Pension Systems and Income Inequality among the Elderly around the World





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INPARR International Research Seminar: Consistency amid Complexity: Navigating the Future of Pensions and Retirement Paris, OECD, June 6, 2018

Outline of the presentation

1) Research perspective \implies 2) Data analyst perspective \implies 3) Policy advice

Theoretical framework & main findings own work

Comparable indicators & awareness of cross-national differences

Bring together expertise in research/data/policy fields (mechanisms pensions/family policy & labour markets)

Theoretical framework & main findings own work

- Theoretical framework for an 'ideal' pension system design. (Myles 1989, OECD (PAAG) 05-15, OECD 2008, World Bank 1994)
- Differences in (welfare) state ideology: liberal vs. conservative vs. social-democratic (Esping-Andersen 1990) / liberal vs. coordinated (Hall & Soskice 2001).
- Cross-national variation in pension systems and pension income mix.
 (Korpi & Palme 1998, Behrendt 2000, Yamada & Casey 2002, OECD 2001)
- New social risk groups require modified pension system design. (Armingeon and Bonoli 2006; Taylor-Gooby 2004)
- → Evaluate and <u>explain inequalities in pension income</u> of the elderly.

Theoretical framework & main findings own work

RQ 1: Why is there cross-national variation of income received by the elderly?

<u>RQ 2:</u> What implications do different <u>institutional pathways</u> of pension systems have for the income situation?

<u>RQ 3:</u> What role do <u>non-public pension systems</u> play in the income-mix and for the development of inequalities?

<u>RQ 4:</u> Which <u>developments</u> can be observed in the public-private income mix and generosity of the pension system?



<u>Approach:</u> Comparative cross-national study of pension outcomes from a historical welfare state tradition perspective.

'Small-N' analysis: Most Similar System Design

Theoretical framework & main findings own work

• What is new? - Comprehensive analytical framework for analysing pension system design and pension outcomes. (Part I: Theoretical framework - Chapters 1,2,3)

3 dimensions: Pension system characteristics

Individual labour market attachment

Living arrangements



Stylised model of retirement income

Working Phase **Pension System** Retirement Phase Full-time / part-time Public basic pension: Timing of retirement Permanent/fixed-term/ Level of public basic pension - Years of residency atypical job Level of public targeted Public work-related pension: Unemployment (means-tested) pension - Contribution period Otherinactivity Level of public work-related - Contribution ceiling pension care obligations Credits (periods of inactivity) Level of private pensions work injury Private pensions: Other in come sources - Contribution period (work, capital, private) - Mandatory / voluntary Living conditions **Employment & Labour Income** Contributions & Entitlement **Poverty & Inequality**

Source: Neugschwender (2016: p29); Ebbinghaus and Neugschwender (2011: p392), adjusted.

Theoretical framework & main findings own work

<u>Finding 1:</u> In Western European societies pension systems are the major explanatory factor for <u>pension income inequality</u> and <u>reproduction of pre-retirement inequality</u>.

But pension system characteristics vary in a comparative cross-national perspective.

Various <u>actors</u> are involved in pension system design (state, employers, financial institutes).

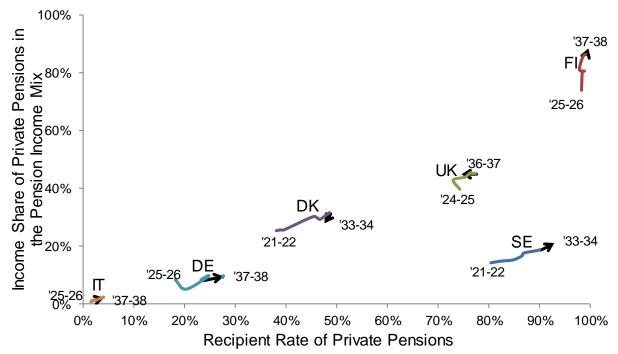
The degree of involvement of these actors follows different state traditions.



As a result, pension systems create <u>cross-national differences</u> with respect to poverty prevention (<u>pension adequacy</u>) and income maintenance (<u>income replacement</u>).

<u>Finding 2:</u> Public (mandatory) <u>first-tier schemes</u> left different scope for development of complementary second-tier schemes.

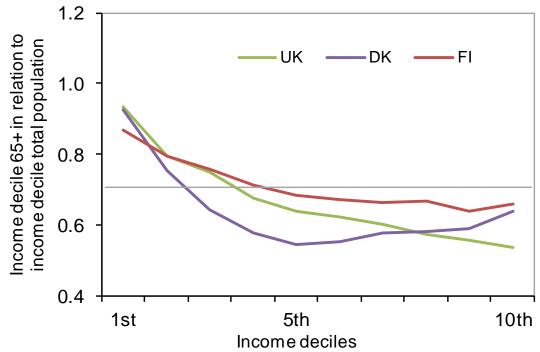
 a) depending on the public pension system tradition complementary second-tier schemes have been *crowded out/in*.



Source: Neugschwender (2016: p122); own calculations based on Luxembourg Income Study (LIS) Database.

<u>Finding 2:</u> Public (mandatory) <u>first-tier schemes</u> left different scope for development of complementary second-tier schemes.

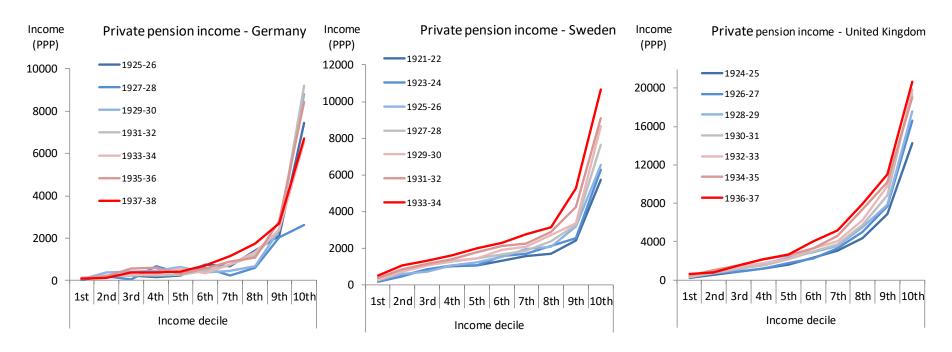
 b) voluntary second-tier schemes create selective coverage, as they are not considered equally important, or are a financial burden for low to medium income earners.



Source: Neugschwender (2016: p90); own calculations based on Luxembourg Income Study (LIS) Database.

<u>Finding 2:</u> Public (mandatory) <u>first-tier schemes</u> left different scope for development of complementary second-tier schemes.

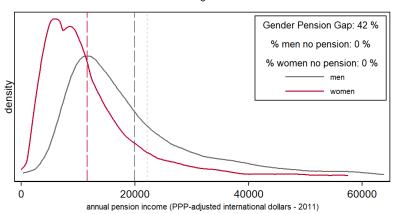
c) contribution ceilings create both under-protection and over-protection.



Source: Neugschwender (2016: p127/8); own calculations based on Luxembourg Income Study (LIS) Database.

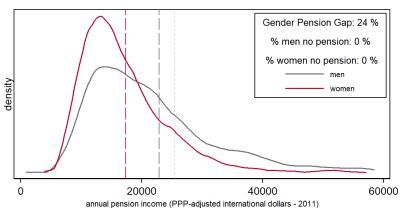
Kernel density estimate for pension income by gender

-- United Kingdom 2013 --



Kernel density estimate for pension income by gender

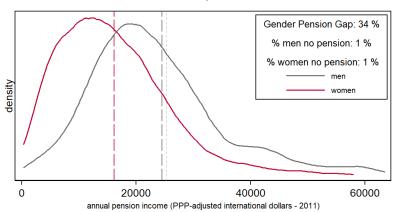
-- Finland 2013 --



Notes: Epanechnikov kernel function based on 1000 quantiles for men and women separately, 0 pension income & top 1 percent censored for the graph Source: Luxembourg Income Study (LIS) Database.

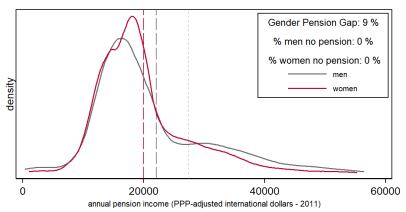
Kernel density estimate for pension income by gender

-- Germany 2015 --



Kernel density estimate for pension income by gender

-- Denmark 2013 --



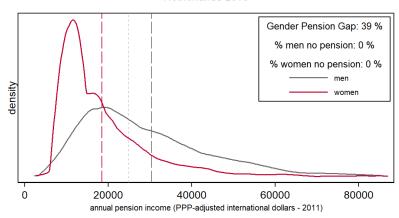
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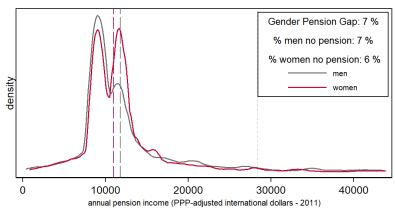
Kernel density estimate for pension income by gender





Kernel density estimate for pension income by gender

-- Australia 2010 --

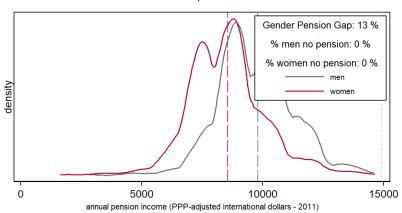


Notes: Epanechnikov kernel function based on 1000 quantilies for men and women separately, 0 pension income & top 1 percent censored for the graph.

Vertical long-dashed lines show mean values for pensions for men and women, short-dashed line shows median of equivalised DHI for the whole society
Source: Luxembourg income Study (LIS) Database.

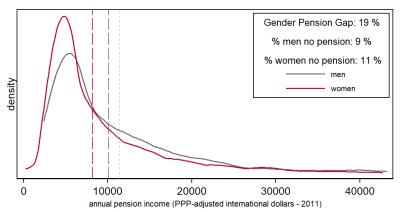
Kernel density estimate for pension income by gender

-- Czech Republic 2013 --



Kernel density estimate for pension income by gender

-- Uruguay 2016 --



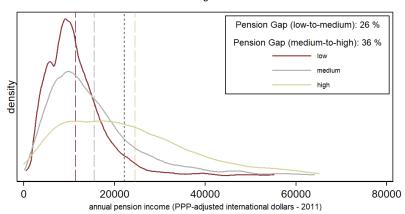
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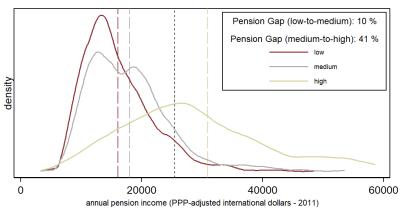
Kernel density estimate for pension income by education

-- United Kingdom 2013 --



Kernel density estimate for pension income by education

-- Finland 2013 --



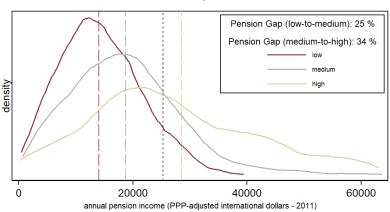
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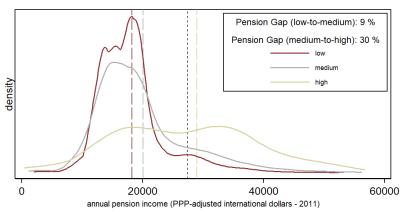
Kernel density estimate for pension income by education

-- Germany 2015 --



Kernel density estimate for pension income by education

-- Denmark 2013 --



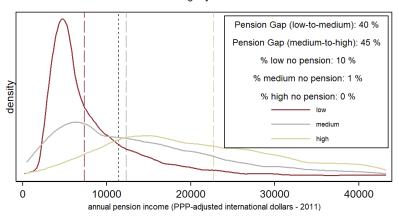
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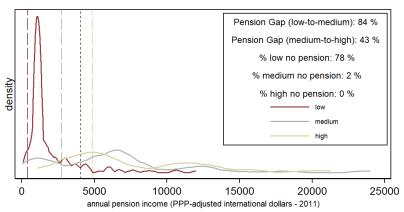
Kernel density estimate for pension income by education

-- Uruguay 2016 --



Kernel density estimate for pension income by education

-- Guatemala 2014 --

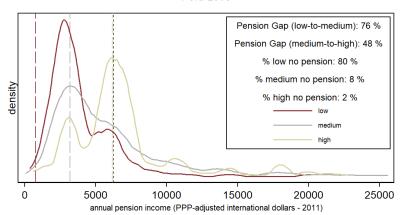


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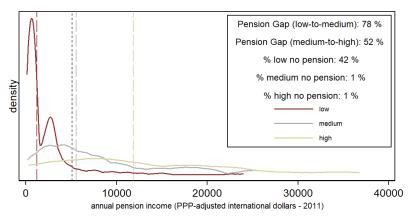
Kernel density estimate for pension income by education

-- Peru 2013 --



Kernel density estimate for pension income by education

-- Mexico 2012 --



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a) strong variation in historical paths of pension systems

Denmark

- basic pension (citizenship)
- basic pension supplement (income tested)
- *ATP* (working hours)

 Labour Market Pensions (collective agreements)

Sweden

- (basic pension), since 1999
 guaranteed pension
- (ATP (earnings-related pension))
- since 1999 Income Pension (earnings-related pension)
- various private and public sector schemes (collective agreements)

United Kingdom

- basic pension (years in employment)
- Pension Credit (meanstested)
- SERPS/S2P (earningsrelated pensions) or ...
- ... contracting out to occupational /personal pension (voluntary decision)

Germany

- social assistance for the elderly
- *GRV* (earnings-related pension)

 earnings-related pension (partially via collective agreements) & state subsidised personal pensions

collectivist path but still maturing (low recipient rate)

collectivist path matured (high recipient rate) individualist/ firm-based path matured (selective) 'topping-up' individualist path (low recipient rate)



social assistance



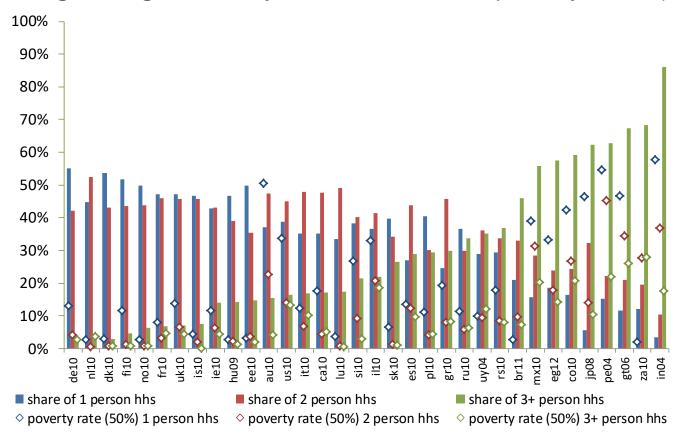
public pillar



occupational & personal pillar

b) strong variation in living arrangements & risk of poverty

Living arrangements by household size & poverty rates (65+)



Source: Neugschwender (2016: p41); own calculations based on Luxembourg Income Study (LIS) Database.

Final remarks: Challenges of pension system design

- Pension reform measures of earnings-related pensions change very slowly future pension outcomes (→ 'forward looking' pension system design).
- But in the meanwhile social contexts are changing (post-industrialism, labour market participation of women, reconciliation of work/family, divorce & single parenthood, ageing societies).
- Employment career interruptions (unemployment, disability, child raising) can lead to substantial interruptions of contribution periods, if no credits are foreseen.
- Labour market stratification/occupational segregation are major challenges for individualised old-age provision (means-tested vs. earnings-related pension).
- Contribution years vary by gender (4.9 years EC: Pension Adequacy Report 2018), occupation, education level.
- Contributions should pay off, guaranteeing pension adequacy and income replacement (but, avoid wrong incentives).

The 'ideal' pension system:

- Bridge between labour market attachment, living arrangements, and stable (<u>individualised</u>) saving for old age and risk protection.
- Protection of 'insiders' and 'outsiders'.
- Redistribution to those in need.
- Close interaction between public, occupational, personal pension schemes (subsidise redistribution mechanisms in occupational/personal schemes?).
- → Two goals: poverty prevention and (mandatory) income maintenance.

There is a lot to be learned from jointly discussing & assessing policy scenarios across policy fields (> re-think social protection from a wider perspective).

Social protection among the elderly not only mirrors individual employment careers and savings choices, but also interacts strongly with outcomes of other policy fields.

Priority: reduce gender pay gap New challenge: education pay gap?

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Thank you!

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Pension pillars and pension income tiers

Second pillar First pillar Third pillar **Public pension Occupational Pension Personal Pension** Voluntary pension Bismarck Collective Beveridge plans agreements Social insurance Minimum pension Third tier complementary mostly voluntary inclusion based on status personal decision compulsory maintenance inclusion for for (MIE), HIE complementary status maintenance covered employees for (MIE), HIE, or 'topping up' mostlyin for HIE in addition to Second combination with status compulsory schemes tier earnings-related maintenance for Bismarckian public pension MIE, HIE social insurance means-tested minimum pension poverty prevention mostlyin or supplement to and status combination with the basic pension maintenance for Beveridge type LIE, MIE, (HIE) minimum pension poverty prevention for LIE, MIE First tier insurance based basic pension minimum pension poverty prevention for LIE, MIE, HIE for LIE

Notes: LIE=low-income earner; MIE=medium-income earner; HIE=high-income earner.

Light grey schemes refer to selective coverage; dark grey schemes refer to comprehensive coverage.

Source: Neugschwender (2016: p15).

Main characteristics of the pension system and public-private income mix

Denmark



by pillars

tradition of public pension: Beveridge

structure of occup. pension: labour contracting

by tiers

poverty prevention: basic minimum pension status maintenance: (public)+occupational

by income source

share of public pension: medium-high share of private pension: low-medium

recipient rate of private pension: low-medium

United Kingdom



by pillars

tradition of public pension: Beveridge structure of occup. pension: contracting out

by tiers

poverty prevention: targeted minimum pension status maintenance: public+occupational+personal

by income source

share of public pension: medium share of private pension: medium recipient rate of private pension: high

Finland by pillars



tradition of public pension: Beveridge

structure of occup. pension: mandatory by law

by tiers

poverty prevention: targeted minimum pension

status maintenance: occupational

by income source

share of public pension: low share of private pension: high

recipient rate of private pension: high

Germany



by pillars

tradition of public pension: Bismarck

structure of occup. pension: voluntary+(labour contracting)

by tiers

poverty prevention: none; social assistance status maintenance: public+(occupational)

by income source

share of public pension: high share of private pension: low

recipient rate of private pension: low

Sweden



by pillars

tradition of public pension: *Beveridge+Bismarck* structure of occup. pension: labour contracting

by tiers

poverty prevention: quaranteed minimum pension status maintenance: public+occupational+(personal)

by income source

share of public pension: high share of private pension: low

recipient rate of private pension: high

Italy



by pillars

tradition of public pension: Bismarck structure of occup. pension: voluntary

by tiers

poverty prevention: income-tested minimum pension

status maintenance: public

by income source

share of public pension: high share of private pension: marginal

recipient rate of private pension: marginal

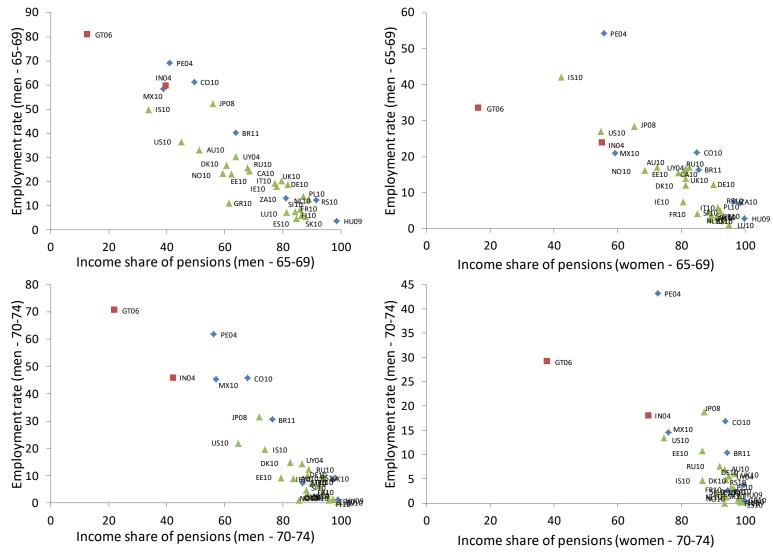
Sources: Neugschwender (2016: p71); Behrendt (2000); Ebbinghaus and Gronwald (2011); Rein and Turner (2004); OECD (2007).

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Labour market attachment and pension income (65+)



Sources: Neugschwender (2016: p49); own calculations based on Luxembourg Income Study (LIS) Database.