COUNTRY SPOTLIGHT IRELAND

Challenging change

Peter Davy **explains the potential reforms to the French pensions system and the issues these proposals face**

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After victory in the French Presidential election and winning a large majority in parliament, Emmanual Macron has the mandate for his reforms, including those focused on French pensions. Whether he has a plan, though, remains to be seen.

The proposals so far are at once ambitious and vague. Announcing them in March, Macron said he aimed to unify the pensions system. This means bringing together the mandatory complementary occupational schemes, of which there are dozens, in addition to the Agirc-Arrco, which covers most private-sector workers and Ircantec for public-sector employees. Together with the basic state pension, these make up the vast majority of most pensioners' income.

It's a huge job, says, PwC Paris partner Hélène Farouz, "just huge".

"First of all, these schemes are all managed by different parties, so you will have to get the consent of all of them on the objective of any new scheme," she says.

It's undeniably ambitious, but the details to date are vague.

"We understand he will most probably set up something new, most probably an occupational pension scheme, but we don't know if it will be like the Agirc-Arrco or something different; obviously it will be a defined contribution scheme, but we don't really have any idea what the split will be between the employer and employee; we don't know the tax treatment… The information so far is really, really sparse."

Perhaps the most important question is why Macron is proposing the reform. Many of the challenges traditionally associated with the French pensions system have already been addressed by past reforms. Despite a history of strikes when big reforms are proposed, progress has been made in making the system

sustainable, according to OECD head of pensions and population ageing Hervé Boulhol.

"There have been some financial sustainability issues with the pension system in France but reforms over almost 25 years have addressed this for the most part," he says. Pensions are not unusually generous anymore, for example. In the most recent OECD *Pensions at a Glance* publication, the gross replacement rate for a full-time career worker at an average wage in France was around 55 per cent, against 53 per cent for OECD. The retirement age, which Macron has said he does not have plans to alter, is in the process of rising to 62. More might be needed, says Boulhol, but there has definitely been progress.

"It is true that in France there is usually a lot of resistance to reforms, but reforms have taken place even if it has been costly in terms of strikes and so on."

There remain, though, a number of challenges. For one, in calculating pension benefits, the French system, unusually, adjust past wages used as a reference in line with inflation. The result is that the cost of real wage growth to the pensions system is reduced, but if wages lag inflation or fail to grow as fast as expected, the expected financial improvements fail to materialise, says Boulhol. It also continues to have a problem with retirement at early ages, he adds.

Perhaps more fundamentally, the myriad of different schemes for civil servants, independent workers, the power sector, transport and so on, make the system complex, adding to costs.

"The system has been improved a lot, but it still costs a lot of money; and it is whether that is an efficient use of the money. It's more a question of the efficiency of the spending and in that sense the complexity of the French system brings administrative costs," says Boulhol.

It is not just about costs either, but confusion and clarity. The system of industry-wide schemes, while historically making some sense, fails to account for modern career patterns, says Paris-based think tank Ifrap director Sandrine Gorreri. In the past people spent their entire career as civil servants, for example, or lawyers or were self employed, so stayed in one scheme.

"Now people move from one situation to another and have careers contributing across different schemes," says Gorreri. "It is a big problem."

Whether it's one that Macron will be able to begin to solve remains to be seen. Gorreri is optimistic but says reforms are unlikely to come smoothly.

"In France most people know that it is very difficult to change the rules for the public sector and civil servants," she warns. Most anticipate strikes in September if the new President does push ahead with big changes, she adds.

Unhelpful caution

To date, not all interventions designed to shore up occupational schemes have been that helpful. In July, for instance, new regulations are due to come into effect, regulating investments and controls for reserves at more than a dozen complementary occupational schemes.

The government decree requires schemes to match assets to liabilities for the next decade and largely bans derivatives – just two aspects that CNAVPL (Caisse Nationale d'Assurance Vieillesse des Professions Libérales) objects to. It represents 10 of the schemes subject to the new rules, covering about a million workers and retired people.

"Association of assets and liabilities is inappropriate," warns CNAVPL president Monique Durand. "It will lead the funds to block large amounts of their reserves in no-return assets." The ban on derivatives to hedge risks is almost as bad. "That is completely opposed to a proper risks management."

"I don't even want to talk about some other unenforceable points that show the lack of awareness of practice from the authors of this decree," she adds.

There are other restrictions on illiquid assets, ETFs and index funds (where they practise securities lending), currency exposures and some types of real estate. The reforms are not just unhelpful but unnecessary, according to French institutional investor association Af2i president Jean Eyraud.

"Technical deficits existing in some institutions are due to ageing and are under control," he says. "These institutions are well managed and their performances are good from a long-term perspective."

Promoting the private sector

The other key policy recently seen from the government is that of promoting private pensions provision. Again, its progress is not without criticism.

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Much has been made of rules for a new pensions vehicle, the FRPS (fonds de retraite professionelle supplémentaire), published earlier this year. The rules create insurance-based occupational pensions operating the IORP Directive. The government has estimated €130 billion of assets could be eligible for transfer into an FRPS.

At Mercer, though, principal Christel Bonnet says it will take more than this to kick start funded occupational pensions.

"We have very few insurers who are going to use this. It's no real change, just that for the insolvency obligations the insurer will use Solvency I, rather than Solvency II. There is nothing very new." To date only one insurer has said it wants to set up an FRPS, she adds.

The biggest obstacle to greater private-sector pensions provision is that most think the mandatory system is sufficient. As Bonnet puts it: "In France we can live with the pension plan."

Macron's reforms are unlikely to change that, says Boulhol, since they're primarily focused on increasing equity and transparency and reducing administration, rather than cutting spending.

"It's difficult to see why this should boost interest in voluntary pensions," he says. Furthermore, if people do feel the need for boosting their retirement income, tax incentives on life assurance (effectively long-term savings plans with some life cover in France) and other structures provide attractive and less restrictive alternatives, he adds.

Even if funded pension schemes are to take off, it may not be the FRPS that is responsible. Didier Le Menestrel, who chaired a competitiveness commission for the French asset management association AFG last year, says he believes France's great hope is to be a new centre for pan-European pensions products.

He admits there is little in its culture to date that supports the development of funded pensions; the PAYG system is "written in our genes", he says. But that could rapidly change with the right support.

"We are optimistic about the future," he says. "It's just as in developing countries where there is no traditional telephone one day wireless comes and then everyone can have a phone without building any new infrastructure."

Likewise France is well placed to step in to fill retirement savings gap, not just in its own territory but across Europe. "France is in continental Europe; we have fund managers; and if the legal framework is there and you have pan-European personal retirement plan then we just have to feed it with our products," he says.

"It's a real opening." ■