

Aging, the Future of Work and Sustainability of Pension System

WKÖ & Salzburg Global Seminar Event

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Agenda Austria | Vienna, Austria

November 5, 2015



Introduction

- Increasing pressure on the pension system because of the demographic trends
 - Rising life expectancy, low fertility rate, changes in the relative cohort sizes

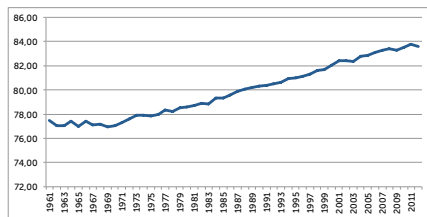


Figure: Life expectancy of a 60-year old person in Austria

- Increasing dependency ratio

The Austrian Pension System

■ Formula 45/65/80

- After 45 years of insurance, at the retirement age of 65 years, 80% of average lifetime income is guaranteed
- Yearly 1.78% of total earnings are credited to the personal notional account
- Early/late retirement between 62 and 68 years (with 37.5 years of insurance)
- Pension contributions adjusted by the growth rate of the average wages, existing pensions by the inflation
- **No automatic adjustment mechanism to demographic changes**

Balanced Pension System

- No adjustment \Rightarrow unbalanced pension system

Total Contribution + Government Contribution = Total Expenses

$$\tau_t * W_t * L_t + B_t = P_t * R_t$$

- Possibilities for an adjustment: higher contribution rate (τ), lower pension (P), higher government contribution (B), higher (effective or statutory) retirement age - or a combination of these.

Demographic Effects in Austria

- Possible corrections on fiscal sustainability of the Austrian pension system and their effect
- Three scenarios
 - No correction: basic model based on the long-term forecasts of Austrian Pension Commission
 - Solely correction over the effective retirement age: yearly increase by one, two and three months
 - Correction over effective and statutory retirement age: simultaneous yearly increase by one, two and three months

Results: Basic Model

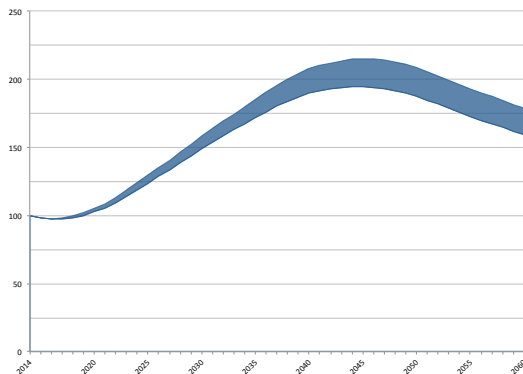


Figure: Government contribution as a percent of the GDP (Index, 2014=100)

Results: Correction over the Effective Retirement Age

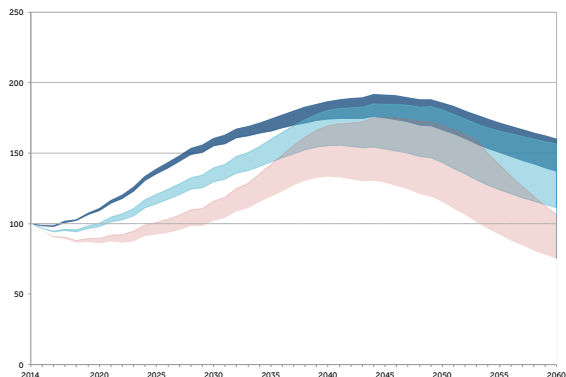


Figure: Government contribution as a percent of the GDP (Index, 2014=100)

Results: Correction over the Effective and Statutory Retirement Age

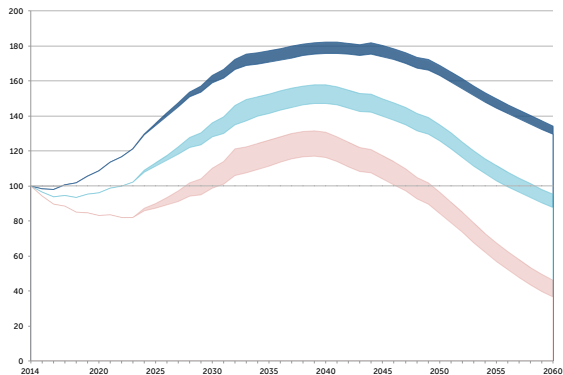


Figure: Government contribution as a percent of the GDP (Index, 2014=100)

International Comparison

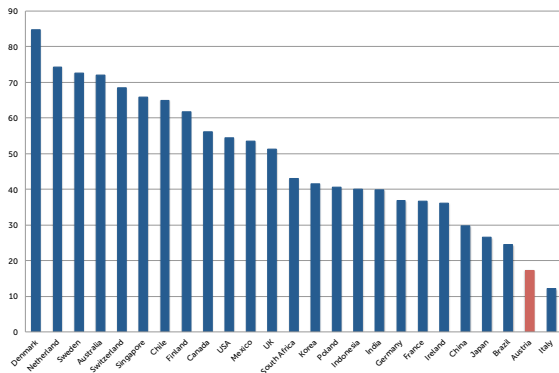


Figure: Sustainability Sub-Index Values of the Mercer Pension Index (2015)

How do other EU countries control for increasing life expectancy?

- **Sweden:** Contributions paid into a personal notional account. Flexible retirement between 61 and 69 years. The annual pension at the time of retirement is a fraction of the accumulated capital and the remaining life expectancy.
- **The Netherlands:** Statutory pension age increased to 67 years until 2023. Thereafter adjusted by the increase of the life expectancy.
- **Denmark:** Semi-automatic mechanism from 2027 on. The statutory retirement age linked to life expectancy at age 60 with a five-year lag between the time of the change in life expectancy and the adjustment of the pension age.

Summary

- Demographic changes affect pension systems significantly
- A correction over the increase of effective retirement age might not stabilize the pension system
- Automatic adjustment of the statutory retirement age by the increase of the life expectancy is recommended
 - Austria: adjustment of Formula 45/65/80 - **constant relationship between the years of contributions and the expected years in pension**
- Cohort effects can also unbalance the pension system. Validation over the growth rate of the total wages might bring a fairer cost redistribution over generations