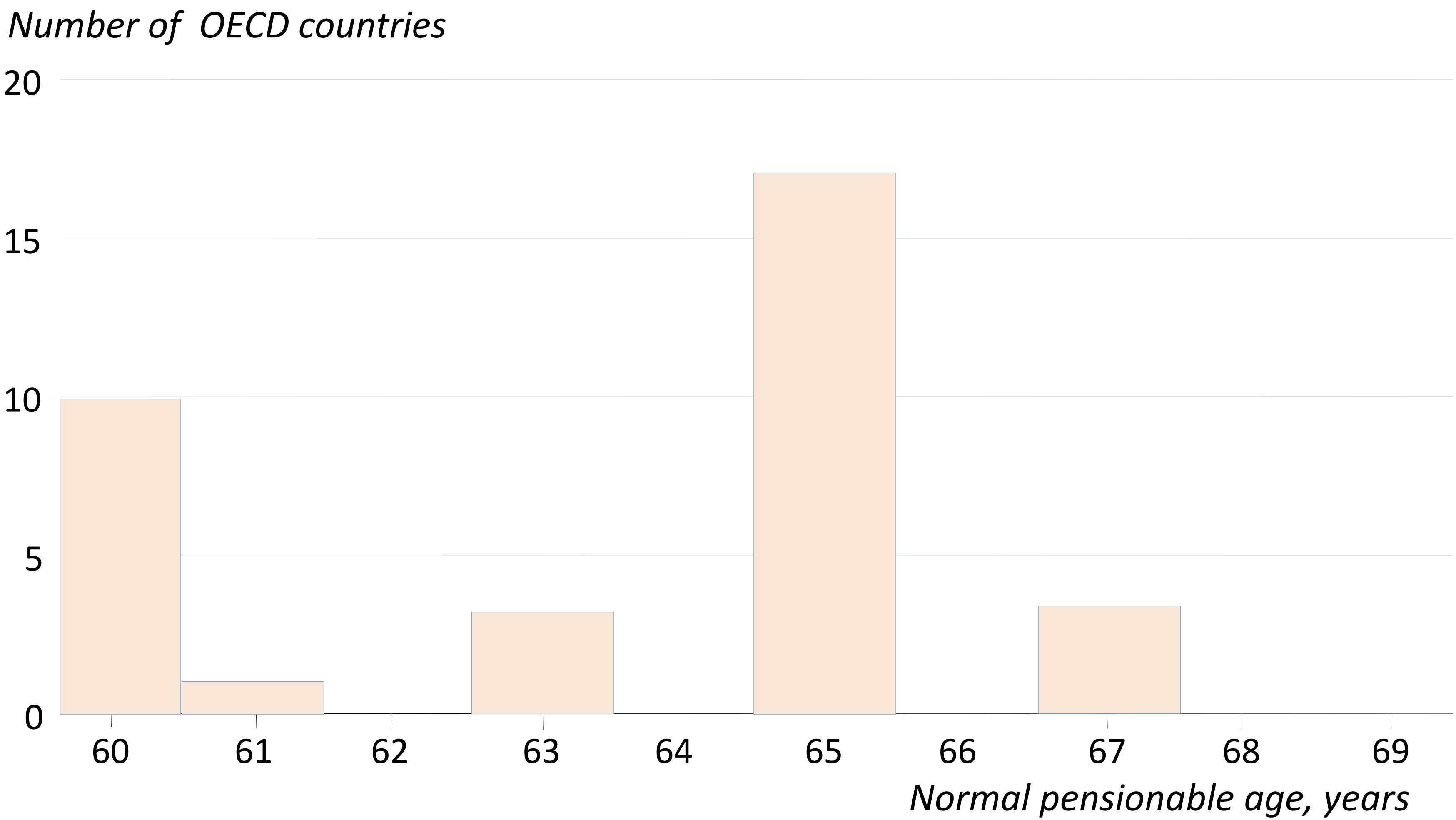
Main themes

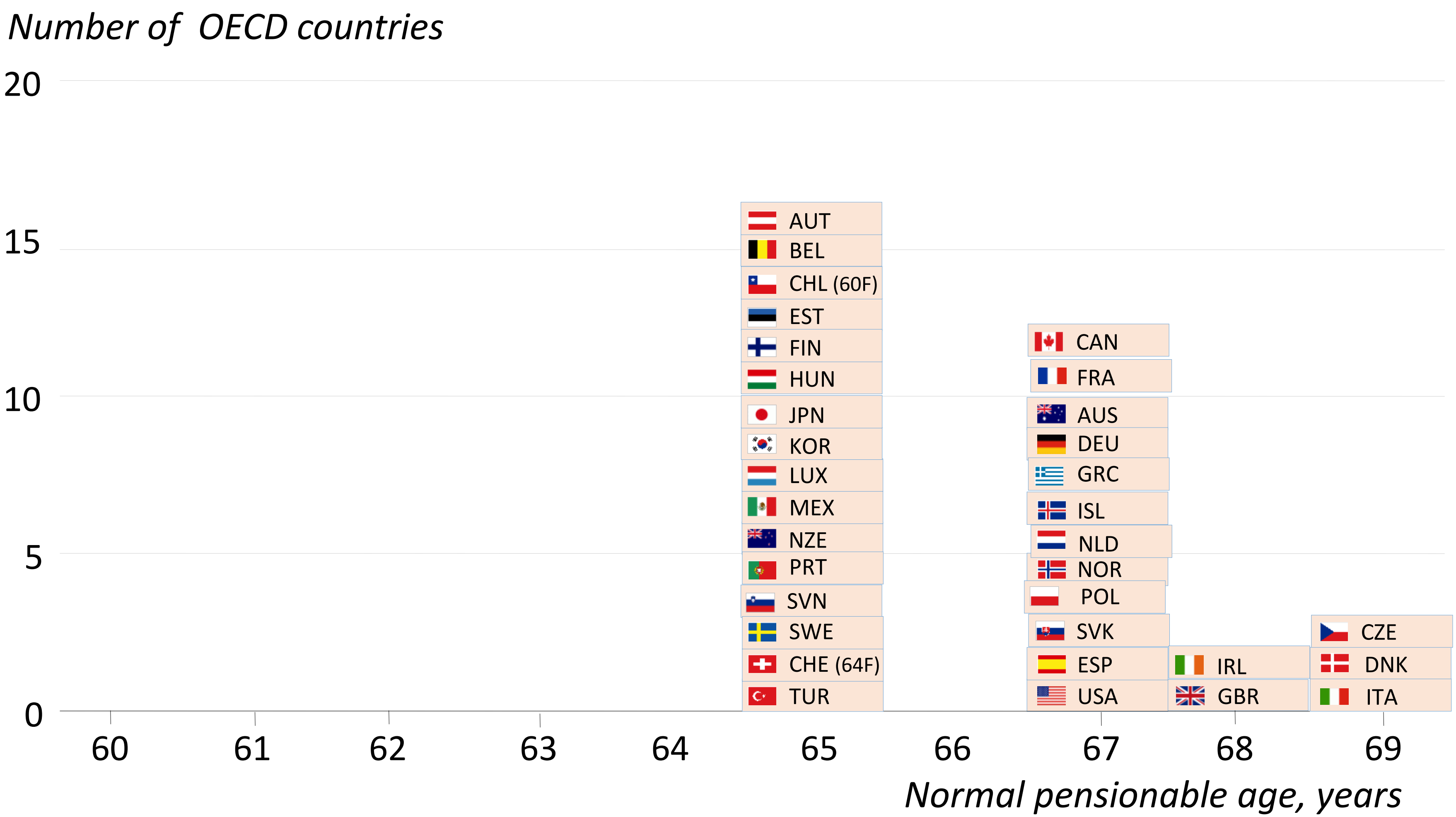
- Pace of change accelerated during the financial and economic crisis and beyond
- Balancing objectives of benefit adequacy and financial sustainability remains difficult
- Need for longer working lives widely accepted
- But cuts in public benefits to achieve financial sustainability leaves ‘pension gaps’
- These can be filled by greater private pension saving

Live longer, work longer

Pensionable age: 2000



Pensionable age: long-term rules



Live longer, work longer

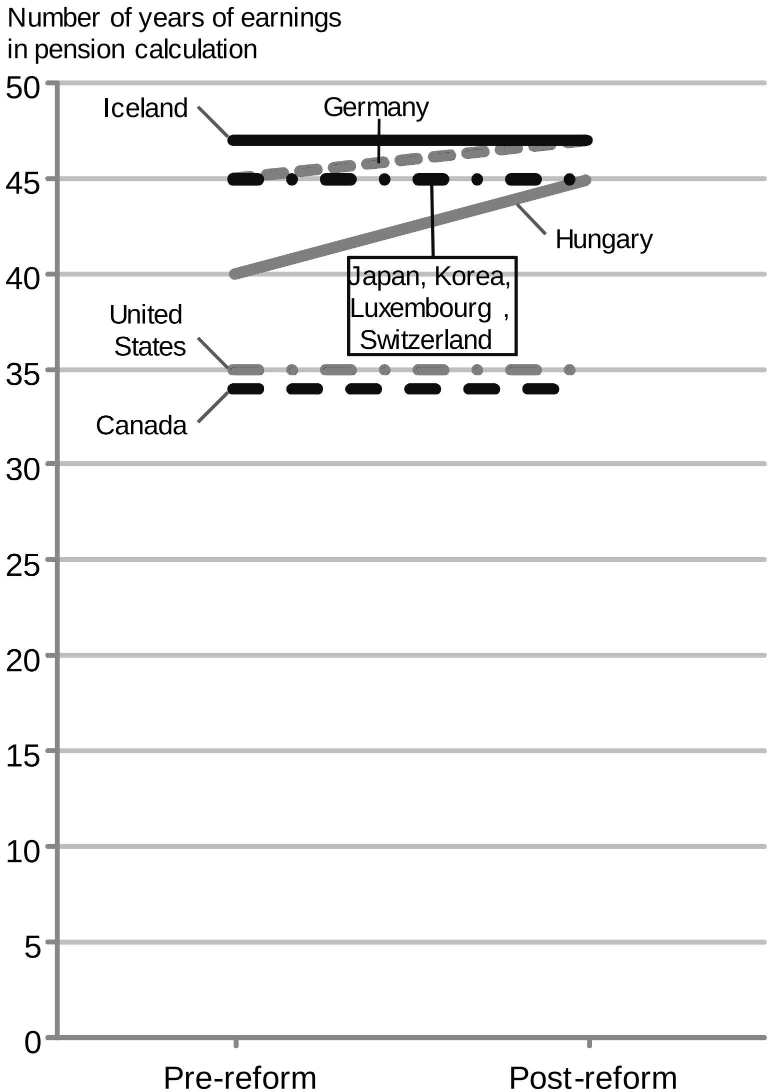
- 18 countries have taken other steps to prolong working lives
- Tighter conditions for early retirement: higher age or longer contribution years
  - Austria, Belgium, Czech Republic, Denmark, Finland, France, Greece, Hungary, Poland Portugal and Spain
- Lower benefits for early retirees
  - Austria, Canada
- Improved work incentives after normal pension age
  - France and Australia in pension system
  - Portugal and Sweden through taxes and contributions

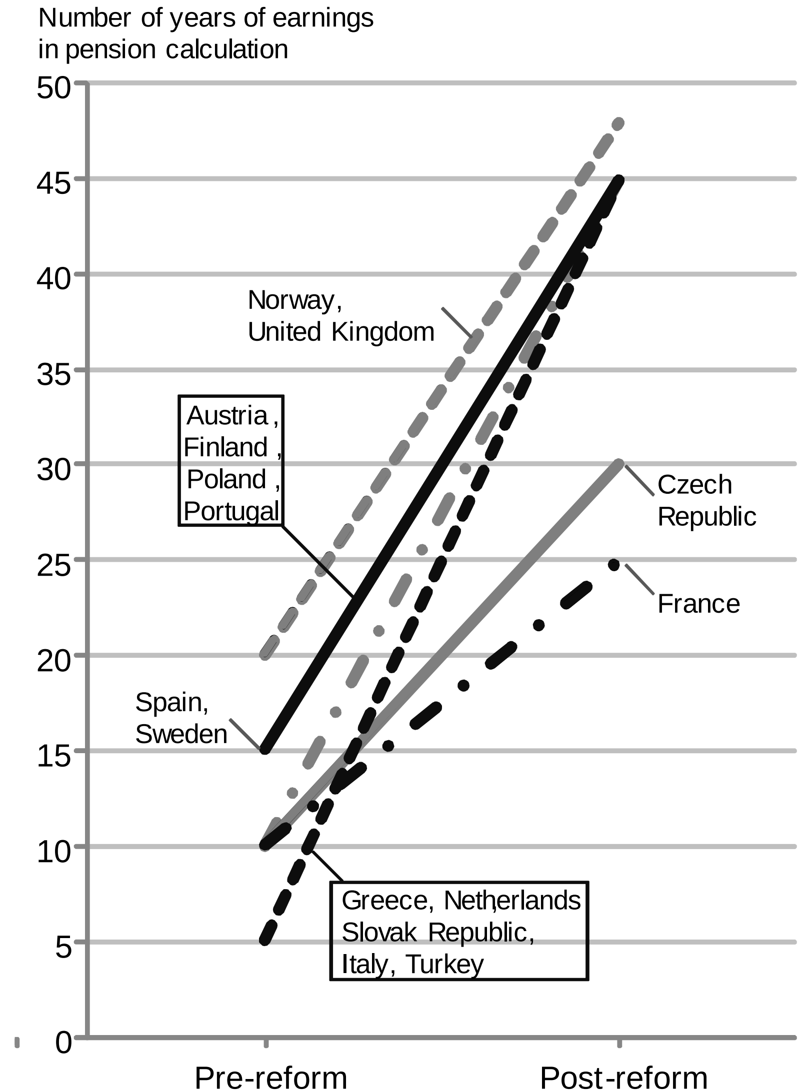
Fiscal sustainability

Reform measures

- Improved work incentives and higher pension ages will reduce costs
- Direct benefit cuts (*e.g.*, in accrual rates) remain rare
  - Austria, Korea, Greece, Hungary
- Indirect cuts through uprating of pensions in payment (indexation)
  - Belgium, Czech Republic, Finland, France, Greece, Hungary, Italy, Norway, Slovak Republic
- Changes in earnings measure and/or revaluation of earlier years' earnings

Earnings measures: before and after

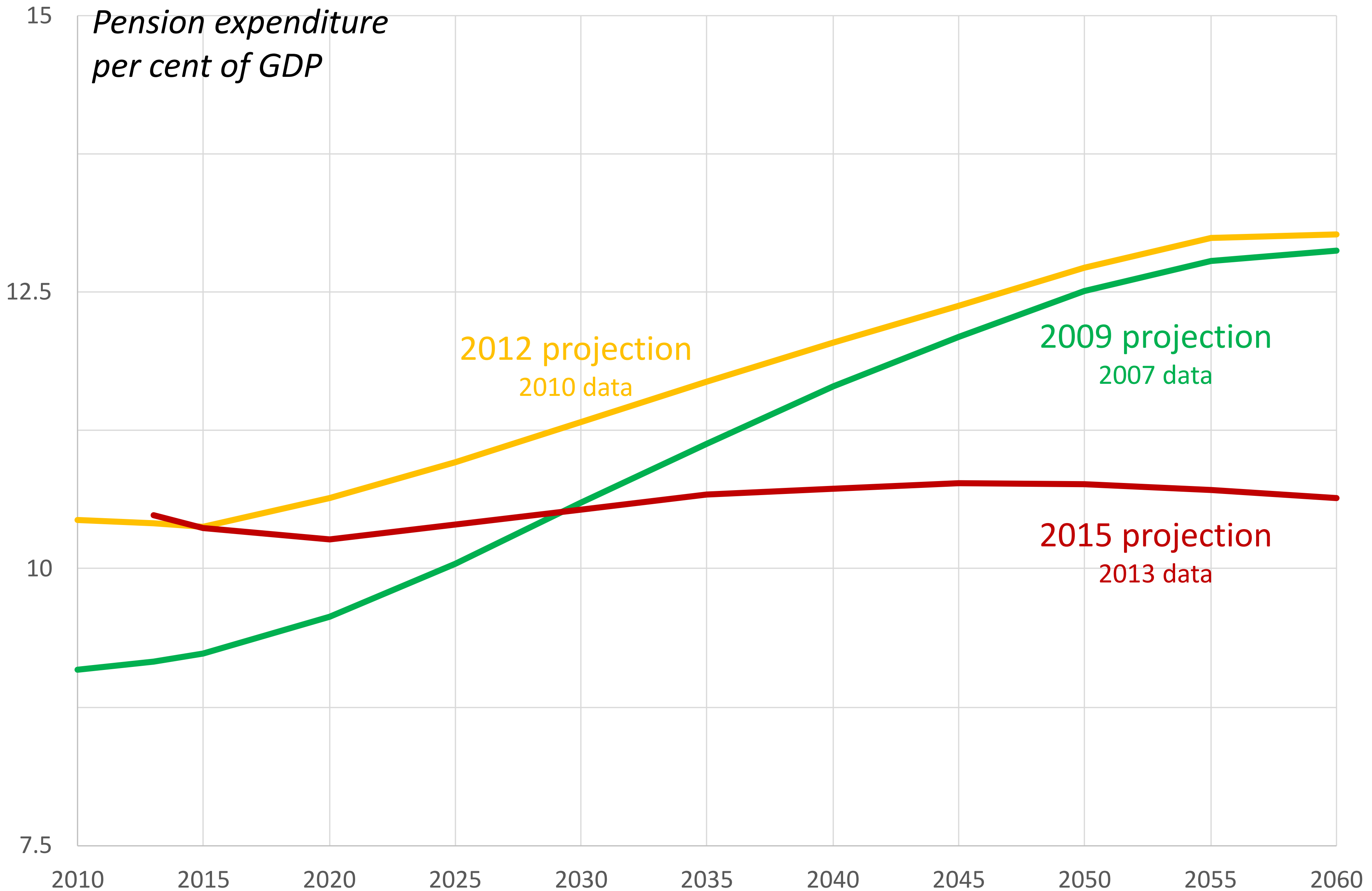




Putting pensions on auto-pilot

- Automatic changes in the pension system to help financial sustainability
- Adjustments based on financial and demographic indicators
- Changing benefits
  - level at time of retirement: Canada, Finland, Germany, Italy, Japan, Norway, Poland, Portugal, Sweden
- Pension eligibility: age or contribution years
  - Denmark, France, Greece, Italy
- Contribution rates:
  - Canada, Germany
- Defined-contribution schemes are automatically sustainable and prefunded

Public pension spending: EU

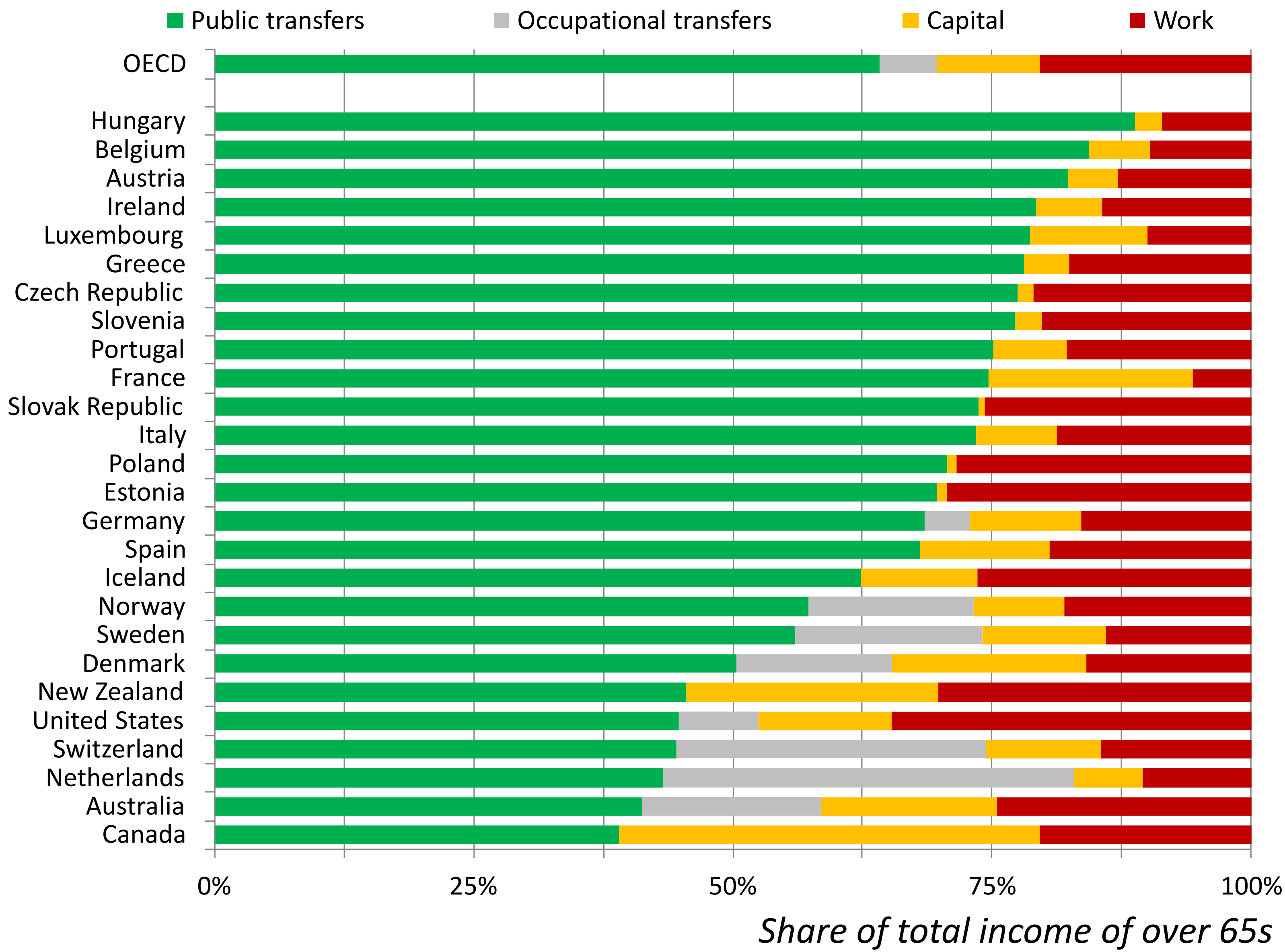


Future adequacy and private-pension savings

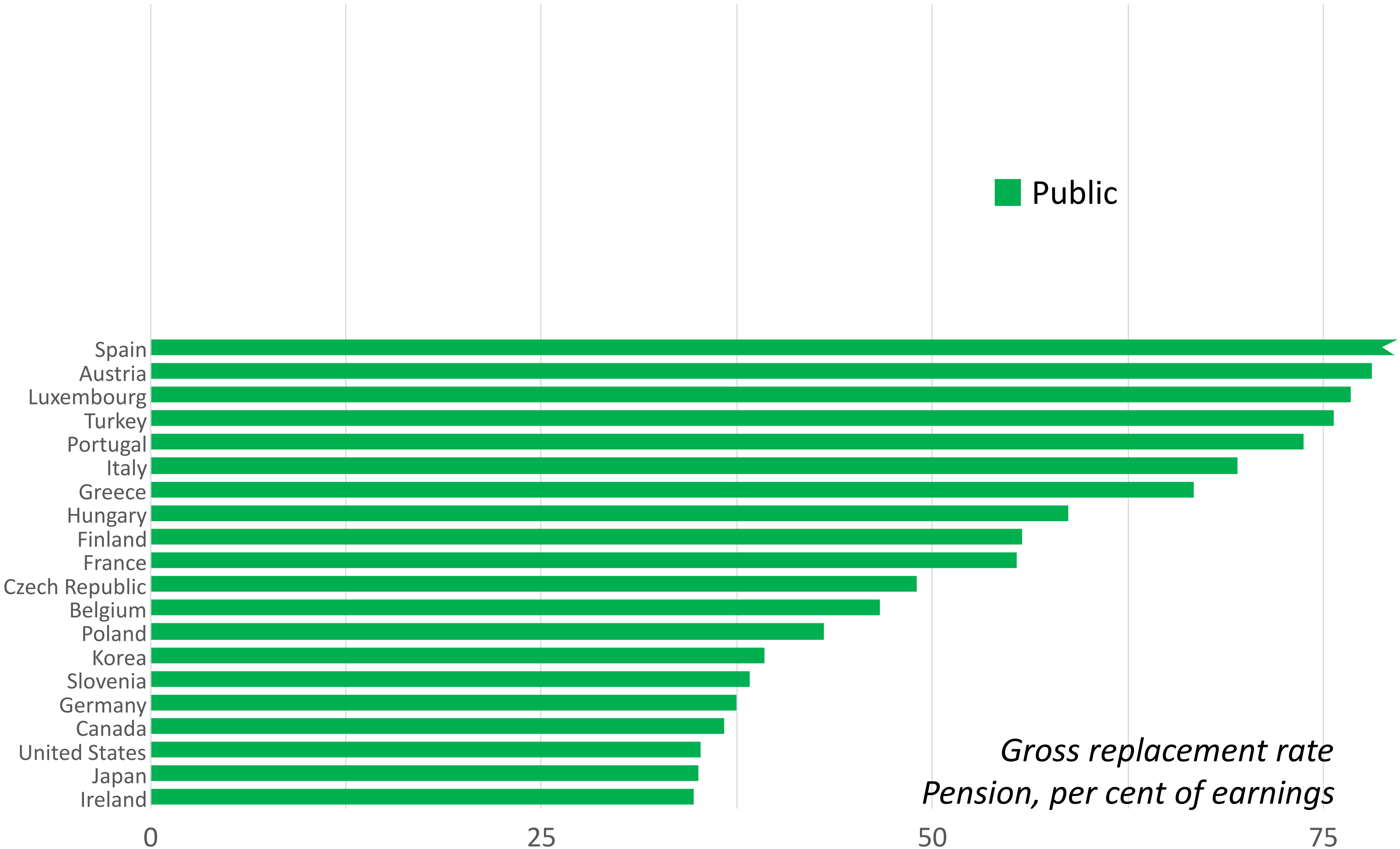
Role of private pensions

- Mandatory schemes
  - defined-contribution in Australia, Chile, Denmark, Estonia, Mexico, Norway, Slovak Republic, Sweden
  - defined-benefit in Iceland, the Netherlands and Switzerland
- ‘Soft compulsion’ or automatic enrolment
  - New Zealand, United Kingdom and some US states
- Widespread voluntary coverage
  - in Canada, Czech Republic, Germany, Ireland, United States
  - supported by tax incentives or matched contributions

Pensioner income sources

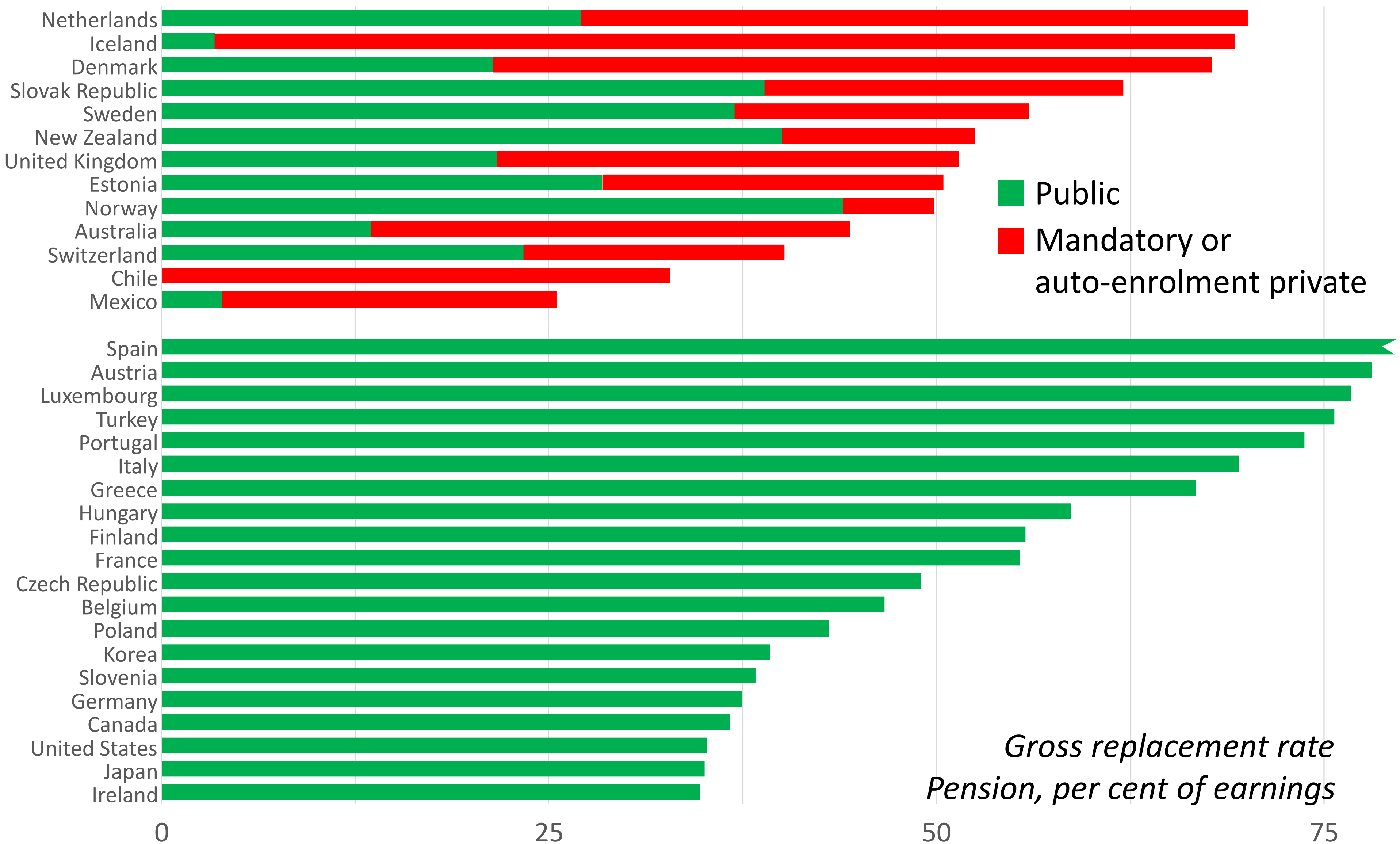


Public pensions

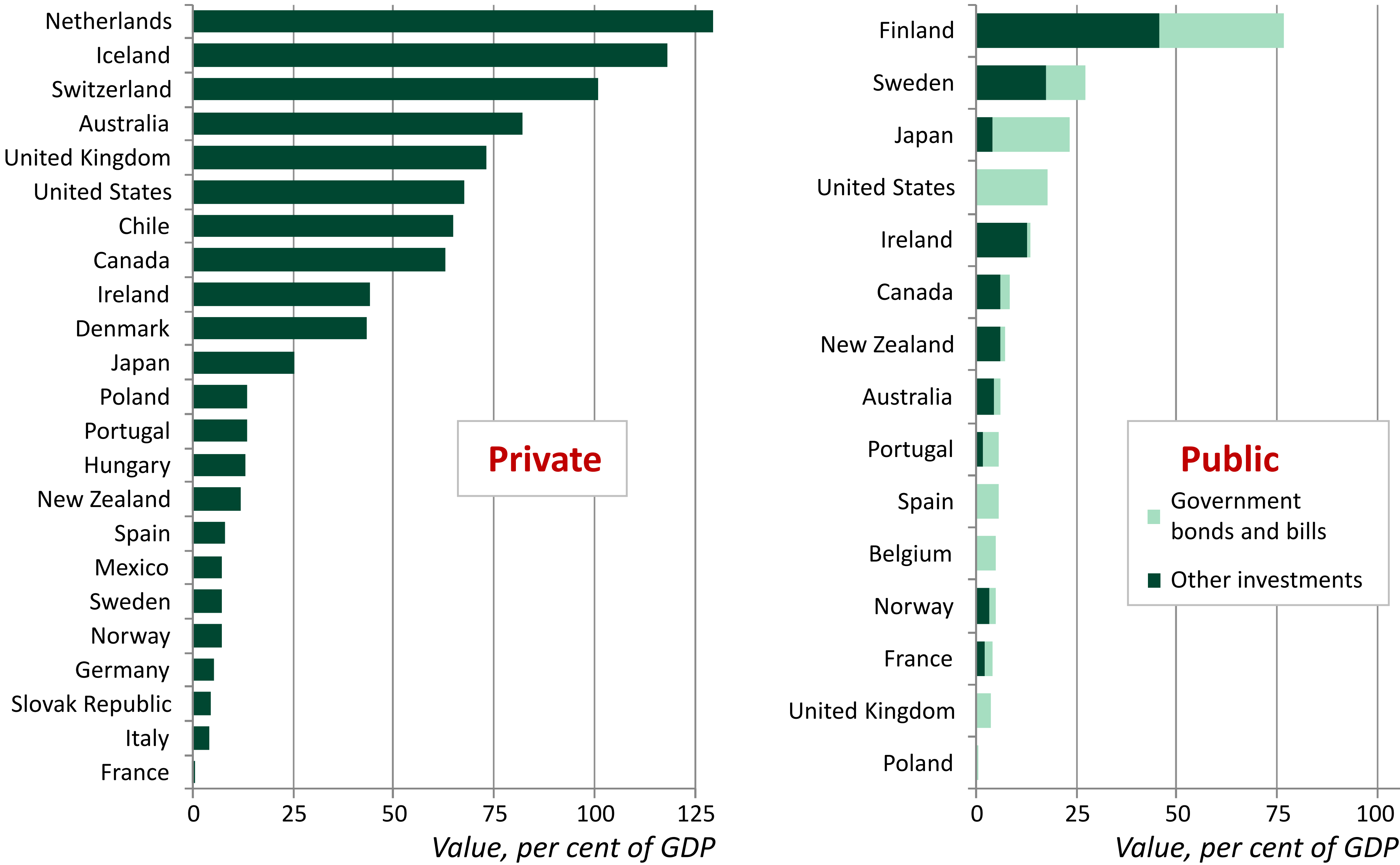


Public and private pensions

Public and private pensions



Assets: private plans and public reserves



Security through diversity

- ‘It is the part of a wise man to keep himself today for tomorrow, and not venture all his eggs in one basket’ (Miguel de Cervantes, 1605, *Don Quixote*)
- Pay-as-you-go public pensions:
  - sustainable rate of return = earnings growth + employment growth
- Funded pensions
  - rate of return in capital market directly or indirectly affects pension value
- Think of pension package as a ‘portfolio’ of different ‘assets’

Conclusions

- Two key objectives for the pension system
  - adequacy of benefits (or social sustainability)
  - financial sustainability needed to ensure pension promises can be delivered
- Balancing the two is the key challenge
- Need for longer working lives
- But fiscally necessary cuts in public benefits leaves pension gaps
- These can be filled by greater private pension saving
- Greater diversity means better, safer pensions
- But public schemes must leave space for private plans to develop