Globalisation and Flexibility: Dancing around Pensions

by

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By Guy Standing[1]

1. Introduction

Across the world, almost without exception, pensions have become the subject of intense and controversial debates. In most places, the debates have been clouded by commercial, political and economic undercurrents that have had little to do with the simple process of finding ways of providing an adequate income for those who have "retired" from the labour force in some way. Ideological crusades have particularly characterized the debates on pension reform in Latin America and eastern Europe, with countries in the latter region intent on emulating policies introduced in Chile and elsewhere, commonly pushed by outsiders, notably the IMF and World Bank. Indeed, one's position on pension reform has almost been a touchstone of one's position on the political spectrum. Contributing further to the intensity of controversy, heavy lobbying by powerful commercial interests have scarcely contributed to objective assessments of the options for improving income security and human development.

Although some analysts have placed the pension reform debates in a broader social and economic context, there is a distinct possibility that we may be missing the plot altogether by focusing on pensions *per se* without considering wider changes taking place in the economy, in the labour market, and in the way a growing number of people are organizing their lives, or wish to do so.

This paper has a modest objective, and will not deal with the specifics of pension systems, which are best left to those with much more expertise at this conference. The objective is to set out some of the contextual issues around the pension reform debates. An underlying premise is that the "pensions crisis", as popularly depicted, is not primarily about the pension system but about the political, social and economic changes taking place around it.

2. Globalisation and Flexible Labour Markets

One feels almost apologetic about beginning with "globalisation". The word has an all-purpose ring to it that makes for confusion. Yet this is the context of all our discussions. For our purposes, globalisation is about increasing *options*, about increasing *mobility* and the *need for mobility*, and – paradoxically – about the perception of increasing *constraints* faced by policymakers and individuals.

In more open economies, savings and investment can flow more easily to where expected returns are highest, firms can shift the location of their production more easily, and they can alter the way they organize their labour force more easily and at less cost. The churning taking place in all these respects is feverish, making many economic and social relationships increasingly transient, fragile and uncertain. Individuals have had to adapt in numerous ways, just as politicians have had to rethink the role of the state, in the area of public social policy as much as anywhere. As for the constraints on independent national policy, there has been a tendency to use

[1] Director, Socio-Economic Security Programme, International Labour Organisation. This paper is a first draft, and should not be cited without permission. All opinions are the author's and should not be attributed to the ILO. Comments would be welcome.

the perception that globalisation is all powerful as a rationalization or justification for certain policies when there is no substantive evidence to conclude that alternatives to them are out of the question. There is no reason to *presume* that globalisation precludes independent government policy that would not correspond to some international norm. Harmonisation has a seductive charm. But what is wrong with diversity or with experimentation?

Among the developments associated with globalisation is the growth of actual and desirable *flexibility*. This is another term that has been used and abused in numerous ways, but which helps us to define the challenge ahead.[2] Six forms of labour flexibility have grown, all of which are having profound implications for all forms of social protection and regulatory policy. Consider each of them.

Organisational flexibility.

A growing number of firms are not just “downsizing” and “hollowing out”, but are regularly recreating themselves. All over the world, a growing number of small establishments emerge, die, re-emerge, change shape, change the work status of those involved, and then change again. The instability creates several challenges, including those linked to social protection policy – such as workers not achieving entitlement to ‘occupational welfare’, more individuals having broken contributions records, and more having a variety of work statuses as a result of the enterprise turbulence. Small unstable firms are less likely to provide workers with enterprise benefits, including occupational pensions.

External flexibility.

More firms have externalized their employment – almost contracting out their employment function. This is associated with such phenomena as sub-contracting, greater use of temporary labour (including “permanent temporaries”), teleworking, and use of agency labour on a temporary basis. Already temporary employment through agencies has become one of the largest sources of employment in the industrialized world. For many of those involved, the availability of a pension is not the first issue that emerges, it is simply *knowledge* of options. People in insecure employment are relatively unlikely to be aware of what they could or should do for their longer-term income security. Across the world – in most countries to a much greater extent than in the UK – it is surely this simple aspect of labour insecurity that determines behaviour. People whose job and work status are defined by the present are most likely to think only for the present. Rational long-term planning is for those with at least modest economic security, which is almost definable in terms of the ability to look to the future with reasonable confidence. Policymakers and institutions such as pensions companies can provide packages of benefits that are portable. They are less able to address this form of “presenteeism”.

Functional flexibility.

With rapid technological change and the informatics revolution, and with greater emphasis on “competitiveness”, it is becoming easier to restructure jobs. More workers and employees have to learn and relearn bundles of technical capacities to remain or become “employable”. This aspect of labour flexibility may seem to have little to do with pensions. Perhaps, indirectly, it does. If more of us have to switch

[2] Themes covered in this section are elaborated and documented in a recent book. G. Standing, Global Labour Flexibility: Seeking Distributive Justice (Basingstoke, Macmillan, 1999).

jobs, not only will we be conventionally skilled one moment and semi-skilled the next, so that our income and income prospects will vary considerably. We will also have the prospect of having to switch jobs and work status, and require savings to help tie over the adjustment periods.

A man or woman may wish to define himself or herself in terms of an occupation, but for more people this may be a chimera. The lack of occupational stability creates more risks and uncertainties that have to be taken into account in personal planning. We have to save for so many contingencies and to be prepared for so many eventualities that it is easy to overwhelmed. The relatively vulnerable in society are the least able to save or prepare.

Working time flexibility.

This may appear to have less relevance for pensions than other forms of flexibility. However, there is evidence that the distribution of working time during the course of working life has been changing, and that this is not adequately captured by age-specific labour force participation rates. For a large and growing proportion of the 'prime age' population actual working hours may have risen, suggesting that people may be working for income more intensively in the peak years of earnings, and that the apparent shortening of the economically active period, which is causing some pension analysts such concern, is actually a redistribution of working time rather than any substantial reduction.

If this is the case – as data strongly suggest has been the case in the USA – then one should be wary about interpreting statistics on duration of working life and those alarming "dependency ratios". If I wish to take partial retirement at age 55 instead of working for an income fully until age 65 and then retiring fully, the ten years might actually merely offset the extra time worked in the preceding ten years.

Wage-system flexibility.

The systemic flexibility associated with globalisation is bringing with it profound changes in the structure of what may be called *social income*.[3] It is not just a matter of wages and salaries being more flexible, led by the trend away from team-based or collectively bargained wages and salaries. It is about the restructuring of the components of total income. This way of looking at developments may be useful for those peering into the future of public, private and communal systems of social support. So perhaps a few lines of explanation may be permissible.

Social income may be presented as a straightforward identity, recognizing that any individual receives income in money or kind from one or more of the five sources. Social income may be defined as follows:

$$SI = W + CB + EB + SB + PB$$

where SI is the individual's total social income, W is the money wage or income received from work, CB is the value of benefits or support provided by the family, kin or the local community, EB is the amount of benefits provided by the enterprise in which the person might be working, SB is the value of state benefits, in terms of

[3] Social income is the term proposed to cover all elements of any individual's income – wages, enterprise benefits, state benefits, community benefits and services, and private benefits. Each of these can be sub-divided. For a full discussion, see Standing, 1999, chapter 3.

insurance benefits or other transfers, including subsidies paid to workers or through firms to them, and PB is private income benefits, gained through investment, including private social protection.

We can further disaggregate the elements as follows:

$$SI = (Wb + Wf) + (FT + LT) + (NWB + IB) + (C + IS + D) + PB$$

where W_b is the base or fixed wage, W_f is the flexible part of the wage (bonuses, etc.), FT are family transfers, LT are local community transfers, including any income from charity, non-governmental organisations, etc., NWB are non-wage benefits provided by firms to their workers, IB are contingency, insurance-type benefits provided by firms to their workers, C are universal state benefits (citizenship rights), IS are insurance-based income transfers from the state in case of contingency needs, and D are discretionary, means-tested transfers from the state.[4]

In that context, across the world the pattern of social income has been changing, with some profound implications. For instance, for many groups of workers there is evidence that there has been a shift from the various forms of non-monetary remuneration to money incomes. On the surface, this might look like a rise in real wages. But if it merely represents a shift in form of payment, it will be an illusion. Among the implications is that a given contribution rate will represent a higher rate than before the shift took place. And the monetary form of remuneration is likely to be more insecure or variable, and leave the individual having to decide whether or not to use income to insure himself for such contingencies as healthcare and retraining. Similarly, the decline in universalistic state transfers obviously means that the individual has to take greater responsibility for insuring herself or finding an employer to do so. The costs for the individual are often substantial, so that the shift could be said to result in a lower social income unless the private return exceeded the value of the forgone state benefits.

In the UK, some of those changes may be marginal, but in much of the world the restructuring of pensions has had important effects on social income security. In eastern Europe, for instance, the collapse of enterprise welfare that had given social support "from cradle to grave" has put great strain on the newly emerging public and private pension schemes. There is simply no community and kinship social support system on which to rely, so perversely a rise in the state pension can coincide with impoverishment because the pension income represents a rising proportion of total (social) income. In east Asia, the economic crisis of 1997 put a strain on the capacity of community networks to cushion the decline in incomes. Because of economic changes and industrialization, this source of income support has become far more fragile. Ironically, there and almost everywhere – above all in eastern Europe – the increasing economic instability and the shrinking state have meant that there is greater need for support from community and kinship networks. In many countries, the shrinking state has been partially concealed by the fact that intended shrinkage (ex ante) has been offset by increased demand or need, in which accumulated needs or acquired rights have prevented governments from cutting expenditure. A typical example is where a government cuts the income replacement rate for unemployment

[4] A source of income not highlighted in this decomposition is income from the sale of goods and services. These are included in W, and effectively in the flexible part of W.

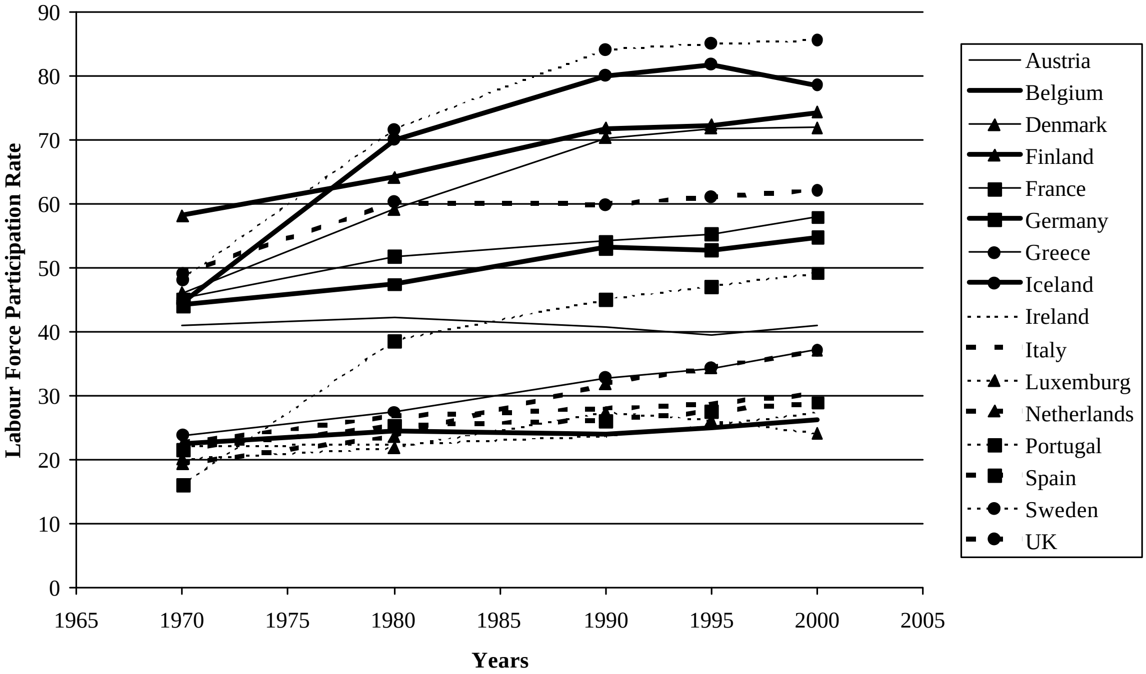
benefits in order to cut expenditure, but where the latter objective is thwarted by a rise in total unemployment.

As for intra-family transfers, ongoing changes are having significant implications. If there are stylized facts, they are that extended families are declining all over the world, nuclear families of the stable variety on which the welfare states were constructed comprise a shrinking minority of all households, and many more people are single-person units or present themselves as such. Behind that are fewer and more fragile inter-generational and intra-generational reciprocities that can be taken for granted. Informal income transfers across the generations was an implicit underpinning of most pension systems, which have always provided part of the social income of the elderly or disabled. With demographic individualization, the pressure is growing for pensions to provide a full income or at least a larger proportion of the total social income. Those who can save – and above all those who can earn mainly from the capital market – are at a growing advantage. Many more of those who have a poor pension will be impoverished than when those family transfer mechanisms were more deeply embedded in society.

Labour force flexibility.

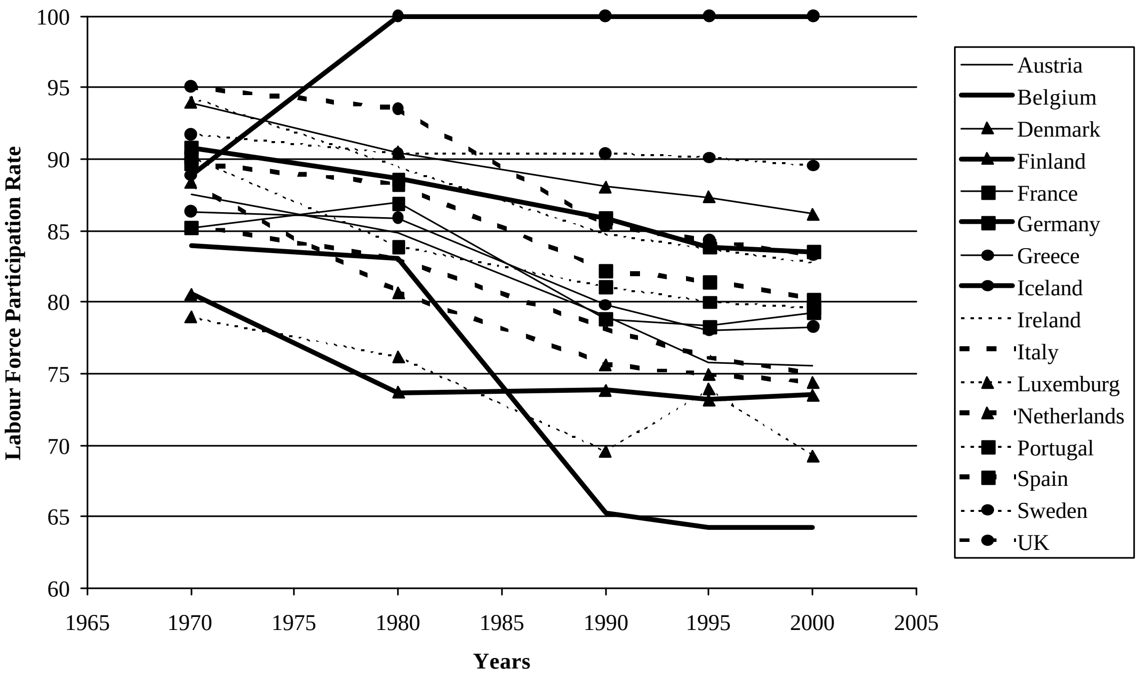
In most countries an increasing number of people have intermittent labour force participation, which partially reflects the feminisation of employment. More jobs are of the type that traditionally were predominantly regarded as women's, and more women have been entering and remaining in the labour force. In Europe, and elsewhere, many older women in their 50s have been entering or remaining in the labour force, particularly since the 1970s (Figure 1). Meanwhile, men's labour force participation rate has been declining for all age groups, although most sharply for men in their 50s (Figures 2 and 3). Periodic withdrawal from the labour force raises familiar questions about contribution records, pension entitlements, duration of employment, and so on. Whatever the formula adopted to take such interruptions into account, there are implications for income distribution in old age, with strong effects for gender inequality among pensioners.

Figure 1: Labour Force Participation Rates of Female Population Aged 50-59, European Union



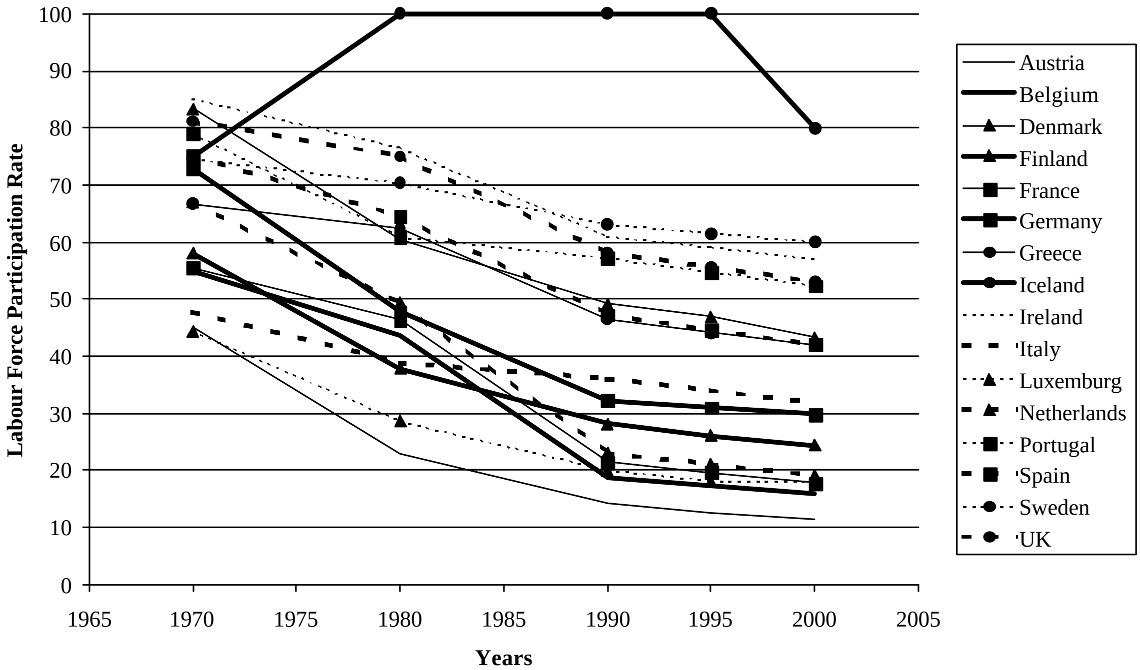
Source: ILO Bureau of Statistics.

Figure 2: Labour Force Participation Rates of Male Population Aged 50-59, European Union



Source: ILO Bureau of Statistics.

Figure 3: Labour Force Participation Rates of Male Population Aged 60-64, European Union



Source: ILO Bureau of Statistics.

3. Socio-Economic Fragmentation

Alongside the various forms of flexibility has been an important process of socio-economic fragmentation of society, the significance of which I will try to bring out later. Essentially, the post-1945 welfare state, with its universalistic social security provision and the Beveridge dictate that the state should cover "temporary interruptions of earnings power", relied on two sets of presumptions. First, it presumed that any interruption of earnings would be short, fairly randomly distributed across the population (at least the bulk of it) and would be part of the normal life cycle. Periods of sickness-induced absence from employment were expected to be limited, unemployment was expected to be rare and short, and the period of retirement was expected to be modest relative to the years of employment. None of these presumptions held from the 1970s onwards.

The second set of presumptions has probably received less attention. It was expected that a majority and a growing proportion of the adult population would be in stable, full-time employment, being unionized and having all the behavioural traits of the "working class". This made it relatively easy to build a system of income protection based on a *social solidarity principle*. Even those not in standard employment relationships were close to it or had family, neighbours or friends who did fit that norm.

It is not just that this model was eroded over the latter half of the 20th century. A fragmentation into distinctive socio-economic strata has shattered the basis of the labourist principle of social solidarity. Although we could quibble with any disaggregation of society into distinctive groups, one can characterize the ongoing societal fragmentation in terms of seven strata. In doing so, we may be able to highlight one of the major difficulties facing reformers of social protection in general and pensions in particular.

At the zenith, in terms of income, wealth, status and power, we have an *elite* of absurdly affluent and eerily powerful individuals, whose billions put them outside any state social protection and regulatory system. Their number may be tiny, but their influence is out of all proportion to that. The pandering to their whims by politicians should be more worrying than it appears to be.

Below this elite in terms of average income is a stratum that we could label *proficians*. Airports and the sky are full of them. They consist of portfolio people, combining consultancies, salaried activity for short periods, entrepreneurial ventures and general money making. Although their numbers may still be small in comparison with the overall population, they have been growing rapidly, and like the elite stratum they are largely detached from the state social protection and regulatory system, seeing their income security through the stock market, occupational health and pension coverage, and their assets. Below them in average income terms are the *salariat*, consisting of the old-style "organizational man" of 20th century fame, in the public sector and in established firms and corporations. They too tend to look to private cover and to non-earned income to give them the income security that they crave. One suspects that the number in this group has shrunk in recent years, but not by as much as is sometimes presumed. The big shifts have come elsewhere.

Below the salariat comes the rump of the working class, the *core* stratum, those in manual, "skilled" wage labour, whether in manufacturing, mining or services. This is the group for whom the welfare state was created and this is the group that has shrunk to minority status in all industrialized countries, making the social solidarity principle based on its behaviour and its needs rather anomalous.

The real growth in numbers has come below that shrinking core, in three distinctive strata. Next down in terms of income are those who make up what we can call *flexiworkers*. These include all those who flit between jobs and work statuses, having little employment security, minimal job security and very little of any of the other forms of labour-based security. Welfare state and regulatory mechanisms have been adjusted to try to take account of their needs, but in most respects have done so only imperfectly, often producing moral hazards and sub-optimal compromises.

Below that mushrooming category of flexiworkers come the *unemployed*. It may seem strange to think of this as a distinct stratum. But there does seem to be a group of people in most industrialized countries who spend more time in the status of unemployment than in employment spells, living lives of interrupted periods of marginal economic activity. Long-term unemployment was not expected to be a feature of welfare state capitalism. Its existence and persistence have been instrumental in policymakers changing the character of social protection, making it far more regulatory in design.

Finally, there is a sad stratum in all societies best described as the *detached*. This seems to be much larger than used to be the case and consists of what some would call *lumpenised* groups of sad victims of our competitive economies, losers who struggle to retain some semblance of human dignity and sundry others who do not wish to adjust functionally to a winner-takes-all mentality. It would be good if paternalists everywhere would be less vindictive, less judgmental and less patronizing towards this stratum. But for our purposes, their existence does pose a challenge to any pension reform agenda.

The principal relevance of this sort of conceptualization is that societal fragmentation suggests that there is likely to be a generalized detachment from any mainstream state system based on social solidarity. One might say that the top three strata are detached by fortune, the bottom three detached by misfortune.

4. Ageing: Demographic Time Bomb or the Spark of Good Society?

Ageing is conventionally seen as a problem, and particularly as a threat to pension systems and national economic growth. The popular image is of a bunch of elderly folk, frail, on walking sticks or cluttering up over-burdened hospitals and old-people's homes while a dwindling proportion of the population are labouring to support them. There are good reasons for being a little cautious about accepting this alarmist imagery.

What is meant by 'ageing'? The conventional way of looking at the situation is to point to long-term changes in the ratio of those aged 15-64 to those aged 65 and older. This reflects *individual ageing* (people living longer on average) and *population ageing* (due to declining fertility coupled with increased longevity). Due to declining fertility after the "baby boom" generation, the annual intake into the 'prime age' bracket has only recently begun to fall in most industrialized countries. But because of increasing longevity among older people, the old-age dependency ratio has risen steadily. After about 2010, in most industrialized countries that ratio is scheduled to rise quite sharply. There might be a medical breakthrough to raise it further – and demographic forecasts used by insurers have traditionally consistently underestimated the rising life expectancy – but otherwise we can be confident that the rise will be close to that forecast.

The demographic figures are quite clear. In 1960, across all industrialized countries the population aged 65 and over was equal to about 15% of the working-age population. By 2030, the figure will probably be 35%. In 1960, men could expect to live about 68 years with 50 of those years being in employment. Now, men can expect to live about 76 years, with merely 38 years being in employment. Any likely change in fertility will make little difference to this trend. In Western Europe, there are about 22.4 persons over 65 for every 100 persons of working age; this is expected to rise to 32.3 in the next twenty years.[5]

A third well-known feature of the long-term trend is the changing pattern of labour force participation, which might even be called *early ageing*. The second half of the 20th century saw female participation rates rising everywhere, while male participation rates declined for all age groups, and not just for older men, although they fell most for men in their 50s. This means that the effective dependency ratio has risen by more than the purely demographic ratio. It is generally argued that the labour market marginalisation of older men should be reversed. How to do so is one of those much-discussed big questions of social policy. But it must not be overlooked that while the male labour force participation rates have fallen – and for those over age 60 the fall has been very substantial – female labour force participation has risen, and this includes the group of women in their 50s.

There are also two aspects of what might be called the *de-ageing* of society. First, on average older people are *healthier* than used to be the case, and consequently

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[5] United Nations Population Division, World Population Prospects, the 1998 Revision (New York, UN Publication, !998), Table A29.

are able to be more active for longer and are able to maintain a high level of consumption relative to their income, if only because they can travel more. One implication is that more of the elderly are likely to want to do some income-earning work well beyond either the "early retirement" age or the standard retirement age. Probably far more are doing so without that being recorded.

Second, older people are more likely to want to do some labour force work, because the pattern of income-earning opportunities has been changing, with more flexibility meaning more variety of work options to suit individual preferences and capacities, because fewer young workers are coming onto the labour market, and because the rise in female labour force participation has reached the stage of coming mainly from *older women*. So, although the image is still one of older worker marginalisation (the main story of the 1980s and 1990s), barriers to the economic activity among older workers are probably coming down.

One senses that ageism in the labour market is actually weakening, paradoxically at a time when pension reformers and politicians are calling for measures to reduce age discrimination. While policies could accelerate the process, the task may be easier than would have been the case a decade ago. The barn door is already open.

5. Pensions: Basic Economics and Emerging Issues

The stylized facts are as follows. Public pensions have been under fiscal pressure because of rising old-age dependency, longer life expectancy among pensioners (and more contributors reaching pension age), erosion of worker and employer contributions, and higher and longer-term unemployment. None of this has made PAYG pension systems unaffordable, contrary to what many commentators have claimed or assumed.[6] But the alarm is real. For instance, the European Round Table of Industrialists, representing over 40 leading EU companies, described the European situation as a "time bomb" threatening Europe's competitiveness.[7]

The projected growth in the "cost" of pensions as a share of GDP in various European countries gives some support to this alarmist vision (Table 1). But what is remarkable is that countries have had very different levels of pension costs, and some countries have managed to sustain a level more than twice that projected for the UK at its projected height.

One cannot dismiss out of hand the possibility that part of the pressure to roll back public pension schemes is a reflection of vested interest. After all, reducing pension "generosity" (a loaded euphemism for what some observers might call adequacy) is in the interest of those who make profits out of pension funds or who wish to do so. This is one reason for making sure that objective, accountable and independent evaluations of alternative options are made and for making good governance of any pension system a high priority, such that *all* interests are taken into account in the design, implementation and evaluation of pension schemes.

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[6] For example, according to Howard Glennerster, of the London School of Economics, in countries such as France, Germany and Japan, governments have been "promising their future elderly populations state pensions that cannot be remotely met from present taxes and social security contribution rates." Cited in The Financial Times, July 2, 1999, p.9.

[7] The Financial Times, November 17, 1999, p.2.

Table 1: European Pension Costs: Time Bomb?
(Projection as a % of GDP)

	1995	2000	2010	2020	2030	2040
Belgium	10.4	9.7	8.7	10.7	13.9	15.0
Denmark	6.8	6.4	7.6	9.3	10.9	11.6
Germany	11.1	11.5	11.8	12.3	16.5	18.4
Spain	10.0	9.8	10.0	11.3	14.1	16.8
France	10.6	9.8	9.7	11.6	13.5	14.3
Ireland	3.6	2.9	2.6	2.7	2.8	2.9
Italy	13.3	12.6	13.2	15.3	20.3	21.4
Netherlands	6.0	5.7	6.1	8.4	11.2	12.1
Austria	8.8	8.6	10.2	12.1	14.4	15.0
Portugal	7.1	6.9	8.1	9.6	13.0	15.2
Finland	10.1	9.5	10.7	15.2	17.8	18.0
Sweden	11.8	11.1	12.4	13.9	15.0	14.9
UK	4.5	4.5	5.2	5.1	5.5	5.0

Source: Financial Times, 23 Nov. 1999.

In that context, it may be useful to summarise the main objectives of reformers, whether in the UK or elsewhere. I am not necessarily subscribing to the validity of the objectives, and the order below does not reflect any implied order of significance:

- Reduce fiscal pressures on pensions, due to ageing, rising dependency, etc.
- Reverse the marginalisation of older workers.
- Overcome the tendency for some pensioners to be impoverished, while many others have "over generous" incomes in retirement.
- Cut national insurance contributions in the interest of improving industrial "competitiveness" and labour market flexibility, so promoting employment.

Whether the existing pressures amount to a crisis or not, they have induced various responses that have curtailed pension entitlements in one way or another – and look likely to curtail them far more in the near future. In the process, many of the changes have eroded the insurance principle little by little. The possibility that the morality of the responses will become more tendentious is a little cloud on the horizon.

Actual responses have been of two types – *incremental* or *radical*. Although all are familiar to participants in this conference, it might be useful to recall the various measures that are on the reformers' table.

6. Incremental Options

- *Raise the retirement age*. This is happening in several countries, and of course in the UK the retirement age for women has been raised from 60 to 65, as it has in Greece. Raising the age further is the preferred option of several lobbyist groups, such as the European Round Table of Industrialists and various other organisations.8 The UK's National Association of Pension Funds has called on the Government to raise the retirement age from 65 to 70. Merrill Lynch has

[8] For instance, OECD, Ageing in OECD Countries: A Critical Policy Challenge (Paris, OECD, 1997), p.17.

estimated that if the retirement age was raised by stages, the old-age dependency ratio would be stabilized (Table 2). One objection to this is the "moving the goalposts" theme. To counter that, the NAPF has proposed that there should be a 15-year "wind down" period before it comes into effect. Another possible objection is that this route persists in treating the life-cycle in the conventional but rigid three phases (school, work, retirement). It may respond to the fiscal pressures, but not to the desire for lifetime flexibility.

One variant of the proposal to raise the pensionable age would be to make the adjustment automatic, by making the retirement age dependant on the current adult life expectancy. Since men and women have different life expectancy this might have to be taken into account by either taking the male life expectancy as the yardstick or having separate retirement ages – perversely implying that women's pensionable age would be *above* that of men. The former option would presumably be preferred.

Table 2: Impact of raising the retirement age in the EU

	1990	2000	2010	2020	2030
% of population of working age					
Where retirement at 65	66	66	67	63	60
Increased retirement age scenario*	66	68	70	67	66
% of population of pensionable age					
Where retirement at 65	14	15	16	20	23
Increased retirement age scenario*	14	13	13	16	17
Pension contribution as % of average salary after increases in retirement age	13.76	12.75	12.38	15.92	17.17

Note: *Effect of raising the retirement age to 66 in 2000, 68 in 2020 and 69 in 2030.
Source: Merrill Lynch. Financial Times, 14 Oct. 1999

- *Lower the income replacement rate of state pensions*. This too has been happening. One obvious objection to this route is that, in effect, it reneges on previous commitments. Persons in their 40s and 50s, in particular, could have contributed or saved on the presumption that their pensions would be a certain level. To change the level as they approach the goal line smacks of moving the goalposts. So, if this is among the most transparent responses, it is also among the least fair, and is probably politically unappealing.

- *Increase contributions rates*. A difficulty with this route is that, ceteris paribus, in some countries the rate would have to rise to very high levels in order to balance costs and benefits. The most drastic case is Italy, where it would have to rise to 48% of average wages if the pensions budget was to be balanced by 2030. In late 1999, the rate was 33%. Raising contributions rates is likely to be politically unpopular, although in an era in which politicians are loath to raise taxes, this may be easier than raising revenue from taxation. Ironically, many national pension systems have come to rely increasingly on general taxation and less on employer and employee contributions. And there has been a shift from employer to worker contributions. The combination of these trends has probably reduced the redistributive character of public pensions.

- *Increase the number of years of contributory employment to qualify for a 'full' pension.* This has been happening in various countries. The number of years of employment used to calculate the amount of pension has risen in such countries as Austria, France, Portugal, Spain and the UK. The upward trend has been prolonged and considerable.
- *Increase the number of years prior to retirement for calculating earnings-related pensions.* This ruse is fairly transparent, although it also prompts questions about the nature of the social compact. To be moderately equitable, it should surely be changed only for those further from age of retirement than the newly stated number of years.
- *Index pensions to prices rather than to earnings*. This is what the UK Government did in 1981. If pensions are linked to earnings, they rise with economic growth, tending to increase fiscal pressure more than if they are linked to price rises, since prices have risen by less than money incomes. However, as we know from the UK's experience in the past two decades, a result of the change is that many more pensioners are impoverished, finding that their pension has fallen further behind average incomes.
- *Make early retirement harder or less financially attractive*. This is widely advocated, and effectively puts into reverse policies introduced in the 1980s, in particular, as a means of lowering unemployment.
- *Give incentives to older workers to remain in employment*. This is not, or should not be, the same as making early retirement harder or less attractive. One way of encouraging people to continue income-earning work is simply to reduce the marginal tax rate on earnings by pension-age persons. In the USA, President Clinton and several Republican Congressmen have recently proposed that all pension recipients aged over 65 should be allowed to earn as much as they wish without losing any pension.[9] This may have an indirect beneficial effect on the budget, since the older workers would pay tax if they declared the income. However, the main positive effect of that move would be that it would not distort decisions on whether or not to work. A second benefit might be that, if it is true that more active people tend to live longer, longevity would rise. Of course, that is scarcely going to ease pressure on pension funds.
- Make pensions rise by more for each year worked in contributory employment after retirement age than for each year of such employment below retirement age. Often at the moment those who work beyond retirement age do not obtain a substantially higher pension when they eventually retire. Making additional years of employment have a stronger positive effect on subsequent pension levels would have the virtue of relying on financial incentives, and would thus be more equitable than the more arbitrary device of rigid rules and regulations limiting access to pensions or measures to reduce pensions for those who have contributed on the expectation that they would receive a higher level.

[9] As of early 2000, social security recipients in the USA aged 62 to 65 lose $1 for every $2 earned above $10,080, those aged 65 to 69 lose $1 for every $3 earned beyond a maximum of $17,000. Those aged 70 or above do not lose anything if they gain earned income.

- *Extend and promote the combination of partial retirement, partial pension*. This is quite popular. In Finland, for instance, this is possible from age 56; in France and Germany, government subsidies facilitate gradual retirement from age 55. This too has the virtue, or could have, of relying on incentives to induce behavioural changes rather than on punitive aspects in pension systems.

- *Compel people to save more*. This is the Singapore route, and is central to private funded schemes. In Singapore, the government forces workers to save 40% of their earnings, most of which can only be tapped when they retire. Other countries have contemplated following suit, and various analysts have proposed its introduction in the UK.[10] It is an example of state paternalism. Its advocates claim that it ensures savings for old-age because many people are short-sighted. It also boosts economic growth by increasing savings. However, there are several objections. First, a high forced savings rate has a similar effect on the propensity to labour as a high tax rate, so that work incentives are affected. Second, and more importantly, it interferes with individual preferences. Some people wish to consume more currently, and spend less later; some have the opposite tendency. The state cannot decide which is preferable without indulging in arbitrary paternalism. Some will be required to save more than they need or desire to save in monetary form. There is a third consideration, which is that according to some empirical research many pensioners have *over-saved* during their working lives if one can assume that smoothing consumption over the lifetime is a rational objective.

- *Allow workers to transfer pensions across national borders*. To some extent this does occur. It may not be seen as a reform to lower fiscal pressures. However, as a measure that promotes labour mobility it might raise older worker employment, and thus indirectly lower unemployment and a demand for public transfers and early pensions.

- *Reduce or remove tax breaks on savings for pensions.* One could use the extra tax revenue from this move to help pay for a public basic pension. There is no evidence that pension saving is in need of a fiscal incentive, especially bearing in mind that those likely to be saving are middle-income or upper-income earners, whose pension income replacement rates have been high.

- *Allow pension funds to invest in foreign markets more easily*. In some countries, allowing pension funds to invest where they wish in order to obtain a high rate of return would presumably reduce any fiscal pressure.

- *Co-ordinate tax and regulatory treatment of pensions internationally*. This of course is one of the major policy dilemmas in the European Union. An orderly system would presumably be a more stable one, and costs could thus be reduced. But it is unlikely to make a vast difference to the fiscal and labour market pressures.

This list of policy options is far from complete. What they suggest is that it would be grossly simplistic to focus on just one or two options to the exclusion of others.

[10] See, for instance, B.Jupp, “Reasonable force: The place of compulsion in securing adequate pensions” (London, Demos, February 1998).

7. Multi-Tierism

All of the measures mentioned in the preceding section can be described as incremental. But perhaps the main response has been the reform of pension systems in the direction of funded schemes, and in particular to multi-tierism. Actually, it is hard to identify any modal pension system, because in most countries a hybrid has long been in place.[11] During the 1980s and 1990s, there was an international trend to a mixed contributions-and-assistance pension structure (Table 3). The changes have continued, led by the major reform in Sweden.

Table 3: Paths towards Mixed Contributions-and-Assistance Pension Systems in West European and Anglo-American countries, mid-1990s

Type of scheme	Tax-financed minimum pension	Minimum plus compulsory contribution-based (dual mandatory system)	Subsidised voluntary schemes	Compulsory contribution-based
First pension scheme[a]	Australia, UK, Canada, Denmark, Iceland, Ireland, New Zealand, Norway, Sweden,		Belgium, France, Italy, Spain	Austro-Hungarian Empire, Finland, Germany, Greece, Netherlands, Portugal, Switzerland, USA
Pension structure in 1996	Denmark[b], Ireland[c], New Zealand	Australia, Austria, Belgium, Canada, Finland, France, Greece, Iceland, Italy, Norway, Netherlands[d], Portugal, Spain, Sweden, UK, Switzerland, USA		Germany[e]

Notes: [a] Some countries adopted a mixed approach from the beginning, as in Sweden in 1913.
[b] With almost total coverage of occupational pensions and small-flat-rate contribution-based pension.
[c] Minimum pension for employees is contribution-based.
[d] Mandatory membership in 62 of 83 industry pension funds supplementing minimum pension from 1980.
[e] With standardised social assistance. Periods of higher education and registered unemployment, as well as up to three years of child-rearing, count as contribution periods. Pension rights are split between spouses in case of divorce.

Source: Overbaye, 1997, op. cit., p.108.

The great debate of the 1990s was between defenders of a standard PAYG system and proponents of privatized, fully funded, defined contribution schemes.

[11] E.Overbye, "Mainstream pattern, deviant cases: The New Zealand and Danish pension systems in an international context", Journal of European Social Policy, Vol.7, No.2, 1997, pp.101-17.

While there are diehards in both camps, with some of the latter being ideologically driven by the desire for a fully privatized, individual account system, by now a majority of analysts around the world favour some variant of a multi-pillar system. Employer-sponsored defined contribution schemes have spread and are expected to continue to do so (Table 4).

Table 4: Employer sponsored defined contribution schemes

	% of employer-sponsored plans that are DC		Typical contributions as a percentage of salary	
	1998	2003	Employee	Employer
Austria	10	30	15.0	5.0
Belgium	45	60	5.0*	10.0*
Czech Republic	100	100	2.0	0.5
Denmark	90	95	4.0	8.0
Finland	0	2	na	na
France	40	50	2.0	3.0
Germany	10	12	0.0	4.0
Greece	40	50	0.0	5.0
Hungary	100	100	1.0	5.0
Ireland	32	45	4.0	6.0
Italy	80	90	1.5	1.5
Netherlands	5	8	4.0	8.0
Norway	0	2	na	na
Portugal	15	20	0.0	3.0
Spain	50	65	2.0	6.0
Sweden	50	75	0.0	8.0
Switzerland	50	60	5.0**	9.0**
UK	25	35	2.0	4.0

Notes: * Or 1% and 2% if salary is below social security ceiling
** Or 4% and 8% if contracted out of state earnings related pension scheme
Source: William Mercer. Financial Times, 5 Oct. 1999.

In the international arena, publication of the World Bank's Averting the Old Age Crisis in 1994 was notable for its huge cost, its unbridled advocacy of radical reform in the direction of individual funding, and its timing. The World Bank has devoted much money and technical advice to the effort to induce governments to reform their pensions in the direction of private funded schemes, particularly in central and eastern Europe. Although one should be hesitant about mentioning a family scrap, it is notable that the most strident critique of the World Bank's approach has come from its own Chief Economist. Although he has recently resigned from that post after completing his three-year stint in the post, he has lambasted the reform agenda in a characteristically trenchant manner.[12] Others have pointed out the large fiscal costs of a transition from a PAYG system to a fully-funded one.[13] And many

[12] P.R. Orszag and J.Stiglitz, "Rethinking pension reform: Ten myths about social security systems", paper presented to Conference on "New ideas about old age security", Washington, DC, The World Bank, September 14-15, 1999.

have pointed out that the risks and uncertainty increase for the poor and for those in precarious jobs.

However, here is not the place to try to summarise the debates.[14] I would like to make just three points, all related to the labour market flexibility and socio-economic stratification issues raised earlier.

First, if there is going to be a global trend to multi-tier systems in which a mandatory funded tier is to be a rising part of the total, what should be the anchor of the system? There is a fear among some observers that the thrust of reform in the direction of "social safety nets" and the "reduction of the burden of pensions" implies lower pensions for the poor.[15] Presumably, there should be a floor, so that everybody in society receives a basic pension of some sort. In the 21st century one hopes there is no place for a system that envisaged a category of undeserving elderly poor disentitled to any public transfer.

What should the *basic pension* be? And on what basis should it be calculated and distributed? The two main options are a flat-rate guaranteed citizenship pension and a means-tested basic pension. Means-testing (and other 'targeting') has been popular with governments in recent years, and all over Europe the number of people dependant on means-tested benefits has increased enormously. Questions persist about low and uncertain *take-up* rates, the stigma of such benefits, administrative costs, the costs relative to the savings supposedly gained from such systems, moral hazards (pensioners just above poverty impoverishing themselves in order to gain a pension), and poverty traps (people being discouraged from doing some income earning activity because they fear losing their basic pension). There is also, or should be, a concern that policy in this direction is guided by an unstated cynicism: The welfare loss to pensioners of the moral hazards and the consequences of the pension trap are economically insignificant, so can be ignored. If this thinking is occurring, it is deplorable.

By contrast, a guaranteed citizenship pension would not only ensure that all elderly people would have basic income security with dignity but would minimize administrative costs, while also facilitating more flexible lifestyles in which those capable of engaging in income-earning work, and wanting to do so, could engage in such work without being penalized. If we want to promote a work-based society in which the poor and educationally less well-endowed can indulge in their work enthusiasms into old age, then moving in this direction should be a high priority.

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13 S.K.Chand and A.Jaeger, "Aging populations and public pension schemes" (Washington, DC, IMF Occasional Paper 147, December 1996).

14 For good reviews, see L.Thompson, Older and Wiser: The Economics of Public Pensions (Washington, DC, The Urban Institute Press, 1998); D.M.Nuti, "Alternative pension systems: Generalities and reform issues in transition economies" (London, London Business School, April 1998). As a general point, I would argue that at the very least eastern European countries have been pushed into private funded schemes *prematurely* before sound financial markets, regulatory systems and economic stability were assured. The reform in Kazakhstan was particularly irresponsible, and even in Poland the recent severe teething pains were predictable.

15 This latter view has been argued by John Eatwell, among others. For a critique of the impact of selectivity and the euphemism of a social safety net as applied in eastern Europe, see G.Standing, "The folly of social safety nets", Social Research, Vol.64, No.4, Winter 1997, pp.1339-80.

Second, with a multi-tier pension system means definitionally that most people will be primarily interested in preserving the value and security of the contributions-based tiers. If the system works reasonably efficiently, the vast majority will be concerned almost exclusively with those tiers and regard the bottom tier as of marginal relevance. This raises the awkward question that should be called the *legitimation crisis* of social protection. If the bottom tier is only of substantive importance for those in the bottom three strata of society, and if they do not conform to the modal voter, will there be a tendency to allow the real value of the bottom, state tier to wither? The answer may well be that this is precisely what will happen, especially if the social solidarity principle has been eroded.

Third, a multi-tier system in which private schemes predominate poses major challenges for *regulation* and *governance*, which are linked to the previous points. Even staunch advocates of privatization acknowledge the need for strong government regulation.[16] The risks and uncertainty for contributors are substantial, and are greatest for the most vulnerable, those who are the "near poor", which include most flexiworkers and the more fortunate of the unemployed and detached. These are least likely to be well-informed, least likely to be able to afford losses from misguided investments and to be able to maintain regular or adequate contributions over a prolonged period.

Pensioners and the state cannot afford to allow pension funds to be reckless in their use of investors' funds, and they are unlikely to favour a highly fragmented pension fund system, because an industry characterized by numerous small funds would tend to be an unstable one, with many failures jeopardizing pensioners' incomes. So, governments will always wish to regulate pension funds in some way. A quite different concern arises from the tendency of pension funds to operate in a "pack" or "herd" fashion. If, for instance, the main pension funds all invested mainly in "tracker" funds, those following something like the FTSE, their size would mean that investment would be concentrated in a small range of firms.

The state of debate on privatization of pensions and multi-tierism is such that a major stocktaking is required. The World Bank, the OECD, the ILO and the International Social Security Association all conducted lengthy reassessments in the 1990s. However, they did those at a time of major reforms and restructuring, in an atmosphere of controversy and some acrimony. It is perhaps appropriate to put pressure on all those bodies to carry out a joint review of theories and evidence in the light of the many reforms carried out not just in Europe but all over the world in the 1990s. This might be something like an international *Commission* – a real case of global multi-sectoral governance, not to produce a set of directives but a balanced assessment of the advantages and disadvantages of all the options. Smaller countries, and emerging market economies, deserve that service from the international community.

8. Concluding Thoughts

> *"It has been difficult to speak about older people in terms of their contributions, social roles, and place in the economy to people who*

[16] E.James, "Public pension plans in international perspective: Problems, reforms and research ideas", in S.Valdes-Prieto (ed.), The Economics of Pensions: Principles, Policies and International Experience (Cambridge, Cambridge University Press, 1997).

assume that elders fall only into the category of those in need. It is hard to speak of possibilities to people who can related only to pity."

Julia Tavares Alvares.

Globally, the biggest issue for pensions in ten years time will be called China. It is about to become an "old" country, with more pension-age people than any other country in the world. By then, the upheavals taking place in pension systems in Europe and other parts of the world should have settled down. The privatization of pensions will raise issues of governance and of equity, through finding ways of ensuring that everybody has entitlement to a basic level of provision. The two sets of issues are related. And they lead us back to that awkward social objective of public transfer schemes – the social solidarity principle. Should state pensions try to fulfil the role of strengthening social cohesion?

There is another way of looking at the current state of debate, which is that in 21^{st} century society, the partitioning of life into the three standard phases of childhood (plus schooling), working life and retirement will cease to be the norm. We should think more in terms of people periodically entering and leaving the labour market, changing work statuses, combining work statuses, and taking lifetime sabbaticals at various times over the whole adult age range. It is not too fanciful to imagine us earning "retirement credits" or "work-break credits", or "career breaks", either through a contributions based scheme or acquired as a citizenship right.

As part of this process of positive work flexibility, we may move towards the provision by the state of a basic income, guaranteed as a right regardless of age, marital status, and work status. A universal basic state pension linked to earnings rather than prices, as recommended by the chairman of the National Association of Pension Funds, would be a step in that direction. We may also have citizenship credit cards giving us all entitlements to a certain minimum credit for schooling, training, leave, healthcare and even public transport. It is a time for visionary thinking and visionary action. That is the best attribute of crises.

Table 5: European pension assets

	% of GDP	($'000)*
Austria	4	1.0
Belgium	10	2.5
Denmark	89	31.2
Finland	31	7.9
France	6	1.6
Germany	12	3.5
Ireland	43	9.7
Italy	19	4.3
Netherlands	141	35.5
Norway	24	8.9
Portugal	10	1.2
Spain	4	0.7
Sweden	90	25.3
Switzerland	105	40.3
UK	86	21.0

Note: *Per capita
Source: William Mercer. Financial Times Survey, 5 Oct. 1999.