Brief comments on
Franco-Marino-Zotteri's paper

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Key points

- Fiscal sustainability in EU countries
- Definitions of pension liabilities
- Comparisons of existing projections of pension expenditures and liabilities
- Further progress needed in estimates

Definitions of pension liabilities

- Accrued-to-date liabilities
- Current workers and pensioners’ net liabilities
- Open-system net liabilities

Sustainability (1)

- F-M-Z argue that the size (or GDP ratio) of NPL do not assess the sustainability of the pension schemes.

- That makes sense, but growing NPL should be a warning signal of the sustainability. The dynamics of NPL should be monitored regularly.

Sustainability (2)

- Information from open-system net liabilities

  - Positive OSNL mean that the pension scheme is “incomplete,” in that benefits must be financed from outside.

  - Clear implications to intergenerational equity

The case of Japan (1)

- Case of Employees' Pension Insurance
- Accrued-to-date liabilities (2001)

Gross:	¥ 697 tril.	139% of GDP
Asset:	145 tril.	29%
Net :	552 tril.	110%

to be paid by additional contributions 455 tril.

to be paid by taxes 97 tril.

The case of Japan (2)

- Open-system net liabilities

Gross:	¥ 2,036 tril.	419% of GDP
Asset:	145 tril.	99%
Expected future contributions		
	1,082 tril.	216%
Net:	809 tril.	162%

to be paid by contributions	529 tril.
to be paid by taxes	280 tril.

The case of Japan (3)

- Assimilation to the conventional public debt

Net pension liabilities ¥644 tril.

Net liabilities of the state as a whole ¥844 tril.

=> Net pension liabilities share a substantial part of public debt.

Can we raise the sustainability?

- The strategy is very simple:

  “Do not promise people too much benefits any more.”

- Two methods:

  - A shift to a funded (DC) system

  - A shift to a “pure” PAYG system

Method 1: A funded (DC) system

- Gross pension liabilities and contributions are always balanced for each generation.

- So, no NPL effectively.

Method 2: A “pure” PAYG system

- The total amount of pension benefits paid out is given by the total amount of contributions.
- No future pension rights committed by the government, so no liabilities.

But in both methods…

- The government has to finance the existing NPL (that is, to reduce open system net liabilities).

- Two methods:

  Method A: additional taxes

  Method B: reduced benefits

Comparisons

- Method A: additional taxes on the current and future generations
  - No net benefit from the reform

- Method B: a reduction of promised pension benefits
  - Advisable generational-equitably but unacceptable politically

Cf. 2004 Pension Reform in Japan

- Partially introduces Method A

  automatic adjustment mechanism of total pension benefits ($\leq$revenues)

- Financing the existing NPL

  The current/future generations are implicitly forced to pay additional taxes.

More NPL analysis

- Assessment and comparisons of reform options from a viewpoint of the sustainability and inter-generational equity
- Dynamics of NPL
- Long-term fiscal strategy

The end

Thank you