Pension: A Special Report

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• Gertrude Janeway died in 2003
• Before she died, she was getting a monthly check for $70 from Veterans Administration earned by her late husband John
• They got married in 1927, when he was 81 and she was 18
• The entitlement spanned three centuries
A pension promise

- A pension promise can be easy to make but expensive to keep
- pension
  - pensions provided by the private sector
  - pensions provided by the state
Social insurance

• It is sometimes claimed that pension system is a social-insurance scheme

• Despite the insurance label, these are essentially pay-as-you-go (PAYG) systems in which benefits are paid out of current taxes
The four challenges #1 and #2

• #1: People are living longer
• #2: The large generation of baby-boomers (born between 1946 and 1964) is now retiring; but the following generations are smaller
The four challenges #3

- Defined-benefit (DB) scheme: promised pensions are linked to salaries
- In the 1980s and 1990s the true cost of these promises was hidden by a long bull market in equities
- The past dismal decade for stockmarkets depleted those funds and left employers on the hook for the shortfall
The four challenges #4

• Defined-contribution (DC) scheme: pension payouts are linked to the investment performance of the funds concerned, thus transfer nearly all the risk to the employees

• But the amount is inadequate
Sharing the burden

• A longer working life
• higher taxes
• lower benefits
• saving more