

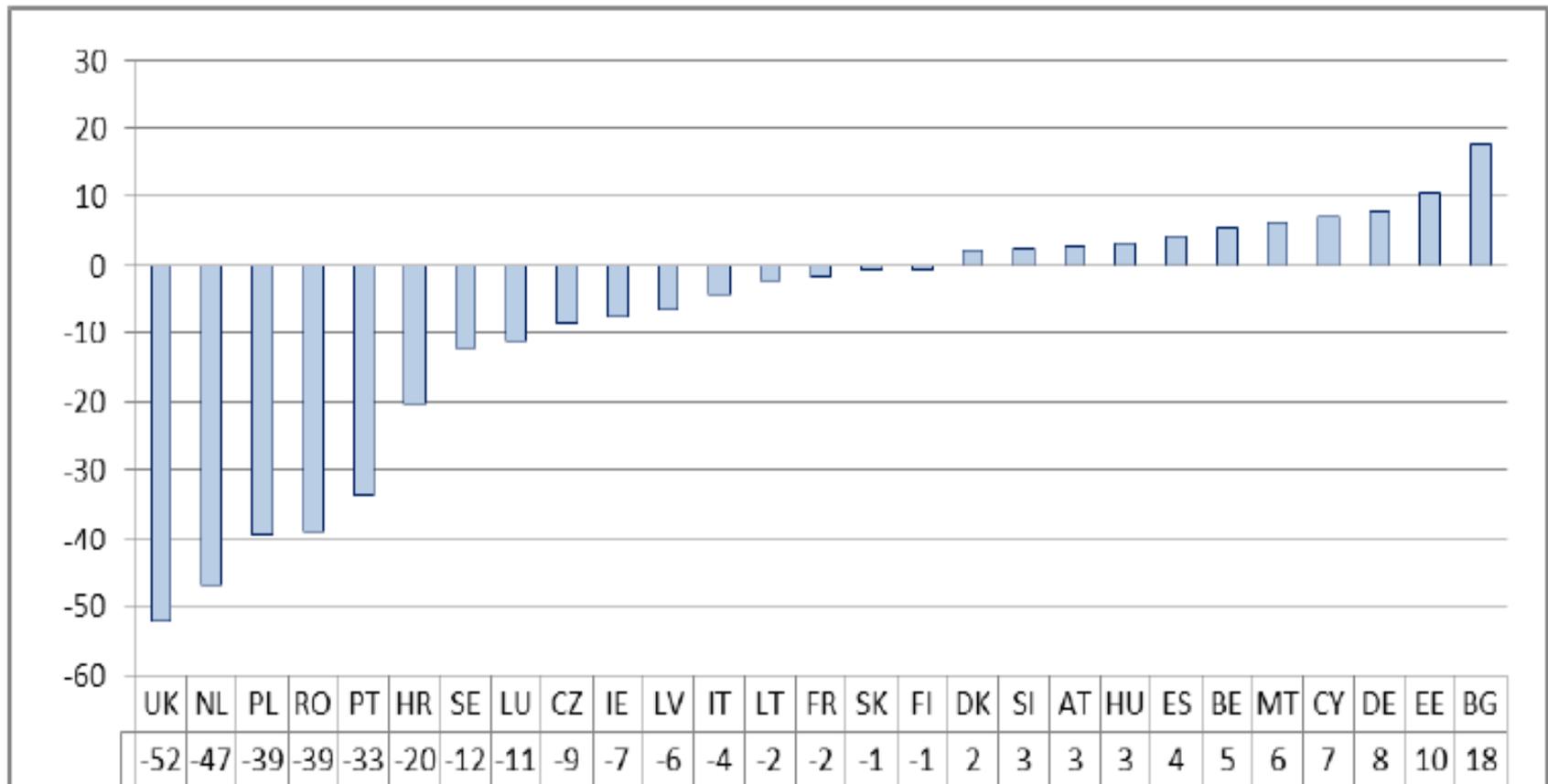
Financial and social sustainability of pension systems

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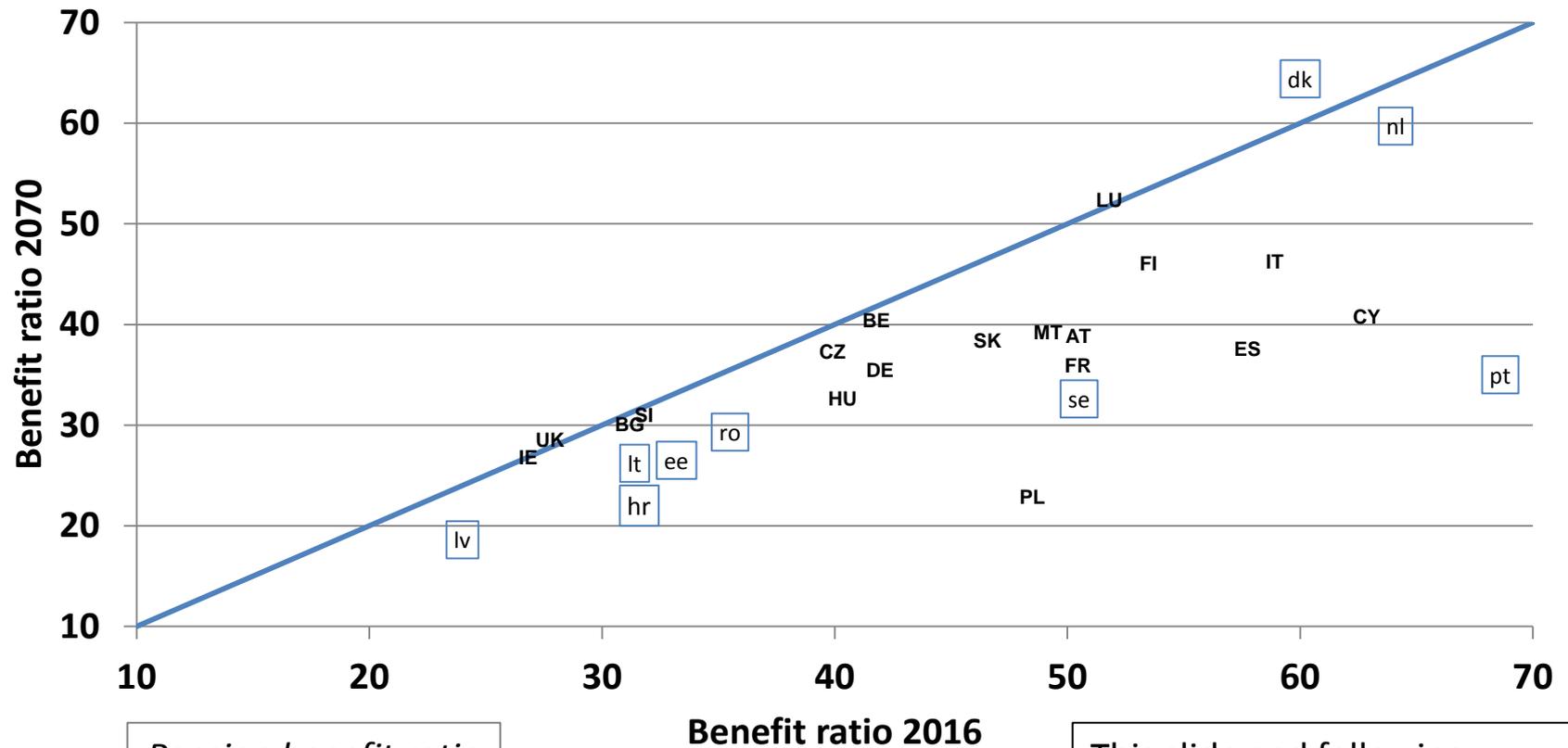
Brussels, 2 July 2018

Declining Theoretical Replacement Rates (TRR), notably on the basis of Average Work Duration (AWG)

Figure 64: Net TRR, AWG case, men, average earner, p.p. change, 2016-2056



Change in pension benefit ratios, incl. private pensions (□) (includes composition effects)

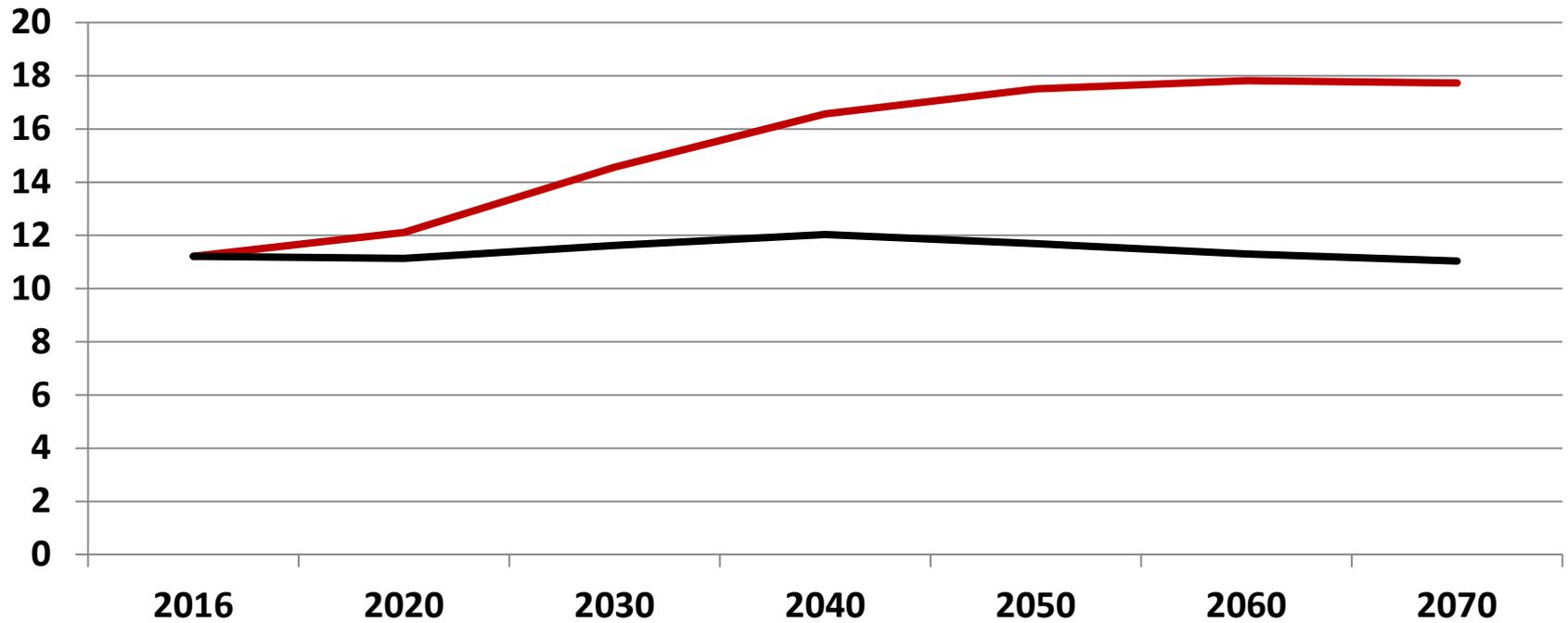


$$\text{Pension benefit ratio} = \frac{\text{average pension}}{\text{average wage}}$$

— No change (Musgrave rule)

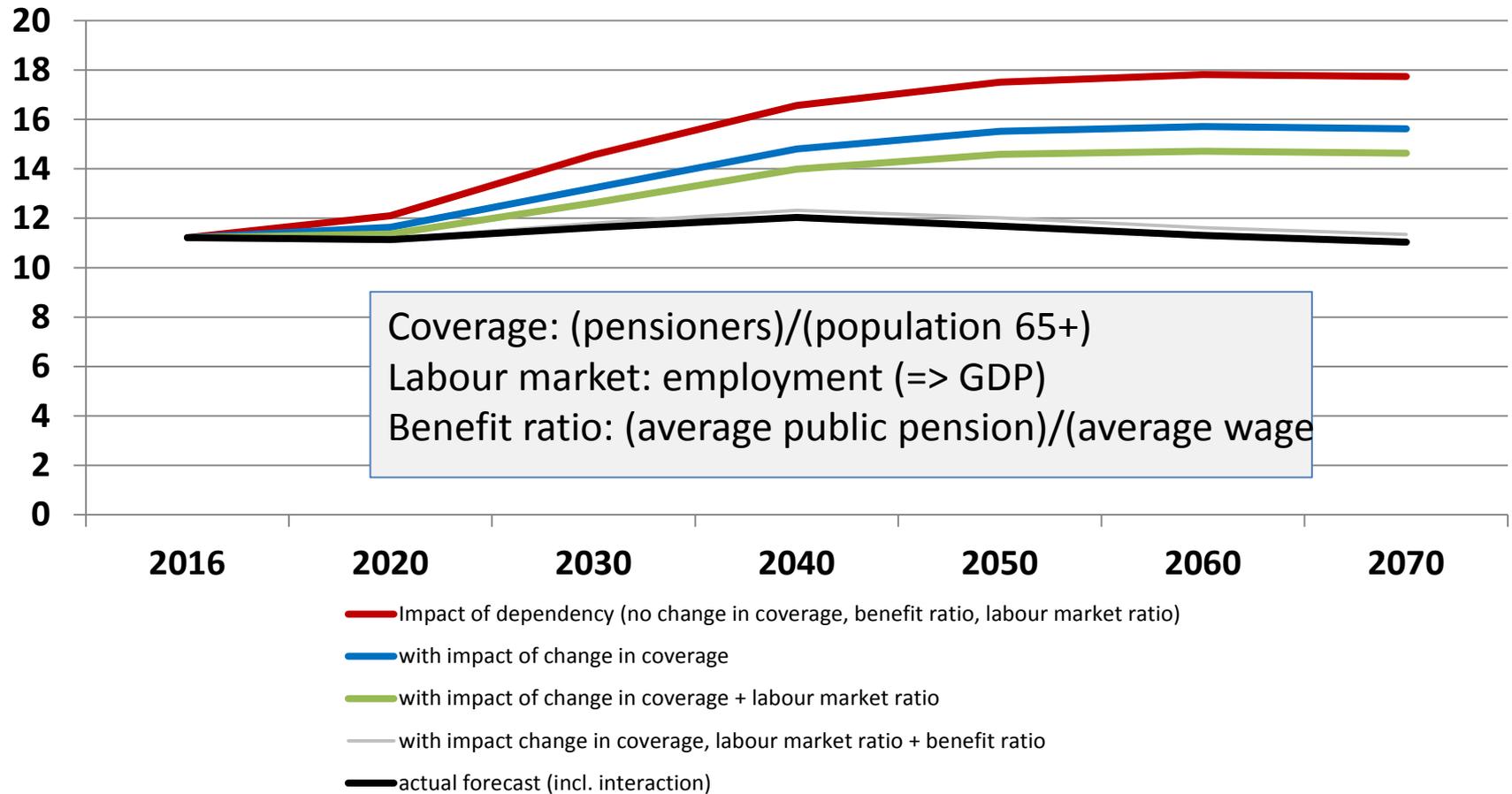
This slide and following slides: data from *Ageing Report 2018*

Public pension spending, % GDP, EU

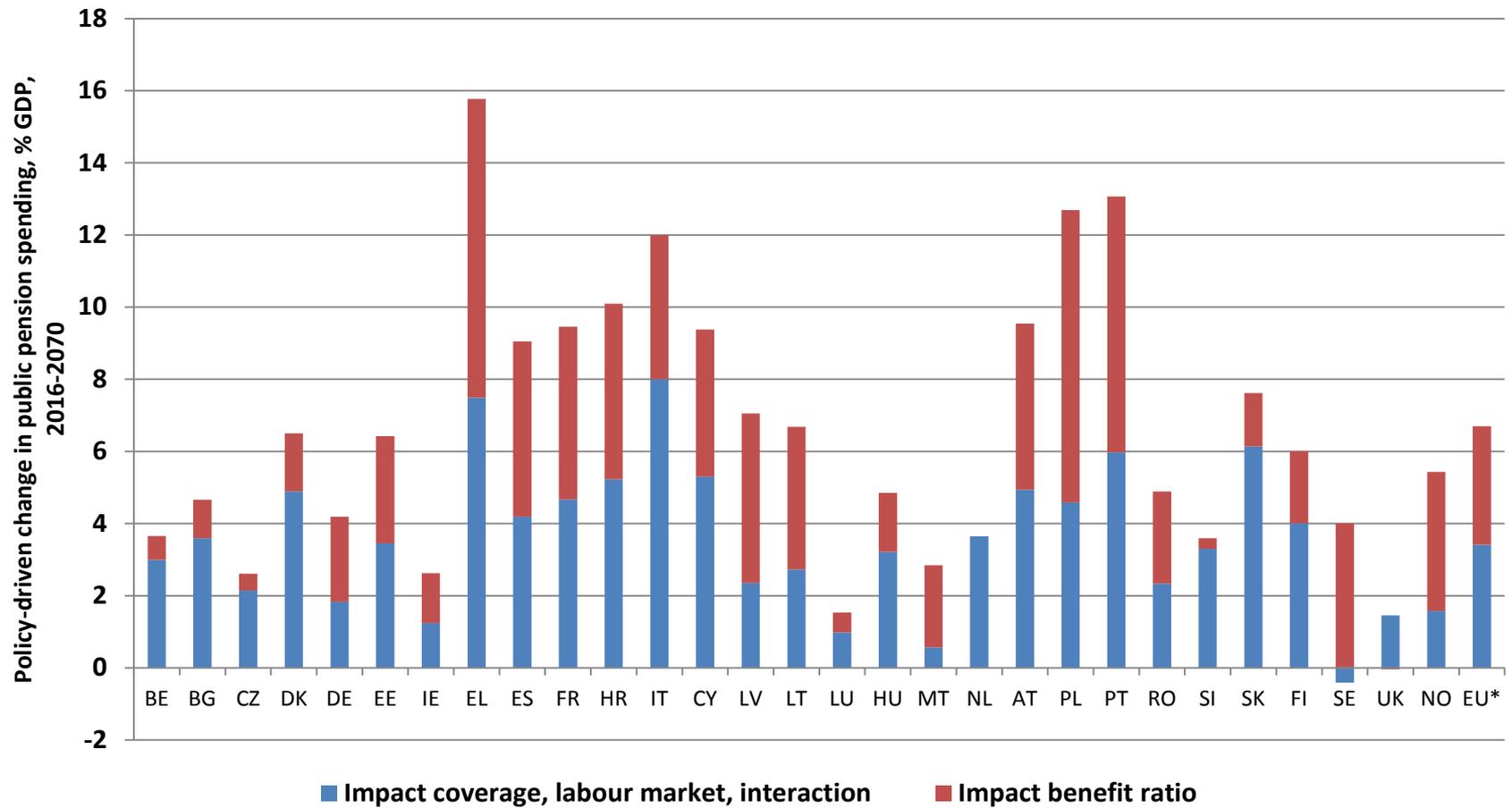


- Impact of dependency (no change in coverage, benefit ratio, labour market ratio)
- with impact of change in coverage
- with impact of change in coverage + labour market ratio
- with impact change in coverage, labour market ratio + benefit ratio
- actual forecast (incl. interaction)

Public pension spending, % GDP, EU, decomposed



Policy-driven change (*) in public pension spending 2016-2070: impact of change in benefit ratios



(*) ! Generous understanding of ‘policy’: change in coverage & labour markets = ‘policy’.
Decomposition *in Ageing Report* mixes policy and endogeneous developments.

Intergenerational risk sharing: the social contract

- Pensions = managing uncertainty
- Options for risk sharing

	Defined benefit	Defined contribution	Musgrave rule
Fix...	Pension	Contribution rate	(net) pension benefit ratio
Economic risk	Risk for workers	Shared risk	Shared risk
Demographic risk	Risk for workers	Risk for retirees	Shared risk

Pointers for policies to reconcile social and financial sustainability

- Pension policies
 - Long-term outlook is not reassuring in a number of EU Member States:
 - Decreasing benefit ratios and TRR
 - In most countries an increasing gap between the Standard Pensionable Age (SPA) and effective exit age => increasing coverage/adequacy risks
 - Social sustainability requires fair intergenerational risk sharing: ‘growth risk’ and ‘demographic risk’ should be neutralized in a fair pension contract.
 - Flexible retirement: length of career should be more important than age (compare Fig. 66 and 67 in Adequacy Report).
- Labour market policies
 - The importance of ‘access to social protection’ for *all* workers (European Pillar of Social Rights)

Resources

- European Commission & SPC, *Pension Adequacy Report 2018*
- European Commission, *The 2018 Ageing Report*
- Musgrave rule: see Myles, 'A New Contract for the Elderly', in Esping-Andersen, *Why we need a New Welfare State*, OUP, 2002.
- Application of Musgrave rule: see Erik Schokkaert, Pierre Devolder, Jean Hindriks, Frank Vandembroucke, Towards an equitable and sustainable points system. A proposal for pension reform in Belgium, *Journal of Pension Economics and Finance*, First View, 27 April 2018, pp. 1-31.
<https://doi.org/10.1017/S1474747218000112>
- Belgian Commission on Pension Reform 2020-2040
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