The Current Situation of the Reform on World Public Pension and Its Enlightenment to China

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Abstract: From a worldwide perspective, the proportion of the elderly in the total population is increasing. How to maintain the adequacy and financial sustainability of pension system will be a formidable challenge for all countries. Most OECD (the Organization for Economic Cooperation and Development) countries and many emerging market countries have reformed their pensions system. Structural reforms and parametric reforms are main reform measures. Meanwhile, employment promotion of the elderly and alleviating old age poverty are drawing much more attention. It can be concluded that , on the basis of empirical analysis of other countries' reforms and comparative analysis, China should combine measures of raising the retirement age with promoting the age management ; and lower the poverty of older people to ensure that the elderly population can receive adequate retirement income; and extend the coverage of voluntary pension scheme to attract more labor force employed in informal sectors to participate in ,thus increasing retirement income eventually.

Keywords: Ageing population with lower fertility; Raising retirement age; Poverty of elderly people; Age management

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1. Introduction

According to the latest population statistics from United Nations, the wave of population aging swept nearly half of the countries in the world in 2015, and the percentage will exceed 80%[1] by the year of 2050. Population ageing has led to increased pension spending in various countries, thus not only increases the government's financial burden, but also challenges the financial sustainability of the pension system.[2] Increased pension spending will also cause extrusion effect on education, infrastructure and other public investments, which reduce capital accumulation and labor productivity, thus will ultimately hurt long-term economic growth.[3] In order to cope with the crisis of population ageing, the main trend in pension reform is to shift the primary responsibility for pension provision from the public sector to the private sector since the 1980s, which has been expected to enhance the financial sustainability of pension.

China's pension system is still not perfect with a low retirement age and a short payment period, though the expansion of financial subsidy and its coverage temporarily obscure the financial risks of mismatching of the system parameters;[4] large-scale population mobility and employment flexibility are not easy to cope with, and it is difficult to break the pattern that the distribution of interests in the segmentations between urban and rural areas and various districts.[5] For China, who is faced with the same problem of population ageing, it is of practical significance to know about the major reform trends of the world's pension systems and learn from the good reform experience of those countries who have entered the aging society earlier.

2. The Main Trend of the Reform on World Public Pension

The public pension system is under great pressure. Although different countries have different pension systems, they face the same challenges: on the one hand, how to ensure the financial sustainability of the pension system? On the other hand, how to ensure that the elderly have adequate retirement income? The contradiction between those two aims existed when the pension system was formed, but in recent years, the economic crisis has increased the fiscal deficit and increased the debt, and various countries have been strengthening fiscal consolidation. It becomes more urgent to coordinate the contradiction between the two aims. Financial sustainability is a major concern in many pay-as-you-go countries, especially in continental Europe. Other countries with smaller public pension systems, such as some emerging market countries, are more concerned about improve retirement income via increasing the coverage of private pensions and raising pension replacement rates. The recent pension reforms① in the world mainly reflect four trends as followed.

2.1 Structural Reform

Over the past decade, many countries have made structural reforms to the public pension system, and among those reforms the most significant trend in the structural pension reform is the introduction or development of the DC (Defined Contribution) type pension scheme, usually as the individual account pension scheme under the mandatory cumulative pension system. The Chilean government took the lead in reform in the year of 1981, abolishing the original pay-as-you-go pension, and introduced individual account pension scheme instead. After that, other Latin American countries followed the Chilean pension privatization reform one after another. Almost at the same period, the World Bank (in 1994) also proposed the multi-pillar pension system, advocating the transition from the non-cumulative DB (Defined Benefit) public pension system to the fully cumulative DC pension system, which accelerated that reform trend. Over nearly 30 years, the footsteps to develop the second pillar pensions took by various countries in the world never stop: Many OECD countries have introduced the cumulative DC pension scheme, with the aim of partially replacing or fully substituting income related public pension schemes. By the year of 2011, there are 31 countries that have built DC pension schemes, thus the number of countries setting up the second pillar pension schemes has grown by 29, compared with the only two countries in 1990, Chile and Britain[6]. (As shown in Table-1)

Table 1. Changes in pension system patterns in various regions, 2011 (1990)

	Zero Pillar		First Pillar			Second Pillar	
	Targeted	Basic	NDB	NDC	PF	DC	DB
East Asia & Pacific	4	3	8	1	10	1	0
Europe & central Asia	11	4	28	5	0	15	0
High-income OECD Countries.	8	9	16	2	0	3	3
Latin America & the Caribbean	16	2	29	0	0	9	0
Middle East & North Asia	1	1	17	0	0	0	0
South Asia	3	0	2	0	3	1	0
Sub-Saharan Africa	3	2	30	0	4	2	0
The Total number of 2011	46	21	130	8	17	31	3
The Total number of 1990	20	10	140	0	17	2	3

Notes: "Basic" refers to the basic pension, namely the GSP (generalized system of preference) pension which is not related to income; "Targeted" refers to the targeted pension, namely the minimum pension for the poor elderly based on property surveys; "DB" refers to the Defined Benefit type pension; "DC" refers to the Defined Contribution type pension. "NDC" refers to the Notional Defined Contribution type pension. "PF" refers to the Provident Fund type pension.

Data sources: Pallares-Miralles,Romero,Whitehouse 2012.

2.2 Parametric Reform

In many pay-as-you-go countries, especially in continental Europe, In order to cope with the problems such as the population ageing, the extended life expectancy and the fertility decline, a series of reforms have been implemented which aim to reduce pension expenditures and increase the long-term sustainability of the pension system. Such reforms whose most important measure is to raise the retirement age are mainly aimed at mandatory pension schemes. To cope with the short-term budget constraints, some countries are taking or are considering cutting pension replacement rates, especially in countries with higher level pensions. Emerging countries, by contrast, have smaller pensions, lower public pension spending; more concerned about expanding pension coverage and raising pension replacement rates to improve retirement income.

2.2.1 Raise the Retirement Age

Over the past decade, most of the 34 OECD countries have passed legislation to raise the retirement age or make provisions for payment period to get full pensions. According to OECD statistics,[7] 8 of them plan to raise the retirement age or full pension age to 67 by around 2030, while the retirement age in Norway and Iceland has already reached 67 in 2012; 4 countries plan to raise the age to 65②. The population structure is aging in those 4 countries whose fertility rate is low, and the elderly support ratio is commonly below the OECD average level (3.92). The reform tends to stipulate that male and female labors retire at the same age. In 2012, 21 countries have had the same retirement age for men and women, and 12 other countries have planned to reach that goal in the future③.

The retirement age in the emerging countries is low which is commonly below the OECD average level and has an apparent gap to it. The retirement age in Argentina and Brazil is 65 (male) or 60 (female), While in other countries such as China, India, Indonesia, Russia, Saudi Arabia and South Africa, are no more than 60 years old. With the ageing of population structure and the increasing of life expectancy, emerging countries should adjust their retirement ages based on actual population conditions as well.

2.2.2 Reduce the Pension Replacement Rates and Consummate the Benefit Formulae

Many OECD countries raise the long-term financial sustainability of the pension system by reducing pension benefits, as long-term fiscal forecasts are relatively pessimistic. Among them, Greece has adopted the most comprehensive reform measures to reduce pension benefits. Emerging market countries outside Europe, by contrast, are more focused on ensuring adequate retirement income, developing corporate annuities and individual voluntary pension schemes to increase the replacement rates. In recent years, the main development trend of the Russian pension system is to improve the benefit level on the basis of ensuring the sustainability of the pension system, and after the reforms in 2007, the pension level was further improved, with pensions and subsidies rising from 27.5% of the average wage to 40%(2010).

The reform measures to consummate the benefit formulae mainly include: Firstly, implement the reform on the pension indexation adjustment mechanism. Secondly, change the wage base of benefit formulae. Thirdly, link pensions to life expectancy. Indexation adjustment refers to adjusting pension payments according to the changes in price and income. In recent years, many OECD countries take the full or partially of the adjustment according to price index instead of indexation adjustment based on income. That measure has kept the purchasing power of pensions; however, it means retirees are no longer sharing the fruits of economic progress.

2.3 Strengthen Age Management to Promote the Elderly Employment

As the generation of postwar baby boom gradually grows old and the fertility rate continues to decline, the proportion of the labor force in many countries declines, and the average age of the economic activity population increases. From 1995 to 2005, the proportion of young and middle-aged people in Europe has declined significantly, and the proportion of elderly people has increased substantially, during this period, the proportion of people over 50 in the European Union's labor force has risen from less than 15% to almost 25%.[8] And the actual age that the laborer exits the labor market is often below the mandatory retirement age, which shows the decline trend. In order to cope with the decline of the labor force and promote the elderly employment, the reform of public pension in many countries not only has been made to improve the sustainability of the system but also pays attention to encouraging elderly workers to extend their working years and increasing the supply of labor to avoid distortions in labor supply. Many countries intervene directly in the labor market to extend the working years, including the cancellation of mandatory retirement rules, the elimination of employer discrimination, or the adoption of more active employment promotion measures. In Britain, for instance, the default retirement age was abolished in 2011, and Norway provides a flexible retirement age of 62-75 in 2011; while Japan and France raised mandatory retirement age.

2.4 Extend Public Pension Coverage to Avoid Poverty of Elderly People

The basic goal of recent pension reform is to provide the guarantee of retirement income to the elderly on the basis of fiscal sustainability, and it is crucial to ensure retirement income for retirees, especially low-income retirees, which also suggests that an important focus of pension reform is equity. However, the problem of the poverty of elderly people will possibly worsen due to the reduction of the public pension system, the trend of extended working hours and the advocating of private pensions. Extending public pension coverage is the basic means to reduce poverty of elderly people. OECD countries have established mandatory or quasi-mandatory public or private pension schemes, with the aim of achieving full coverage of the pension system. But there are still part of the employees have not been incorporated into the pension system, even if the public pension schemes can't make the complete coverage realized as well, as the informal employment has a particularly low participation rate, especially in low-income countries. (see Figure 1)

For emerging market countries, it is top priority to extend the coverage rates of the pension system on the basis of the financial burden in an affordable range, thus making low-income earners, self-employed and flexible employment personnel incorporated into the coverage. On average, the pension coverage is particularly low in emerging Asia, while Latin America relatively high and the Middle East and Africa higher (As shown in Figure-1), which reflects the development level of the formal economy of the countries to some extent, as the pension insurance generally covers the public sectors and the formal private sectors. For countries with low coverage, a zero-pillar pension with redistributive nature should be established first. India set up a new pension system (NPS) in 2004 which featured wide coverage and low cost. What's more, the system also set up a joint contribution scheme for low-income earners, who can participate in the form of self-help groups or relative groups with the aim of maximizing the participation of low-income groups to extend the coverage rates; it also raised the maximum age limit for participation from 55 to 60, allowing more people to participate in the pension system.

3. The Enlightenment to China

3.1 Combine Raising the Retirement Age with Strengthening the Age Management

With the dual effects of prolonged life expectancy of the population and low fertility rates, China and the OECD

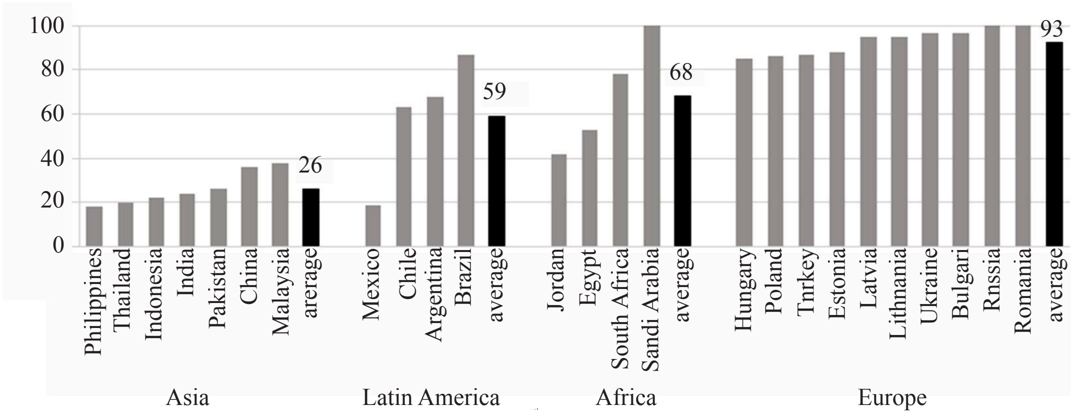

Figure 1. Public Pension Coverage in Emerging Market Countries

Data sources: IMF. The Challenge of Public Pension Reform in Advanced and Emerging Economies [EB/OL]. IMF Policy Paper, http://www.imf.org/external/np/pp/eng/2011/122811.pdf, 2011, 53.

countries are also caught in the dilemma of low birthrate and aging. Reforms to raise the retirement age are the trend of the times.[9] According to the 2015 UN Population Development Report, China's population life expectancy will increase significantly in the future. The average life expectancy in 2050 is 82.5 years, which is 7.1 years higher than the 75.4 years in 2015. The proportion of the elderly population aged over 65 years will continue to increase, and this proportion will reach 27.6% in 2050. Almost one in every four people is the elderly. And from 2010 to 2050, the fertility rate in China is between 1.55-1.74, which is always lower than the replacement level of 2.3 generations. What follows is a rapid increase in the ratio of old-age dependency, and the burden of heavy intergenerational support will eventually be transformed into a burden on laborers, corporate burdens, and financial burdens. The huge demand for pensions will also be financially sustainable for China's pension system. Sex challenges. The direct means of maintaining the balance of pension funds mainly include raising the retirement age, raising the payment rate, or lowering the level of treatment. In fact, China's pension replacement rate itself is relatively low. In 2013, it was only 43.37%.[10] Blindly reducing the replacement rate of pensions will hurt the adequacy of pensions, and lower the pension due to the characteristics of the rigid growth of pensions. The measure of substitution rate is not suitable for national conditions. On the other hand, taking the basic old-age insurance for urban workers as an example, China's pension insurance contribution rate is 28%, ranking first in the world, second only to Hungary, Italy, Hungary, and Spain. The space for raising the contribution rate is very small, blindly raising the rate. It can increase the burden on enterprises, increase the phenomenon of corporate evacuation, and even reduce the actual payment of pensions. Therefore, the more practical method is to increase the statutory retirement age.

However, it is worth pondering that raising the statutory retirement age may just be the first step we need to take. The actual problems are strongly associated with those who aged 50-60 years old: "Whether they are willing to continue their work, whether they are able to continue to work and whether they have the opportunity to continue their work". Those issues directly affect the effectiveness of the reform. The retirement age reform should not merely be to increase the statutory retirement age, use laws and regulations to "supervise" elderly people not to retire or delay their retirements, or to establish early or late retirement pensions and penalties, but also to strengthen age management ④ . There are two main factors that hinder elderly labors from continuing to participate in market labor: age discrimination ⑤ and the decline of productivity. Although the establishment of a reward and punishment mechanism for pensions is an economic measure to ensure that elderly labors are willing to continue their work, it cannot eliminate the impact from those two factors; however, age management helps break age barriers and provides a good employment environment for elderly labors. The ageing of the population is often accompanied by an aging labor force. In the near future, age management will no longer be an old-age policy. It is also a universal labor market policy.

3.2 Strengthen Basic Protection for Vulnerable Elderly People and Reduce the Incidence of Poverty of Them

Compared with developed countries, China's social security system is still at a primary level. Pension expenditures and pension replacement rates are low. Many elderly people fall into poverty because they cannot obtain sufficient retirement income. The poverty rate in old age is much higher than other groups. Lixiong Yang[11] used the minimum living guarantee data to calculate that the elderly poverty population in China was about 18 million in 2009, accounting for 10.77% of the population aged 60 or over in that year. The minimum living security data is only the smallest number of people living in poverty. Scale, so the actual elderly poverty rate should be higher. Under the background of rapid ageing and aging, how to effectively alleviate poverty in the elderly is an important concern for the reform of the old-age security system in China.

To learn from the reform experience of OECD countries, to cope with old-age poverty should focus on improving the level of pension with the redistribution nature: Firstly, improve China's basic pension system, increase coverage, encourage informal employees to participate in insurance; establish a reasonable treatment The automatic adjustment mechanism, especially the basic pension level, should be adjusted in time according to changes in wages and prices. Secondly, the minimum living security system as a "social safety net" should provide basic financial assistance and physical assistance when the elderly are in trouble, strictly apply for conditions and regulate the actual operation, so that "should be guaranteed" is the key to solve problem. Thirdly, establish an old-age security system to provide low-cost or unpaid services to low-income elderly people. For example, the government purchases community home-based care services or medical care services and provides it to impoverished elderly people as a form of relief or security. Old-age care and medical care are necessary expenditures for the elderly[12]. For the improvement of the lives of impoverished elderly people, it is even more effective that the government provides protection in the form of pension services than cash subsidies.

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Annotation

① The research objects of the article are mainly divided into OECD countries and emerging market countries, among which OECD countries include 34 member countries and emerging market countries have 8 countries, namely Argentina, Brazil, China, India, Indonesia, Russia, Saudi Arabia and South Africa.

② The 8 countries include: Australia 2023, Denmark 2027, France 2017, Germany 2029, Greece, Spain 2027, UK 2026, Poland Men 2020, Women 2040; 4 countries include: Czech Republic, Estonia, Hungary, Turkey.

③ Including Austria, Chile, Estonia, Greece, Italy, Poland, Slovakia, Slovenia, Turkey, and the United Kingdom.

④ The term age management (Age management) in the narrow sense refers to the organization of employees of different ages, as long as they are elderly employees, to carry out certain human resources management activities; broadly refers to the aging of the labor force through public policy or negotiations between employers and employees. Conduct comprehensive management.

⑤ Older workers are discriminated against in terms of age, as they are required to provide age restrictions in recruitment, lack of promotion and training opportunities, and low benefits. There are also many subtle forms of expression, such as: limiting the work responsibilities of older employees; encouraging early retirement of older employees when employees are redundant.