



NUI Galway
OÉ Gaillimh

The Other Crisis: Whither Irish Pensions?

John McHale, NUIG

DEW Conference,
November 2

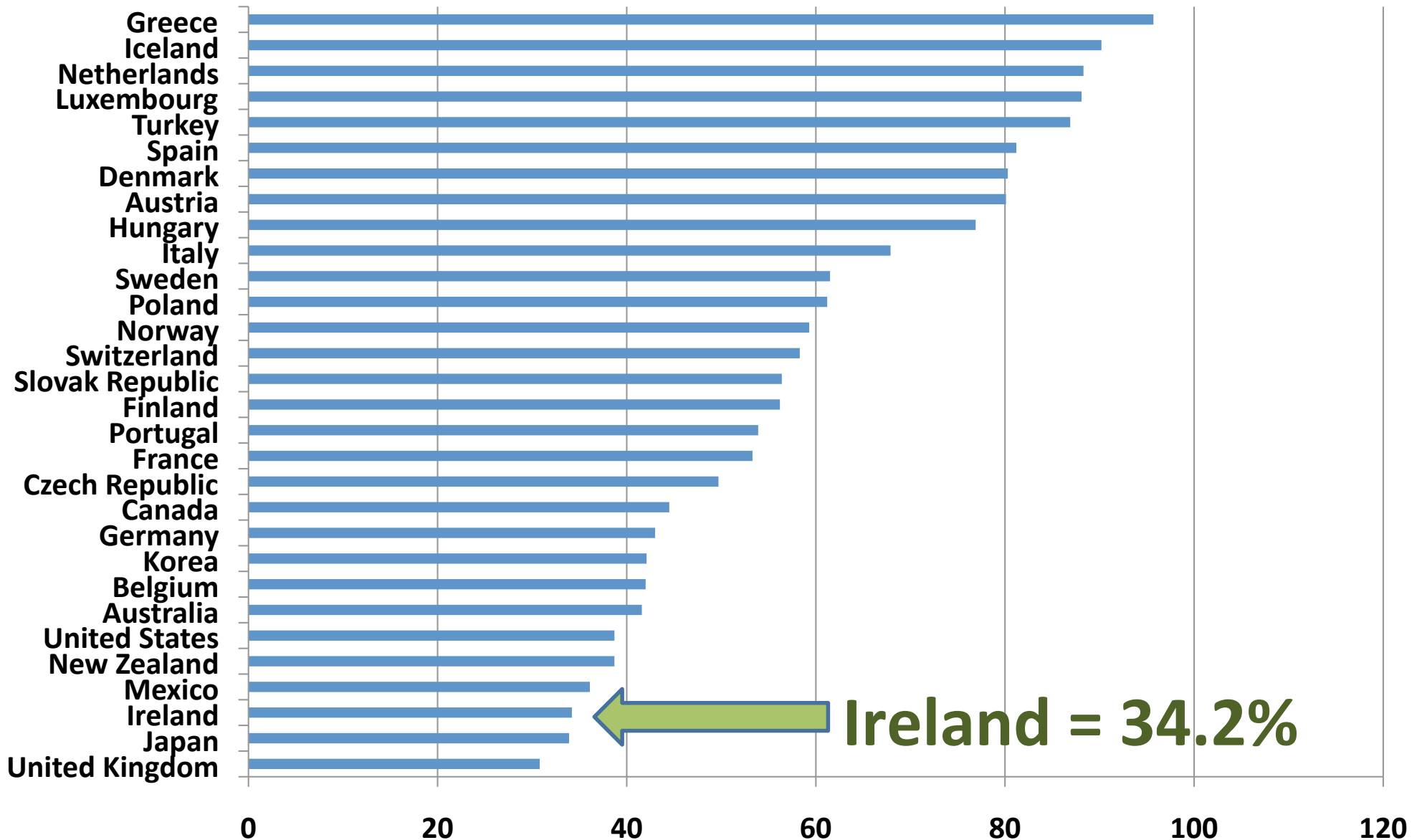
The Irish Pensions System

- Flat-rate social welfare pension
 - €230.30 (Contributory)
 - (Largely) unfunded
 - Pure tax
- Tax-favoured, voluntary supplementary pensions
 - Tax relief at marginal rate
 - Predominantly occupational pensions (DB); but shift towards private pensions (DC)

The slow-burning crisis

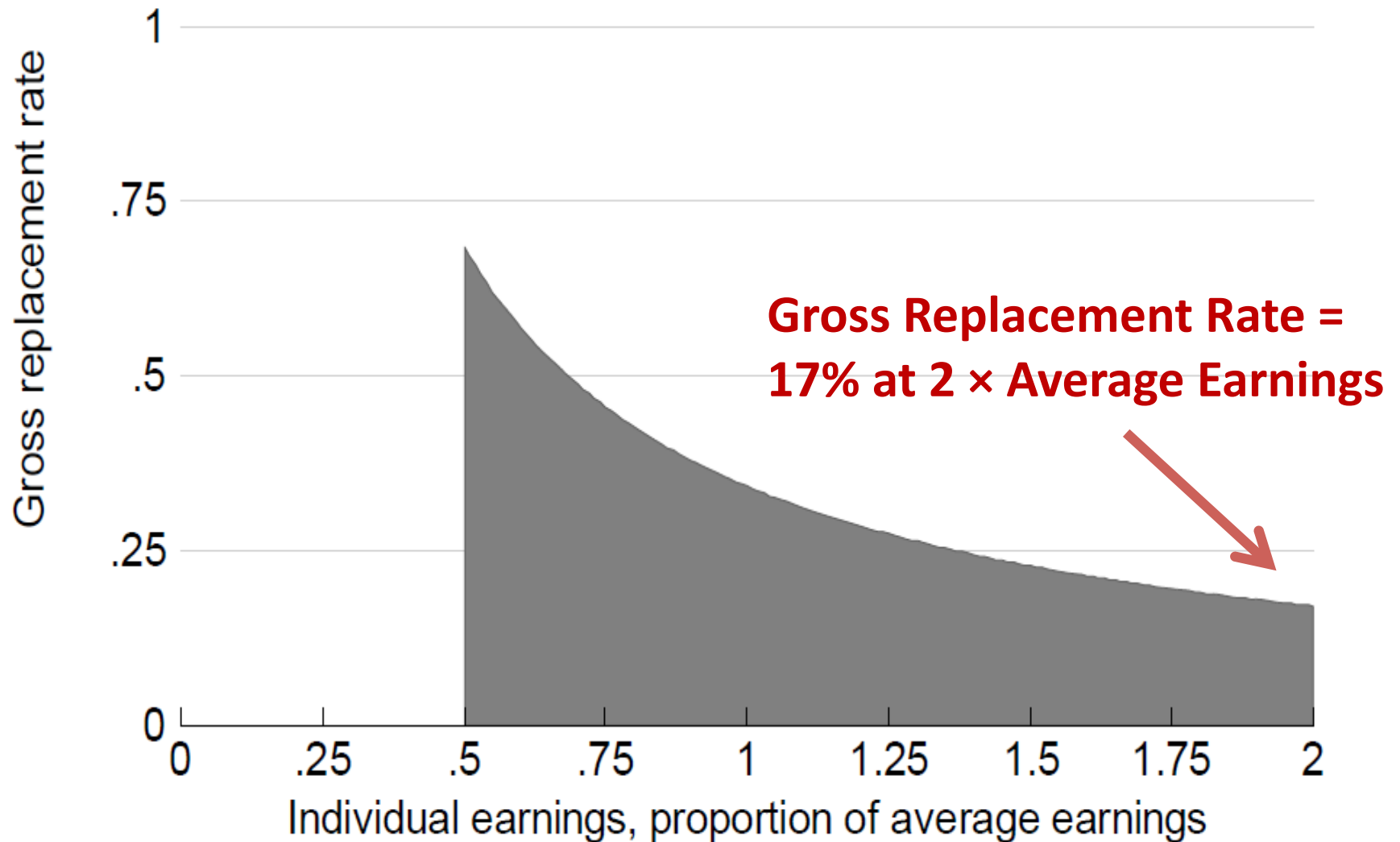
- Inadequate replacement rates from the state pension
- But still facing escalating cost due to population ageing
- Inadequate/insecure supplementary coverage

Low replacement rates at average incomes



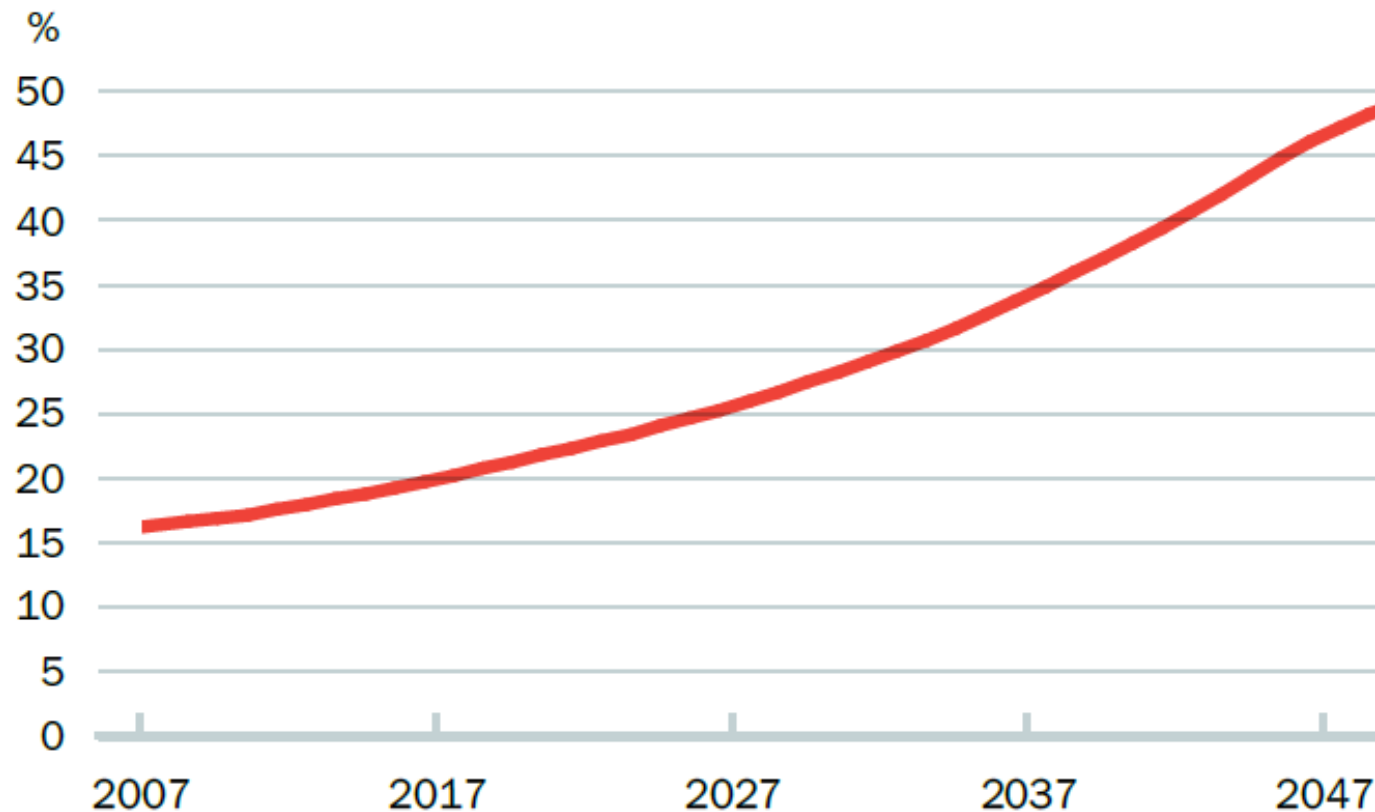
Source: OECD, Pensions at a Glance, 2009

Lower replacement at higher incomes



Population ageing → escalating cost

Projected Old Age Dependency Ratio

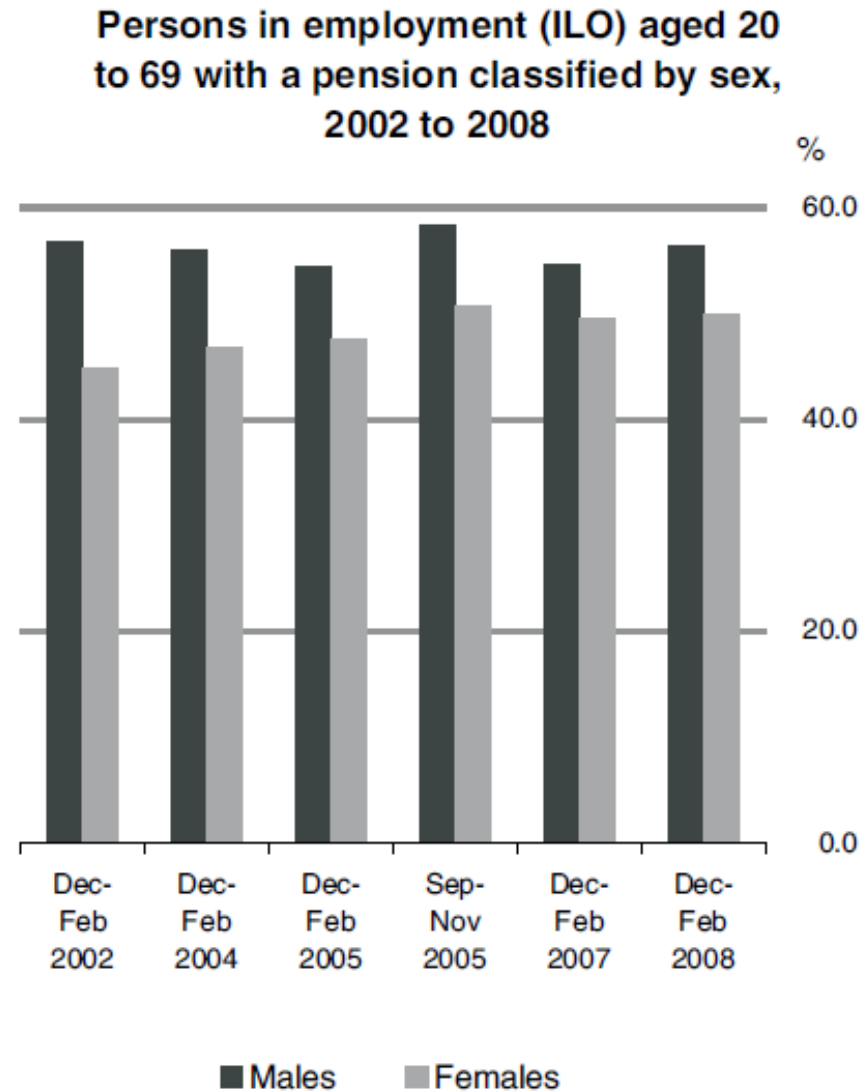


Definition: Population aged 65+ as a % of the population aged 15-64

Source: Green Paper on Pensions 2007

NPRF Commission, Annual Report 2008

Inadequate private provision

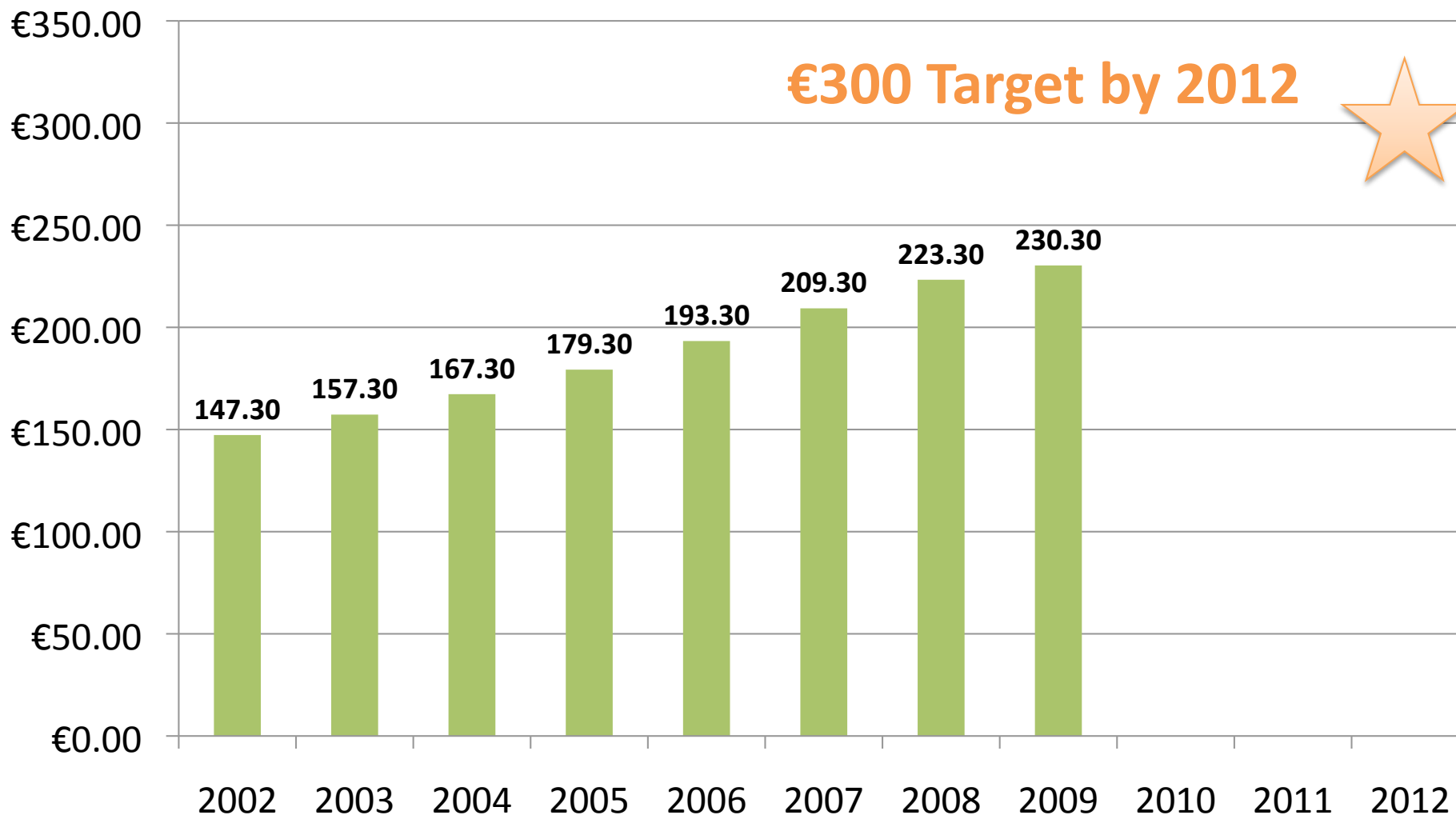


Source: CSO

Where the reform debate stood circa '07

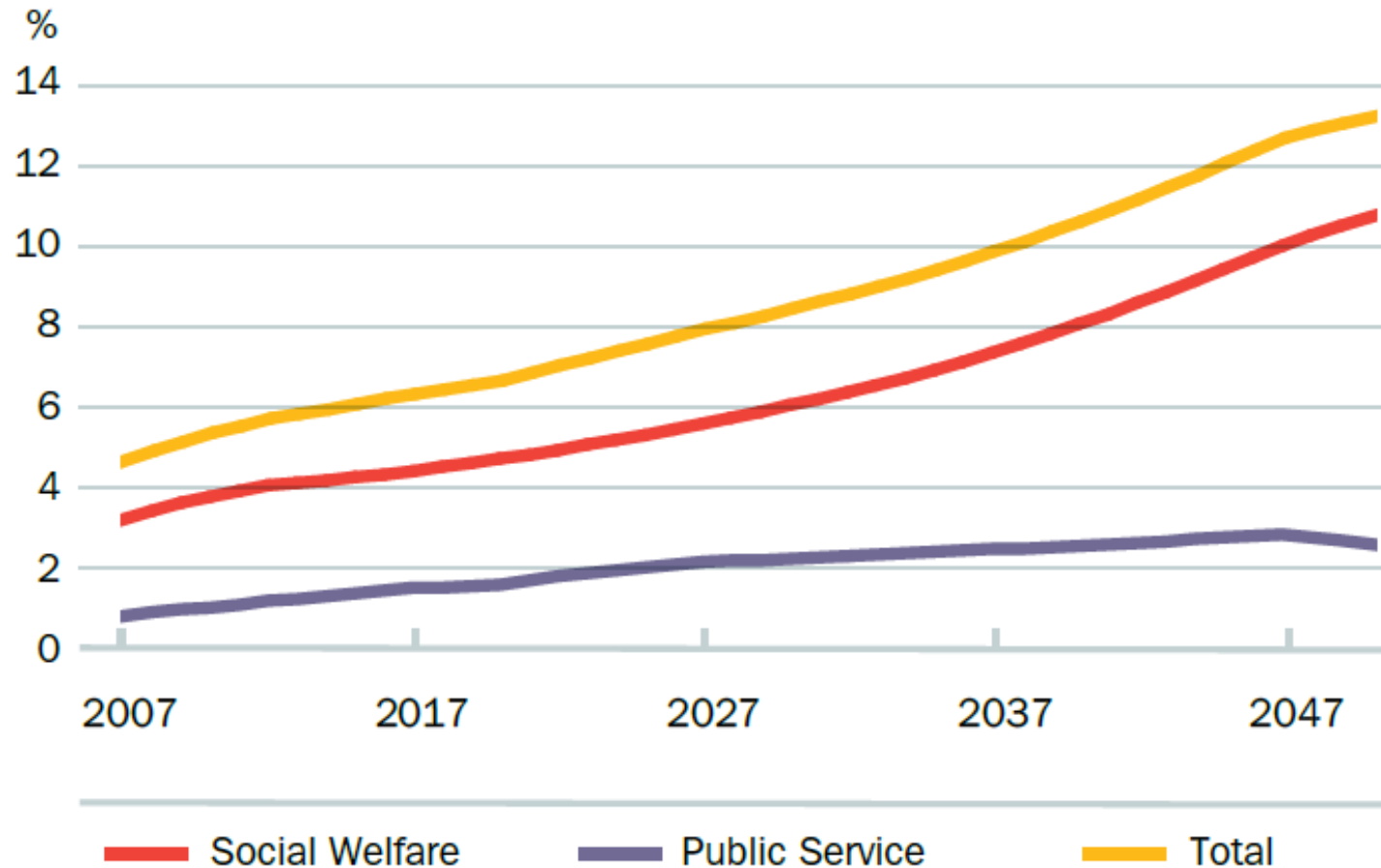
- €300 by 2012
- Pre-funding via NPRF
- Lessons from behavioural economics
 - SSIA-type matching design
 - Soft mandatory model

Raising the flat-rate pension



Source: Department of Social and Family Affairs

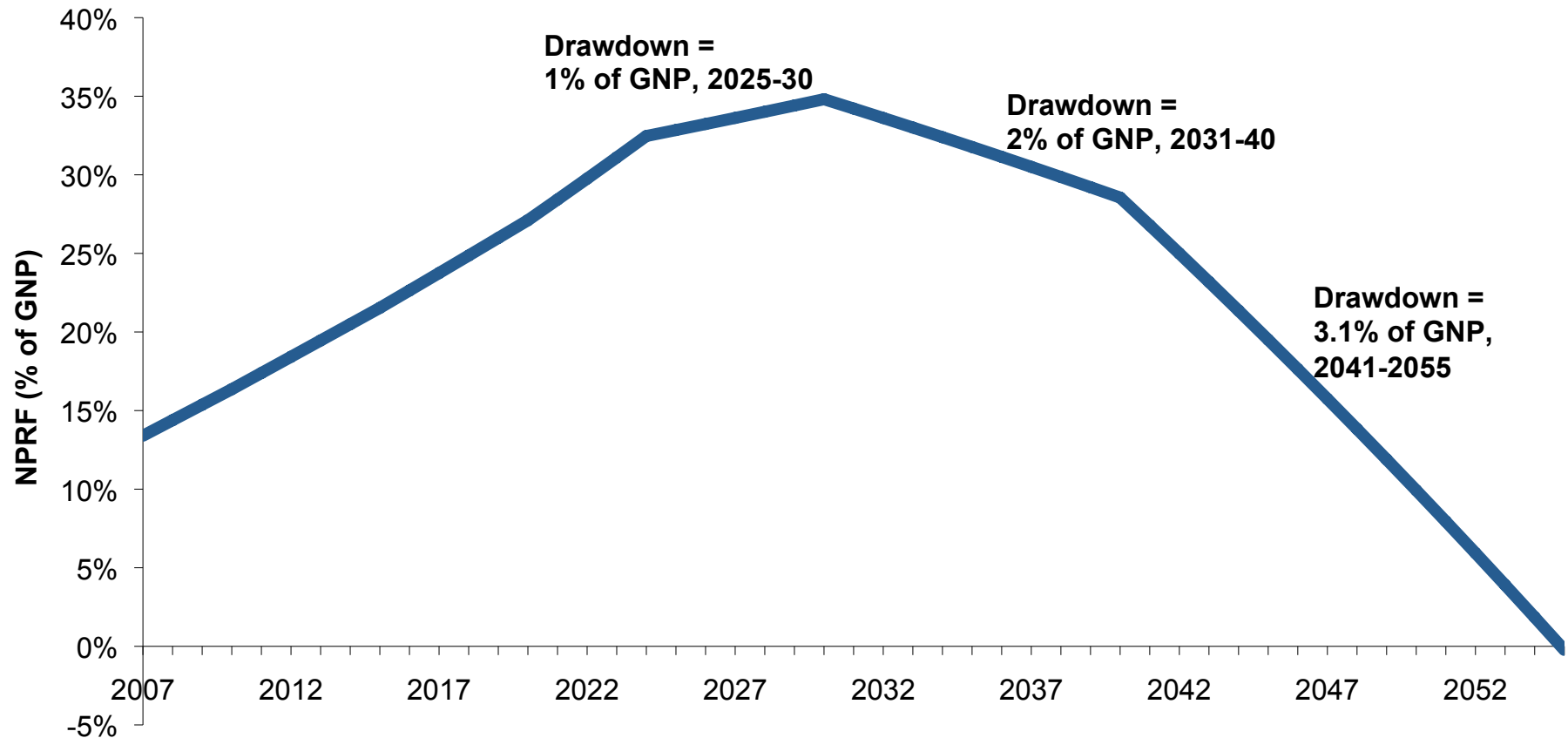
But rapidly escalating costs by mid-century



Source: Green Paper on Pensions 2007

How the NPRF was to help . . . The view from 2007

Hypothetical Evolution of the NPRF



Assumptions:

- (1) Fund size on December 31, 2007 = 13.4% of GNP
- (2) Assumed average annual GNP growth rates: 2007-2010 = 4.1%; 2011-2015 = 3.8%; 2016-2020 = 3.5%; 2021-2055 = 2.8%
- (3) Real rate of return on fund assets = 4%
- (4) 1% of GNP is added to the fund each year until 2055

Raising private provision: drawing lessons from behavioural economics

The screenshot shows the KiwiSaver website homepage. At the top right, there are links for 'About this site', 'Accessibility', 'Brand', 'Statistics', and 'Print page'. The KiwiSaver logo is on the left, with the tagline 'Poua he Oranga'. A search bar is on the right. A navigation menu includes 'Home', 'New to KiwiSaver', 'Already in KiwiSaver', 'Providers & schemes', 'News', 'Contact us', and 'My KiwiSaver'. The main heading is 'Retirement saving made easy', followed by a sub-heading 'KiwiSaver is a voluntary, work-based savings initiative with a range of membership benefits.' To the right, a text box states 'KiwiSaver is open to all New Zealanders under 65 years old.' Below this is a photo of two smiling women. A carousel of six dots is visible. Two main content boxes are shown: 'New to KiwiSaver' and 'Already in KiwiSaver', each with a right-pointing arrow icon.

About this site | Accessibility | Brand | Statistics | Print page

KiwiSaver™
Poua he Oranga

Search

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Retirement saving made easy

KiwiSaver is a voluntary, work-based savings initiative with a range of membership benefits.

KiwiSaver is open to all New Zealanders under 65 years old.

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New to KiwiSaver

Find out about the benefits, how KiwiSaver works, how to join and more.

- ▶ How does KiwiSaver work?
- ▶ Is KiwiSaver right for you?

Already in KiwiSaver

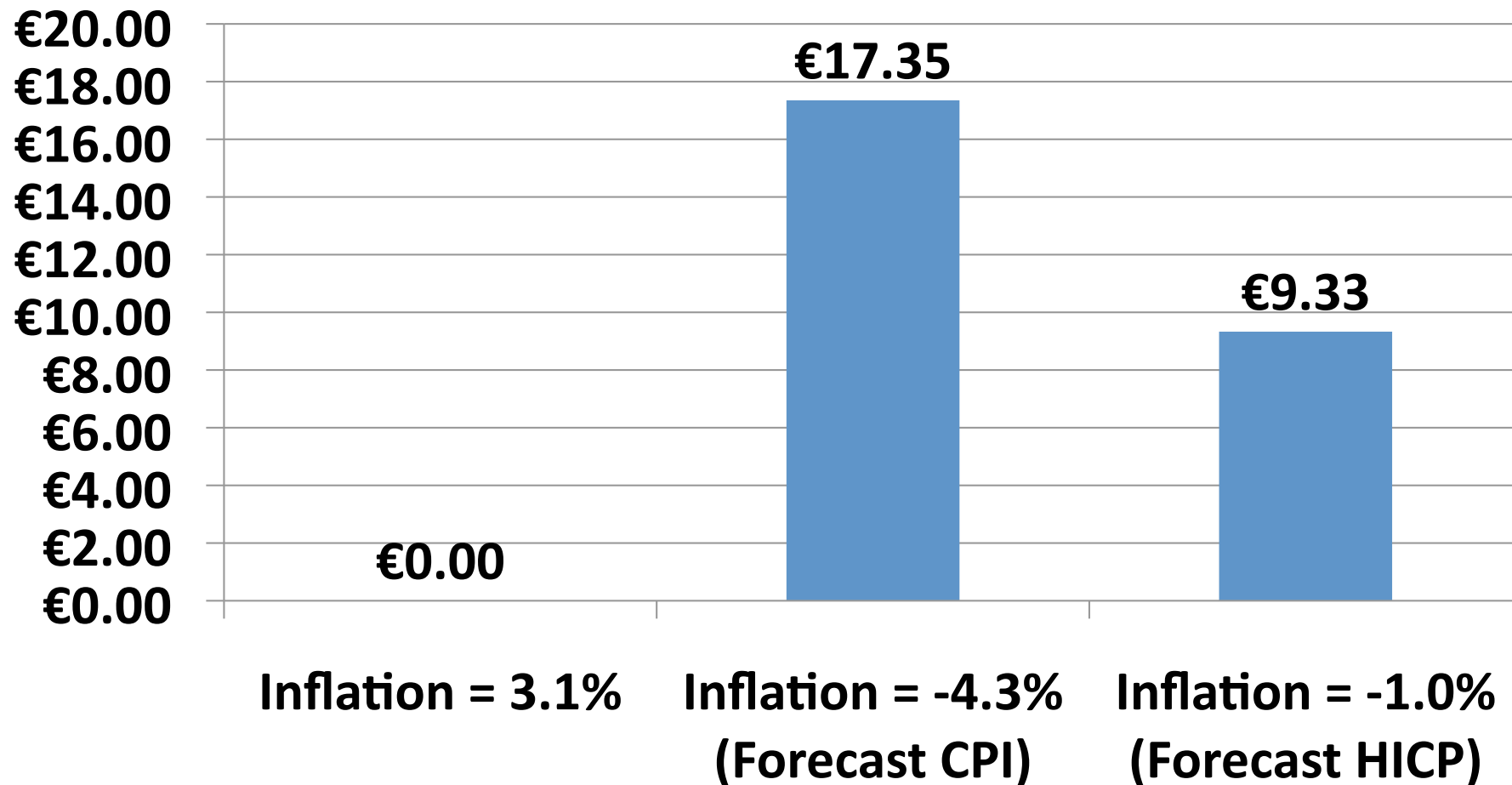
Find out about making contributions, how changes to your circumstances affect your KiwiSaver and more.

- ▶ Your KiwiSaver contributions
- ▶ Situation changed?

From a slow- to a fast-burning crisis

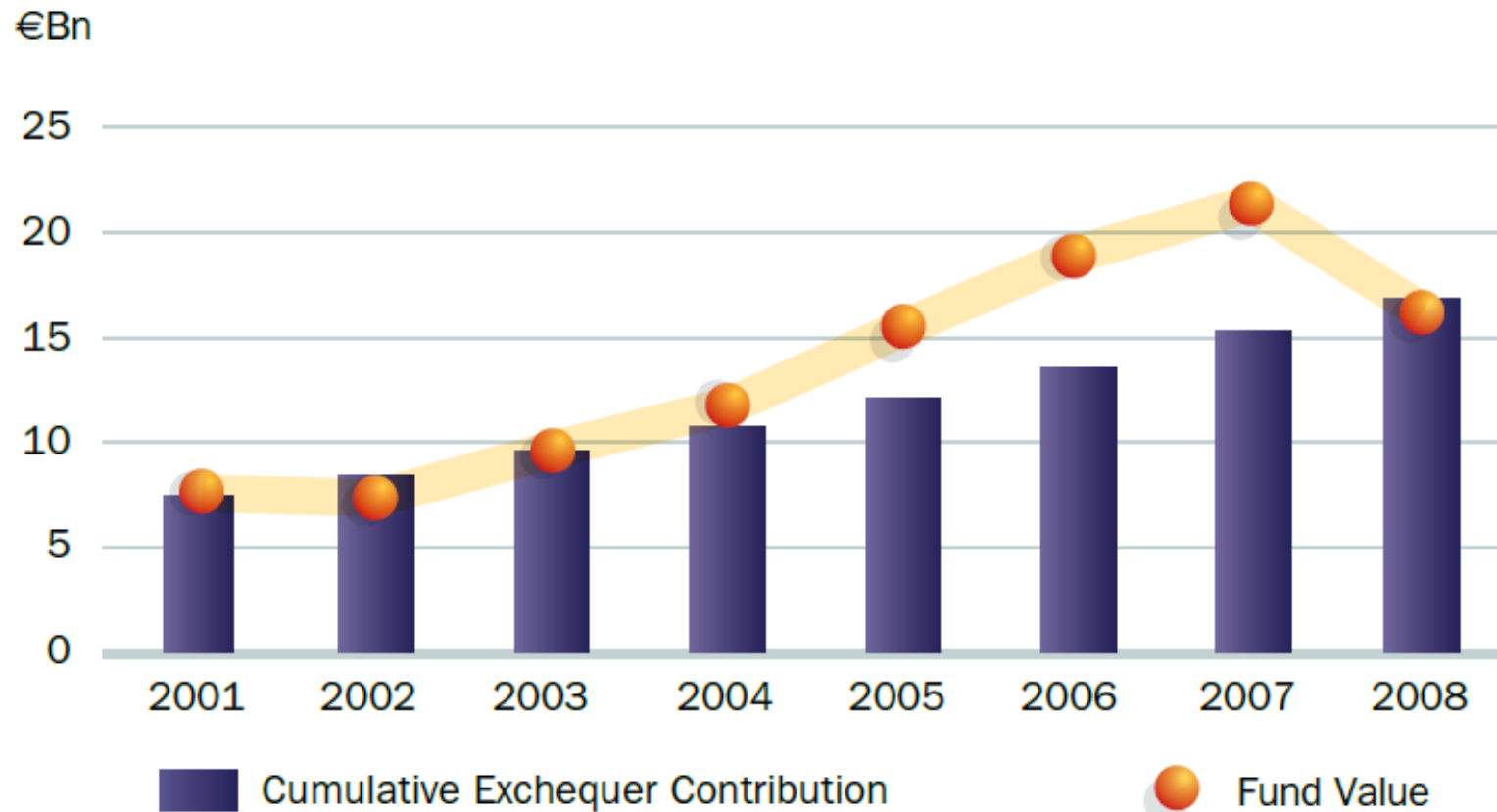
- Economic crisis → Unintended increase in real benefit
- Intensification of long-term fiscal constraints
- Major hits to pension assets

Unintended increase in the real flat-rate benefit (2008 prices)

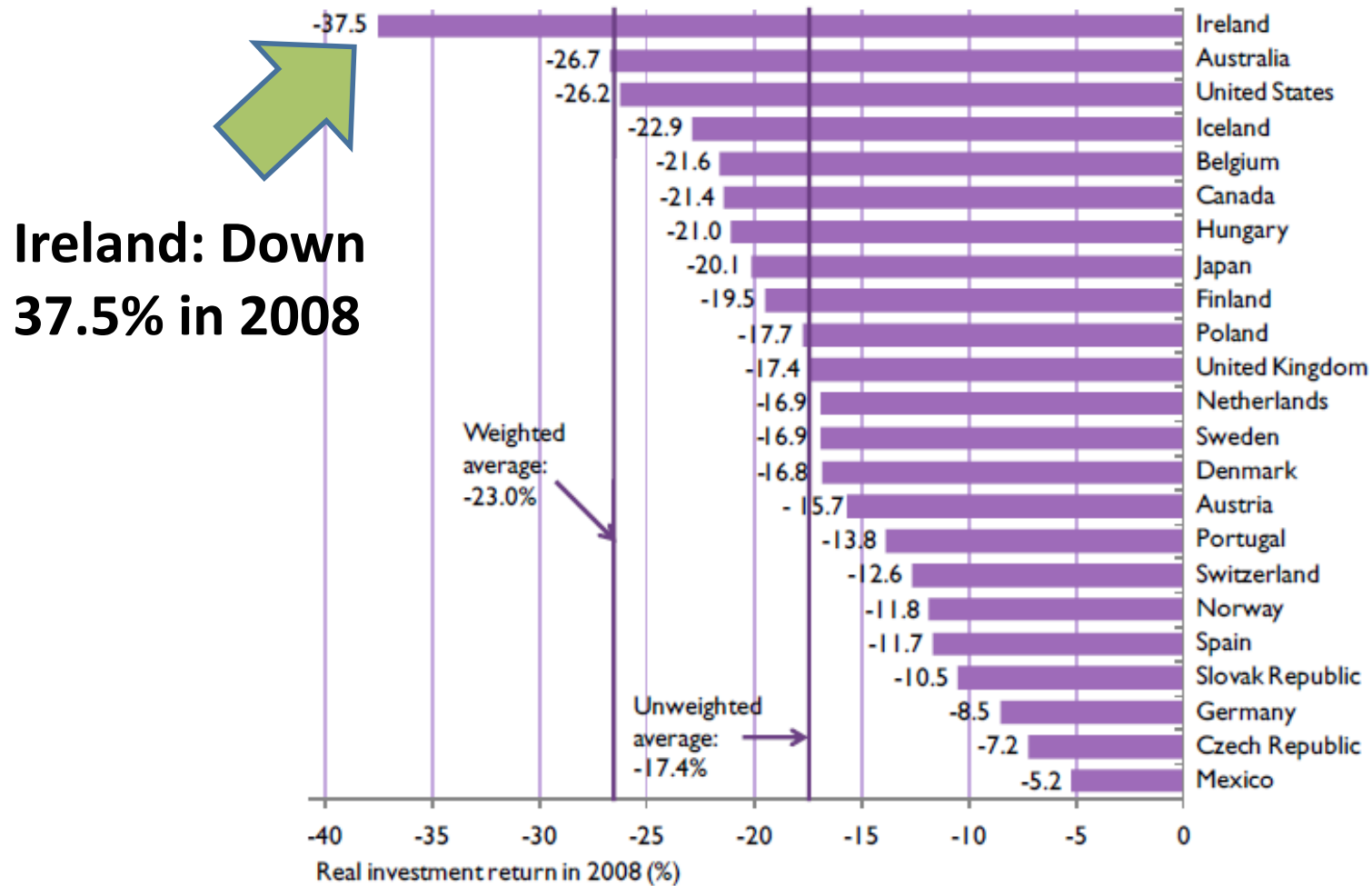


Forecasted CPI and HICP from ESRI QEC, Autumn 2009

NPRF returns are wiped out



Pension funds' real returns in 2008



Note: includes countries where pension fund assets in 2007 were worth more than 4% of GDP

Source: OECD *Pensions at a Glance 2009*, Figure I.3

Where to from here?

- Should the flat-benefit be spared in the budget?
- How to respond to the tightening of the long-term fiscal constraint?
 - Need to consider indexing benefits to longevity
- Wisdom of pushing mandatory saving in a recession?

**But need to improve
pension provision has not
gone away**

Notional defined contribution (NDC)

	Defined Benefit	Defined Contribution
Unfunded	Flat-rate pension	NDC
Funded	Occupational pension	Private Pension

How might it work?

- 6 percent contribution rate
- Individual accounts (regular statements)
- “Notional” rate of return based on growth of the wage bill
 - Adjustments to ensure financial stability over time
- Annuitisation at retirement

Advantages

- Limited impact on lifetime wealth and thus consumption
 - Immediate positive impact on confidence
- Strong link between contributions and benefits → Not viewed as a tax
- Relatively low risk compared to financial investments
- Immediate flow of revenue to the exchequer

Disadvantages

- Revenue windfall gradually disappears over time
- Unfunded, so does not add to national saving
- Lower expected rate of return than in a funded system (but also lower risk)

Summing up

- Easy to dismiss something new
- But must remember we face a set of flawed options
- NDC stands up well, all things considered