

*Have we
averted the
old age crisis?*

7TH INTERNATIONAL PENSION RESEARCH ASSOCIATION (IPRA) CONFERENCE
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Origins of Averting

- ▶ Growing awareness of problems with maturing DB schemes
 - ▶ “Reforming Public Pensions” OECD (1988)
 - ▶ “Ascent into Bankruptcy: Social Security in Latin America”, Mesa-Lago (1989)
- ▶ Australia, Colombia and Peru introduce mandatory, privately-managed DC schemes in 1992-1993
- ▶ Limited World Bank involvement in pensions until entrance of high pension spending clients in Eastern Europe and the FSU
- ▶ Larry Summers enters as Chief Economist in 1991 steeped in three decades of academic pension economics literature
- ▶ Team led by Estelle James was oriented towards macro/fiscal and financial sector issues

Basic Message of Averting—pre-fund saving part of old age system and make redistribution more transparent

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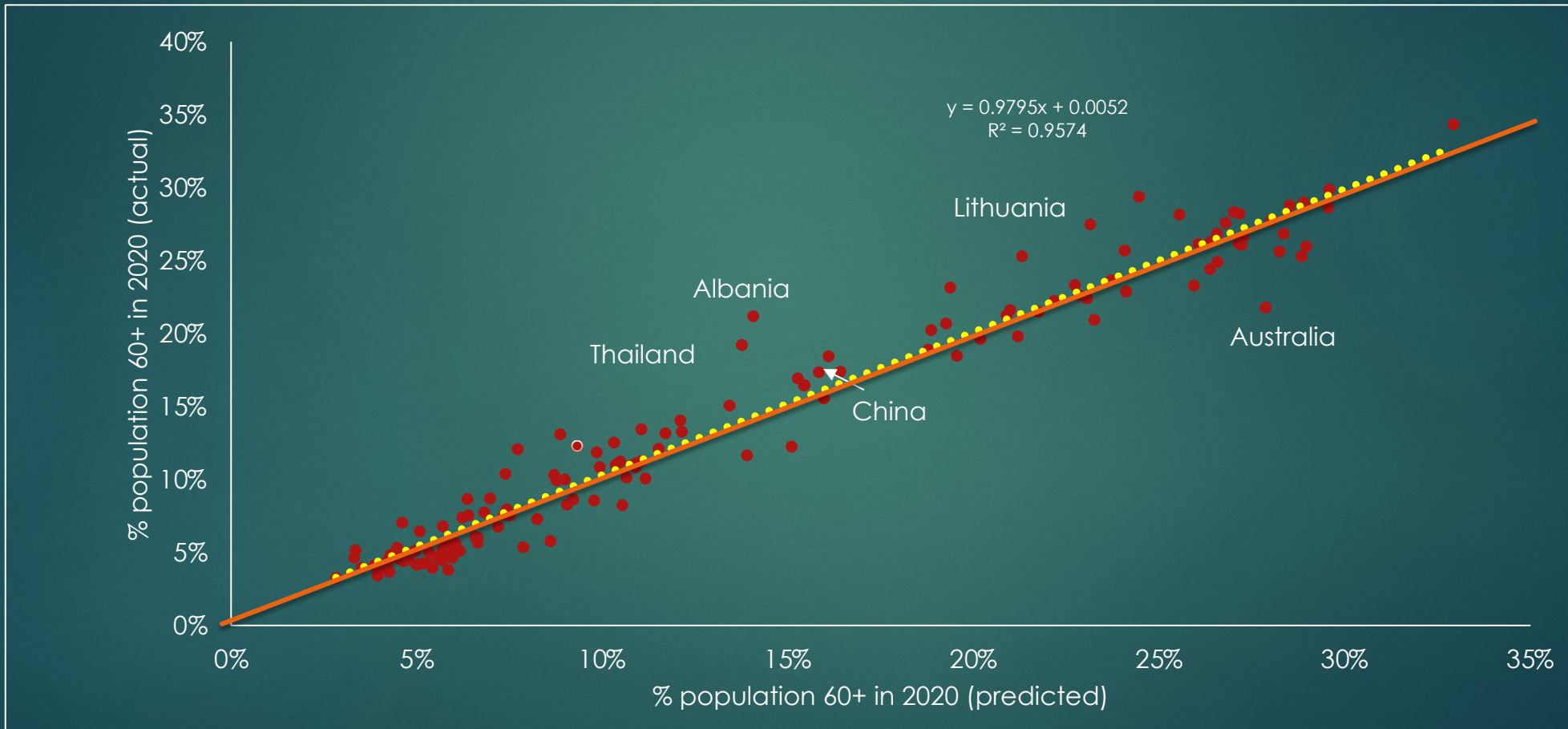
- ▶ Old age programs have 2 objectives:
 - ▶ Saving--getting people to save when young so they have enough money to live on when old
 - ▶ Redistribution--to prevent poverty and help those with low lifetime incomes to live with dignity
- ▶ In most systems, these 2 objectives were mixed in a DB pension and financed by a payroll tax on a PAYG basis. PAYG required increasingly high tax rates as old age dependency rates rose. High costs hurt public treasury, worker take-home pay, saving, work incentives & economic growth. DB often intro. non-transparent undesired redistributions.

*** This slide was presented by Estelle James at the conference for the 20th anniversary of Averting**

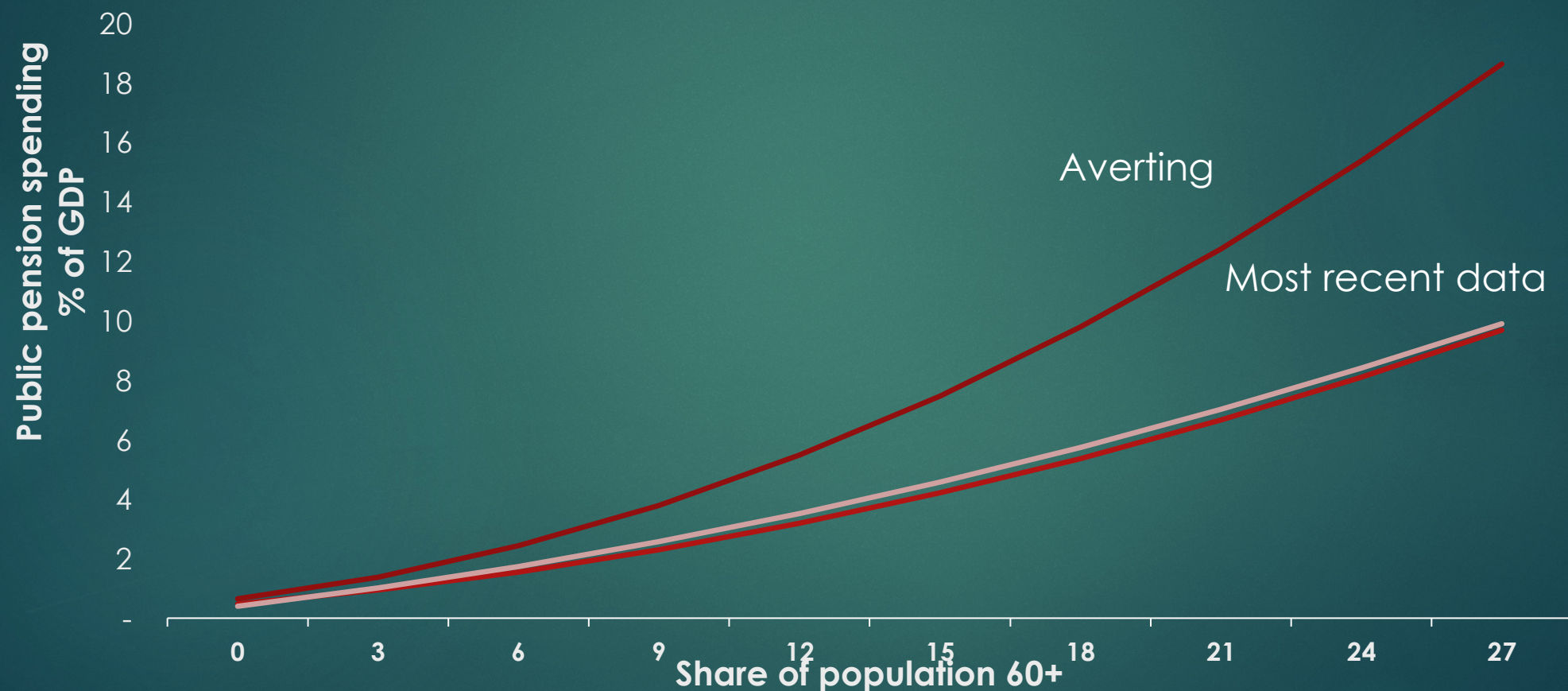
What happened in the next thirty years?

- ▶ Population aging took place, mostly as expected
- ▶ There was a wave of parametric reforms
- ▶ The role of DC schemes grew globally
- ▶ The focus shifted from DB/DC, PAYG/FF to coverage

Countries aged as expected (mostly)



Despite aging, pensions became more financially sustainable...



...reflecting parametric reforms in most OECD countries

The main elements of pension reform packages in selected OECD countries

	Parametric						Systemic		
	Pension age		Retirement incentives	Calculation		Indexation	DC	NDC	Life Expectancy
	M	F		measure	revaluing				
Austria	●	●	●	●		●			
Finland			●	●	●	●			●
France			●	●	●				●
Germany			●						●
Hungary	●	●	●	●		●	●		
Italy	●	●	●			●		●	
Japan	●	●		●					
Korea	●	●							
Mexico							●		
NZ	●	●							
Poland			●	●		●	●	●	
Portugal		●	●	●	●	●			●
Slovakia	●	●		●			●		
Sweden				●			●	●	
Turkey	●	●							
UK		●	●						

Note: Includes only 16 countries that have had major reforms since 1990.

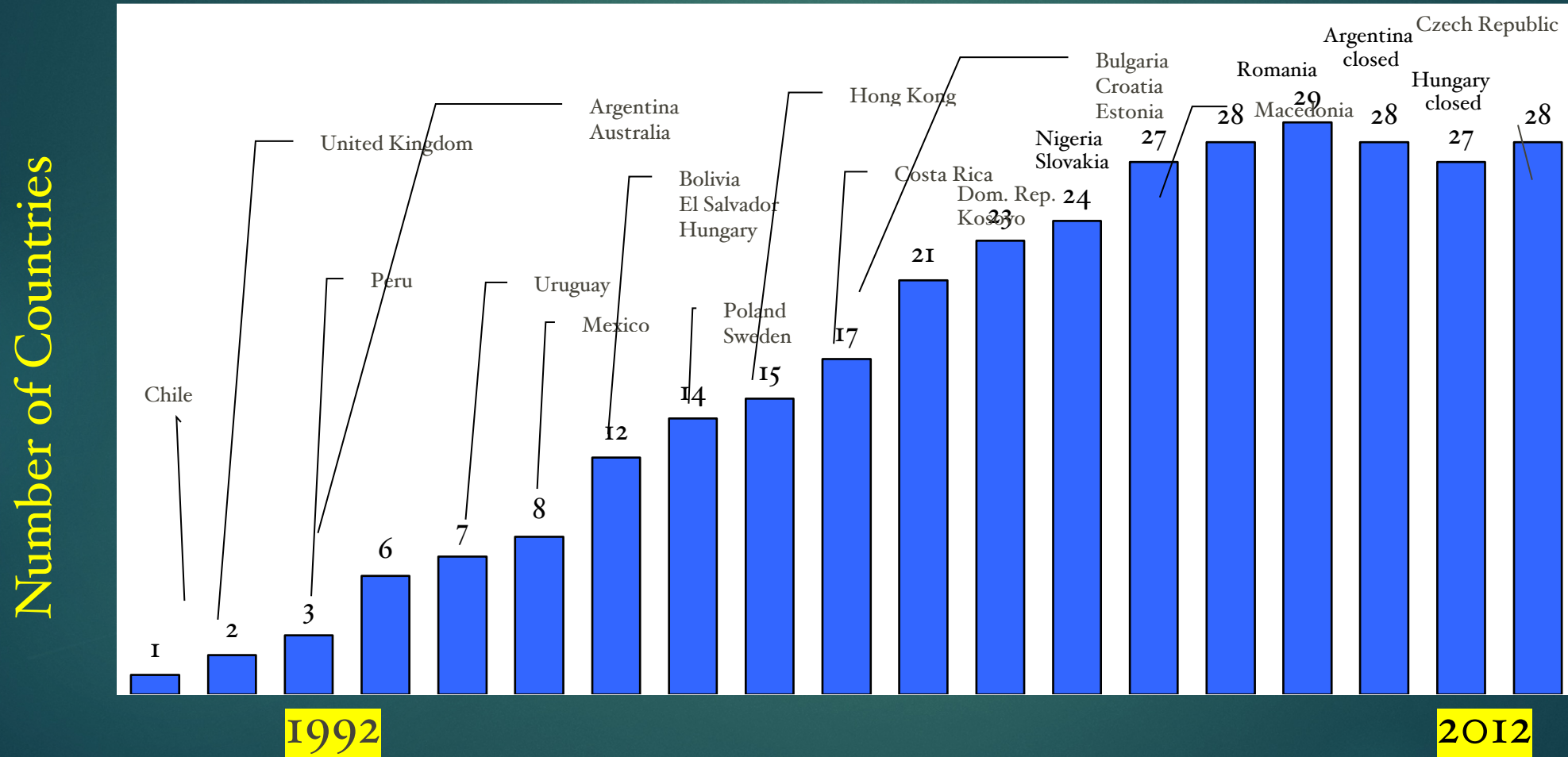
Source: OECD *Pensions at a Glance*

...and many in non-OECD countries

- ▶ Between 1995 and 2018*
 - ▶ 78 countries raised their contribution rates
 - ▶ 55 increased their retirement ages
 - ▶ 61 modified their DB formula
- ▶ New DB schemes tended to have lower target replacement rates (e.g., Cambodia, Indonesia)
- ▶ Most of the World Bank's technical assistance after Averting focused on parametric reforms

* Source: FIAP (2019)

In parallel, many countries added DC elements to mandatory schemes



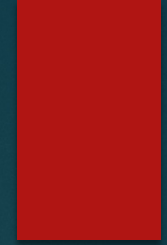


Table 1. Pension privatization and reform reversals in Eastern Europe.

Country	Pension privatization	Reform reversal
Hungary	1998	Dismantling, 2010
Poland	1999	Dismantling 2014, 2019
Latvia	2001	Scale-down, 2009
Bulgaria	2002	Scale-down and Back-to-PAYG Option, 2011
Croatia	2002	Back-to-PAYG Option 2011, 2019
Estonia	2002	Scale-down and Voluntary participation 2020
Lithuania	2004	Scale-down 2009, Carve-out eliminated in 2019
Slovakia	2005	Scale-down and Back-to-PAYG Option, 2009
N. Macedonia	2006	Scale-down 2014, Back-to-PAYG Option 2019
Romania	2008	Scale-down and Voluntary participation 2018
Czech Republic	2013	Dismantling, 2014

Source: Authors' compilation based on official reports. For more details on reform reversals, consult Ortiz et al. (2018), Altiparmakov (2018a), Bielawska et al. (2016), Schwartz and Arias (2014), Guardiancich (2013). Estonia is the only country that did not rely exclusively on carve-out financing but has supplemented the carve-out contributions (4% of earnings) with additional employee contributions (2% of earnings).

But the expansion of DC schemes stalled and, in some cases reversed, due to poor implementation, fiscal pressure and the 2008 financial crisis

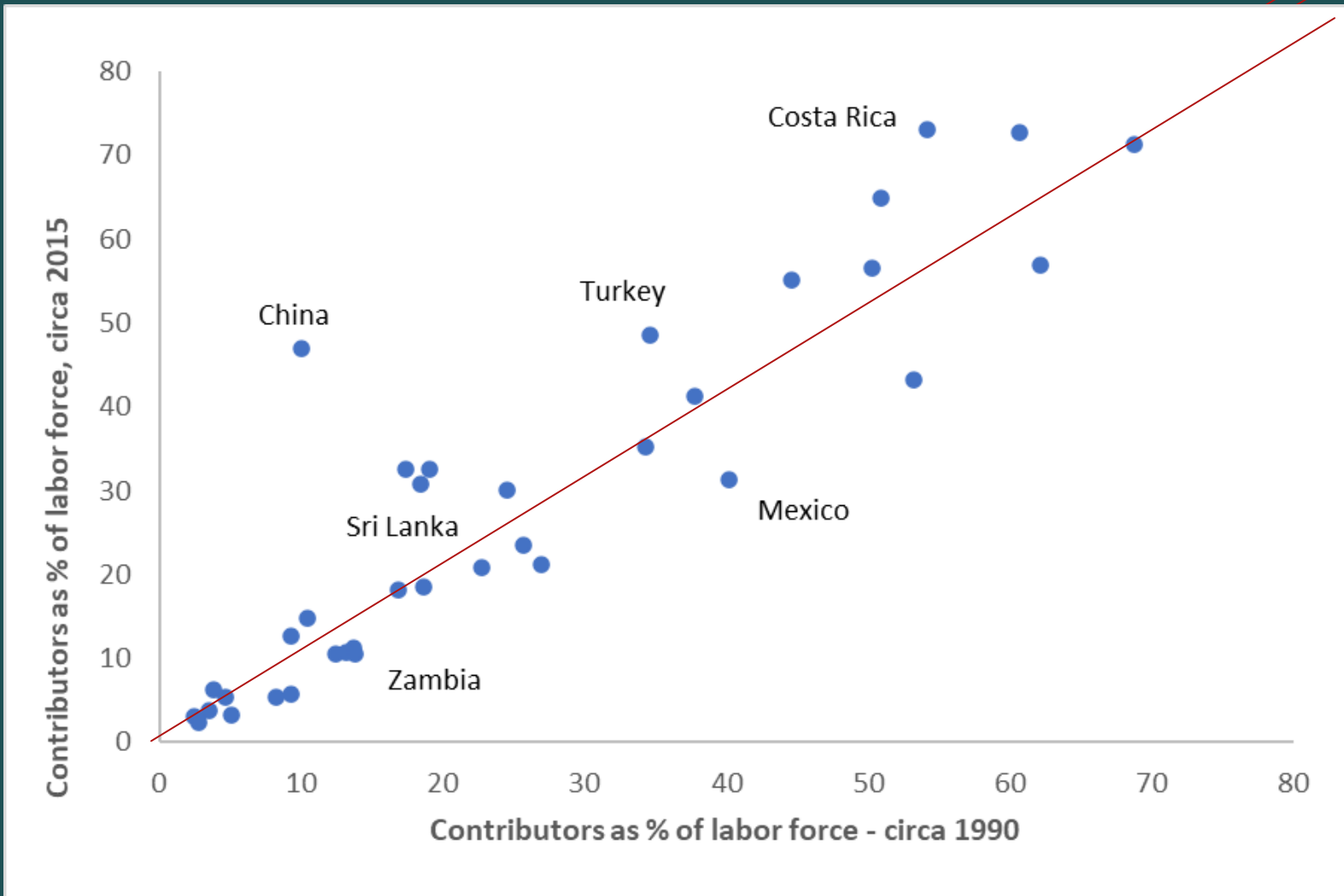
Protests, December 2017

Greece cuts nominal
pensions

Chilean replacement
rates below expectations



The focus shifts from pension 'model' to the problem of persistent informality

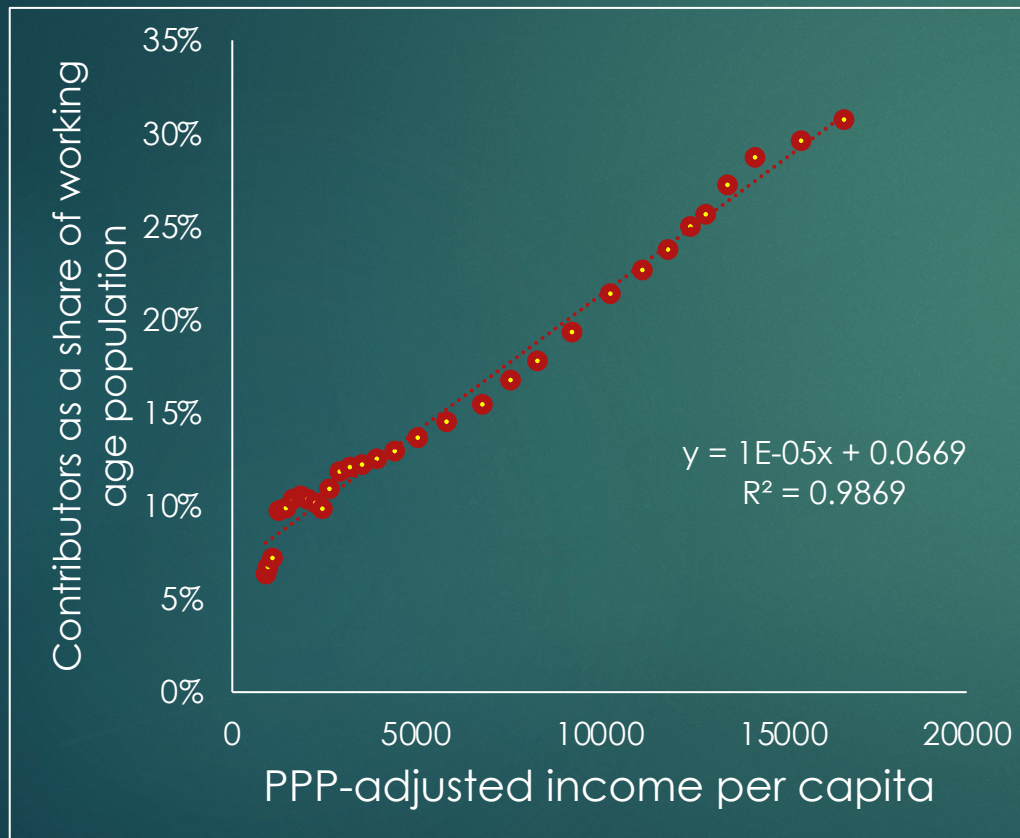


While a few countries have achieved significant coverage increases, these are in the minority – China stands out

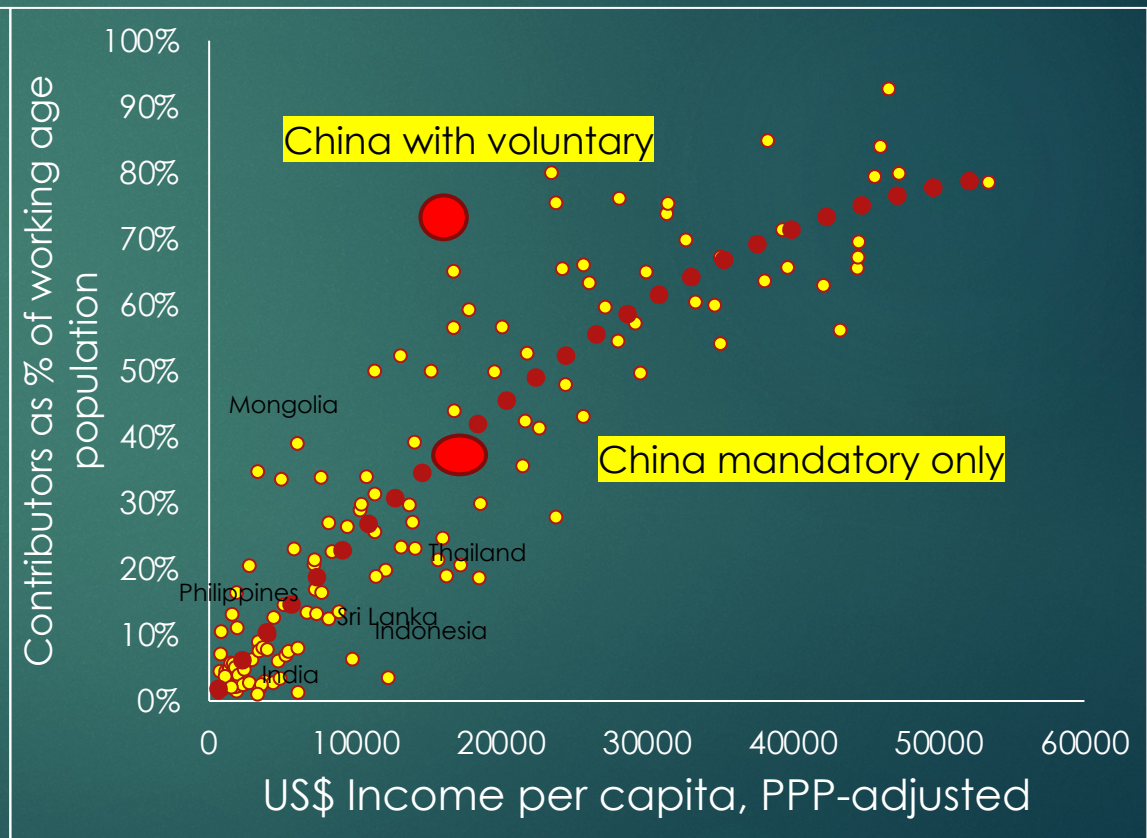
Two policy responses are emerging and China does both

Even China with its 10-fold income increase since 1990 has resorted to voluntary pensions

China coverage and income per capita: 1989-2019

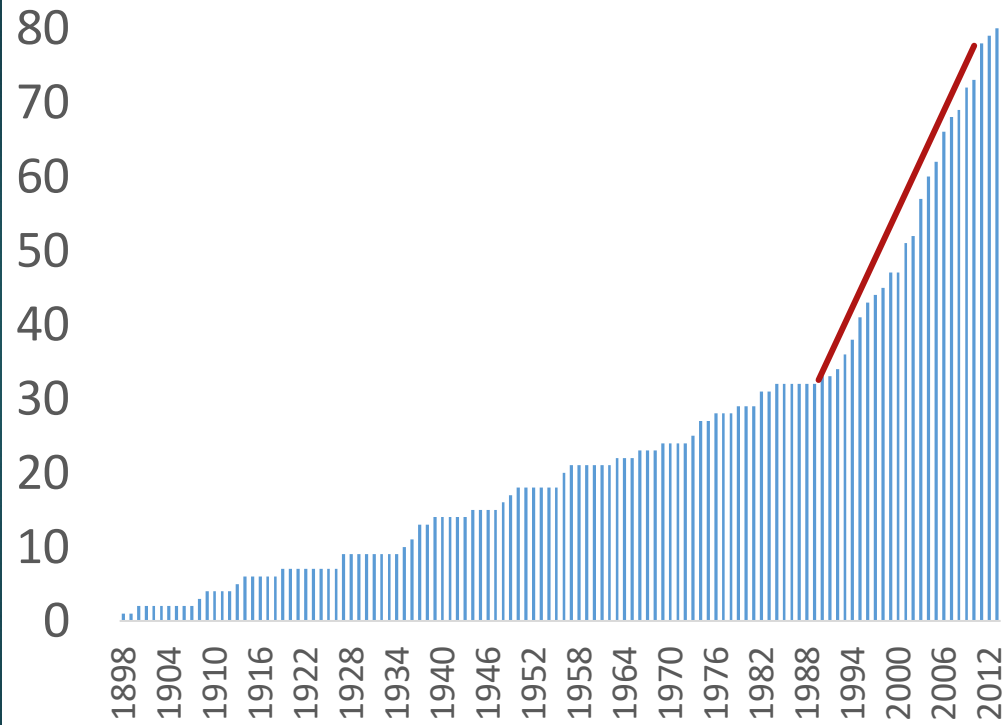


China coverage with and without voluntary scheme

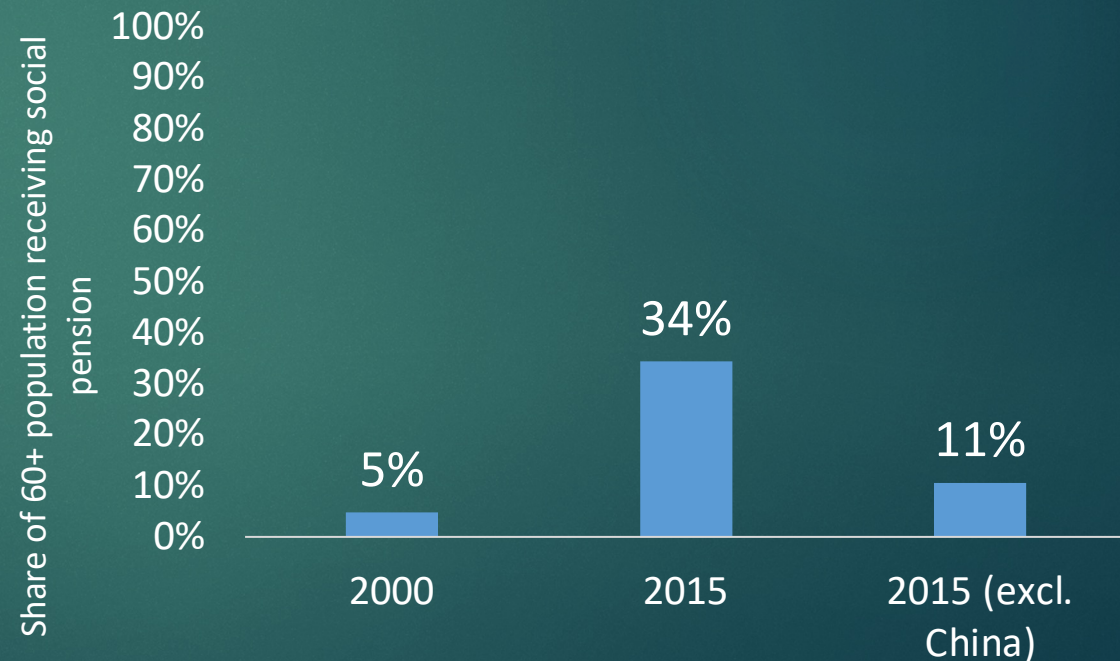


...and, along with dozens of other countries, China expands social pensions

Number of countries with social pensions



Share of elderly in low and middle income countries receiving social pensions



So has the crisis been averted? *No.*

- ▶ Averting's diagnosis of the need for parametric reforms has been validated by a wave of parametric reforms, but many DB schemes are still headed for deficits in the long run
- ▶ Even well designed DC schemes have not succeeded in the context of persistent informality and low contribution densities
- ▶ And the potential positive impact of funding has been lost when the transition is debt financed
- ▶ Meanwhile, persistent informality means that any model that relies on formal labor market status is doomed to fail
- ▶ The two policy responses emerging are social pensions and schemes for informal sector workers but most social pension levels are inadequate and voluntary schemes have had limited take up (except in China) and both require a large fiscal commitment

Concluding thoughts on Averting

- ▶ Was in many ways the starting point for the international pension policy debate since the mid-1990s
- ▶ Made a strong case for reforming PAYG DB schemes and encouraged parametric reforms
- ▶ Encouraged the adoption of DC schemes but the way they have been implemented has disappointed
- ▶ Recognized the role of a general revenue financed, redistributive element in the pension system but did not anticipate the importance of social pensions and voluntary contributions in the context of persistent informality