INDUSTRY

Race against time

Pension systems across Europe are not prepared to deliver adequate retirement benefits. But is there enough time to fix the problem?

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When asked as to when Europe will enter a full-blown pensions crisis, Cass Business School's Pensions Institute director, Professor David Blake, offers a blunt assessment. "It's already here," he says.

Blake has been one of the most vocal harbingers of doom in the UK, but his evaluation is hard to counter. Stunted population growth in the West has left countries with fewer working age people to pay for first pillar benefits. Meanwhile, in the second and third pillars, rising longevity, coupled with much lower and more volatile asset returns since the turn of the century, have wreaked havoc across retirement saving vehicles.

"The global financial system appears to have fundamentally changed since 2000," says Blake. "The benign world of 1950-2000 had stable real returns of around 6 per cent. So not only do we have the demographic crisis, we also have problems with the financial system being able to deliver stable real returns going forward."

The statisticians have certainly backed Blake's bleak outlook. Last year, the World Economic Forum (WEF) sounded one of the loudest official pension alarm bells to date. It predicted that the world's six largest pension structures – situated in Australia, Canada, the Netherlands, Japan, the UK and the US – will have a joint shortfall of €199 trillion by 2050, effectively setting up the industrialised world "for the biggest pension crisis in history". And earlier this year, the European Commission released its own report on pension adequacy, finding that 17.3 million people aged 65 and over were at risk of poverty or social exclusion in the EU.

Looking to the future, the commission estimated that the time spent in retirement will increase from 51 per cent of that spent in employment to 53 per cent by 2060. It warned that a new balance had to be struck between working life and retirement in order to sustain adequate pensions.

Implementing solutions

The good news is that there is a broad consensus on what needs to be done to avert disaster. With DB schemes having been the main victims of the shifting socio-economic landscape, and countries racking up further debt in an attempt to preserve state benefits, the responsibility for retirement saving is falling onto the shoulders of Europe's workforce. As Blake says: "All this means that in future people will have to work much longer and contribute much more to their pension schemes than previous generations."

In its 2017 report, the WEF called on governments to ensure that the retirement age by 2050 reaches at least 70, and that people were made to understand that the state pension may not be enough to retire on in the

future. In many cases, it said, "people will need to 'top-up' their state pension entitlement via private savings". To make this a possibility it also urged countries to help employees to start building up pension pots in the second pillar through, for example, an auto-enrolment regime such as the one found in the UK. To supplement this, it also recommended the introduction of financial education in schools and an online pensions dashboard (as in place in Denmark and being developed in the UK) to allow savers to view their pension data in one place.

In the UK, the country's Pensions and Lifetime Savings Association (PLSA) has also published a blueprint on how to achieve retirement income adequacy through the second pillar. It argues that savers need to be given retirement income targets and has commissioned a research institute to develop them by early 2019. It also believes that the UK should raise the minimum contribution levels for automatic enrolment from 8 per cent of band earnings to 12 per cent of total salary between 2025 and 2030.

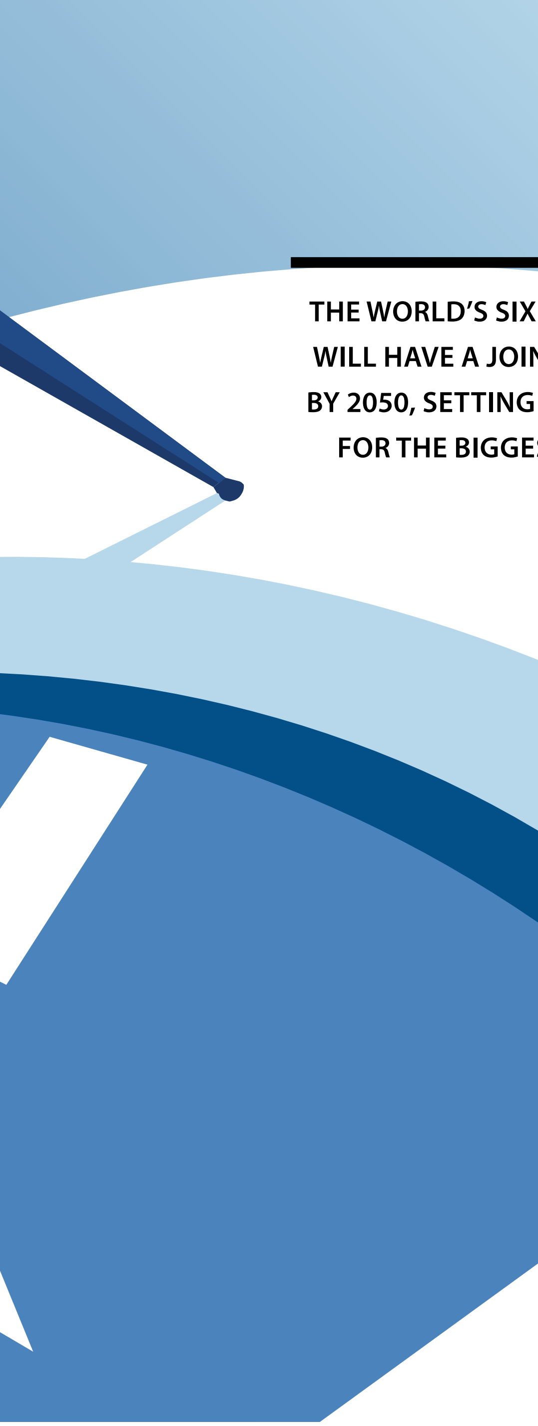
The bad news is that time is running out for governments to implement the right strategies. What's more, any sense of urgency seems to be constantly hampered by political infighting across the continent.

In the Netherlands, as the Federation of Dutch Pension Funds's (Pensioenfederatie) spokesperson Mandy Ros points out, trade unions and employer representatives have been arguing over Dutch pension arrangements for at least a couple of years now as they try to reach a compromise over benefit promises and indexation. Although Dutch pension funds are in rude health, with the retirement replacement ratio relatively high compared to other European nations, Ros admits that the protracted negotiations, against a backdrop of persistently low interest rates, is taking its toll.

"This has decreased the trust and appreciation for the Dutch pension system in the Netherlands," says Ros.

Across the border in Germany, Angela Merkel's embattled government has agreed to shore up the first pillar by maintaining the pension payment level for the coming seven years. With no concrete plan in place for the state pension after 2025, Willis Towers Watson has said that contributions into private pension funds need to double to cover the savings gap.

Other countries that are heavily reliant on pay-as-you-go (PAYG) arrangements across Europe, such as those found in France and Spain will have to do similar, as the European Commission stated in its pension adequacy report. "Complementing statutory pensions with broad and



THE WORLD'S SIX LARGEST PENSION STRUCTURES WILL HAVE A JOINT SHORTFALL OF €199 TRILLION BY 2050, SETTING UP THE INDUSTRIALISED WORLD FOR THE BIGGEST PENSION CRISIS IN HISTORY

well-designed supplementary schemes can help support adequate pension outcomes," write the report's authors, who then go on to rather casually propose "further in-depth consideration" of the matter within different national pension environments.

Fighting public opinion

Blake advocates action that goes far beyond mere "consideration". In relation to the first pillar, he believes that Europe needs to introduce much more rapid increases in the state retirement age than currently planned, to well over 70 within the next 20 years.

However, this will take some doing. Opinion polls have shown that many people of working age, accustomed to seeing their parents enjoy long retirements, are still against extending the retirement age at a faster rate, meaning that any such manoeuvres by governments will probably result in political suicide.

In Norway, the Centre for Senior Policies (SSP) has found that fewer people than ever before are willing to work after reaching retirement age. In its Norwegian senior policy barometer 2018 the SSP says that from age 60 onwards, the share of people wishing to continue working after receiving the right to pensions has fallen from 75 per cent to 54 per cent.

Expanding on the barometer, the SSP's director, Kari Østerud, says:

"The average *[desired]* retirement age in Norway is 65.7. When we started asking this question in 2003 the answer was 61.

"So the wished averaged retirement age has increased by nearly five years in the past 15 years. This shows a great change in the desire and motivation for working longer. In the past three years, however, we have seen a small decrease in the average wished retirement age from 66.2 in 2015 to 65.7 in 2018.

"We do not actually know why this is happening, but it seems that we have reached a limit for how long people want to work. It seems to be around 66 on average."

This limit is a concern, says Østerud as one year's extended occupational activity per person can provide a combined €4.2 billion in added wealth. "Through working longer, older workers contribute to their own retirement pension and the longer you work before you retire, the higher the pension you receive," she adds, admitting that it is puzzling and worrisome that fewer people than before are willing to work until they are 70. To try and reverse the situation, Østerud argues that attitudes and negative stereotypes about older workers must be combated, while several companies still need strategies for how to develop and retain older workers.

Taxing times

Another two long-term options open to governments presiding over ageing populations are to try and stimulate their GDP numbers to enable an increase in wages and therefore a natural rise in private pension contributions, and to allow in younger migrant workers to make the pension contributions and look after the indigenous older population. Neither is easy or straightforward, and in many ways the first option is a prerequisite for the second.

However, if governments continue to hesitate over second pillar provision and larger jumps in the state retirement age, and these additional measures are not taken, then the only real – and arguably easiest – choice left is to collect more tax.

But even this will only prove to be a sticky plaster solution. Blake warns that wholesale changes are needed. The alternative? A wholesales collapse of the current pensions eco-system. ■