

# **The Balance Sheet of Social Security Pensions in Japan**

**by**

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# Organization

**Brief Outline of Pension Provisions**

**Demography**

**Basic Facts:**

**Identifying Main JPN Problems**

**The 2004 Reform Bill**

**Sensitivity Analysis**

**Future Policy Options**

**Concluding Remarks**

# **Brief Outline of Pension Provisions before the 2004 Reform**

**2-tier Benefits**

**Contributions**

**The Biggest Business**

# Two-tier Benefits (DB)

## Basic Flat-rate Benefits (PM, PP)

66,200 yen = USD 630

## Earnings-related Benefits (40Yrs)

28.5% of Career Average Monthly Real Earnings

## Replacement Rate (One-earner Couple)

Around 60% Net (233,000 yen = USD 2,200)

## CPI Indexation

Normal Pensionable Age: 65

# Contributions/Transfer from GR

## Contributions

13.58% of **Annual Wages**

13,300 yen = USD 125 (PM, PP)

## Subsidy from General Revenue

1/3 of Flat-rate Basic Benefits

Mainly PAYG, but

with Partial Prefunding

# The Biggest Business in Japan

## Aggregate SS Pension Benefits

44 tr. Yen = USD 420 billion in 2003  
(9% of Japanese GDP)

cf. The Automobile Industry

40 tr. Yen (Domestic Output in 2000)

Rapidly Growing

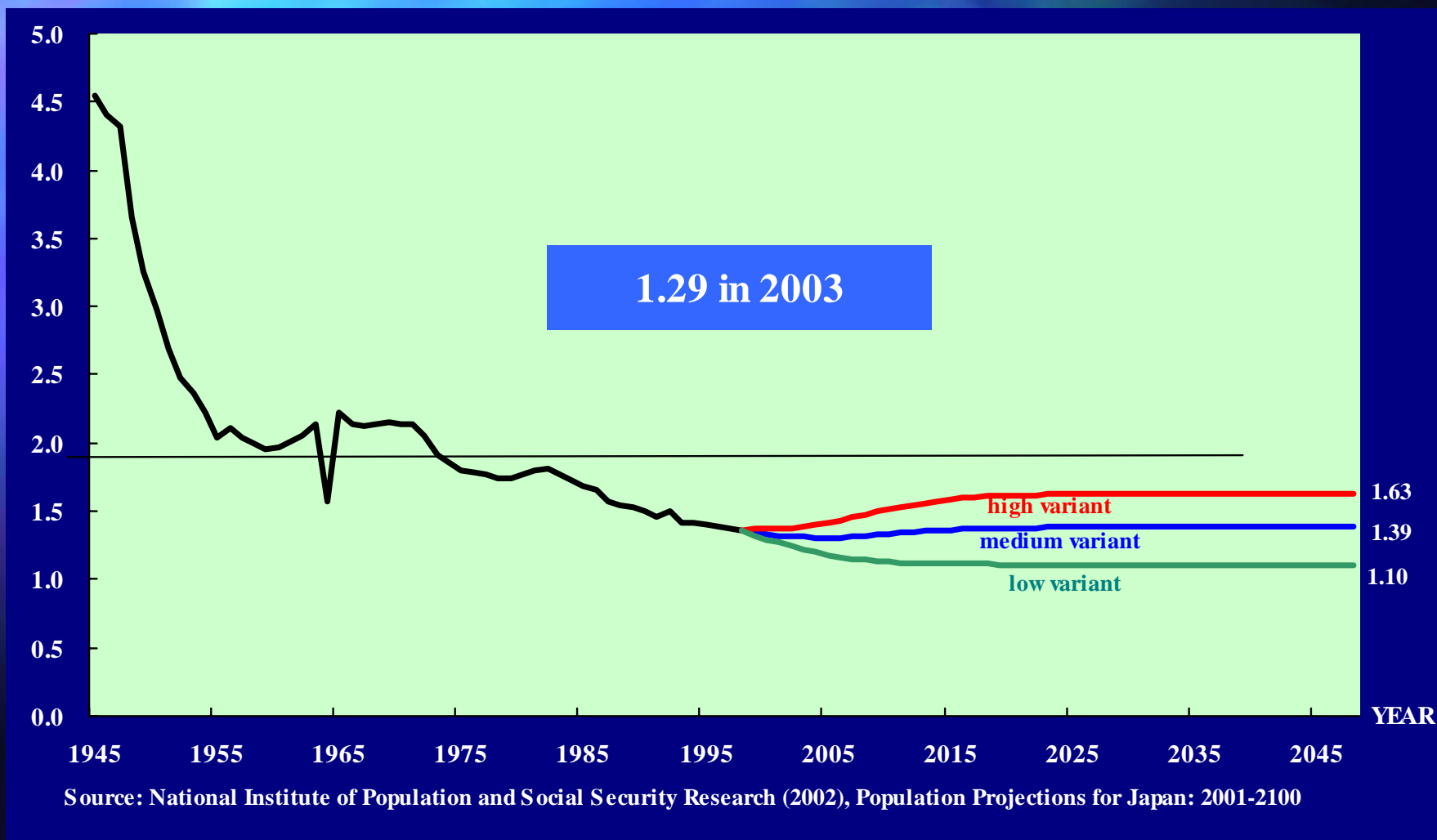
# Demography

**TFR**

**Total No. of Populations**

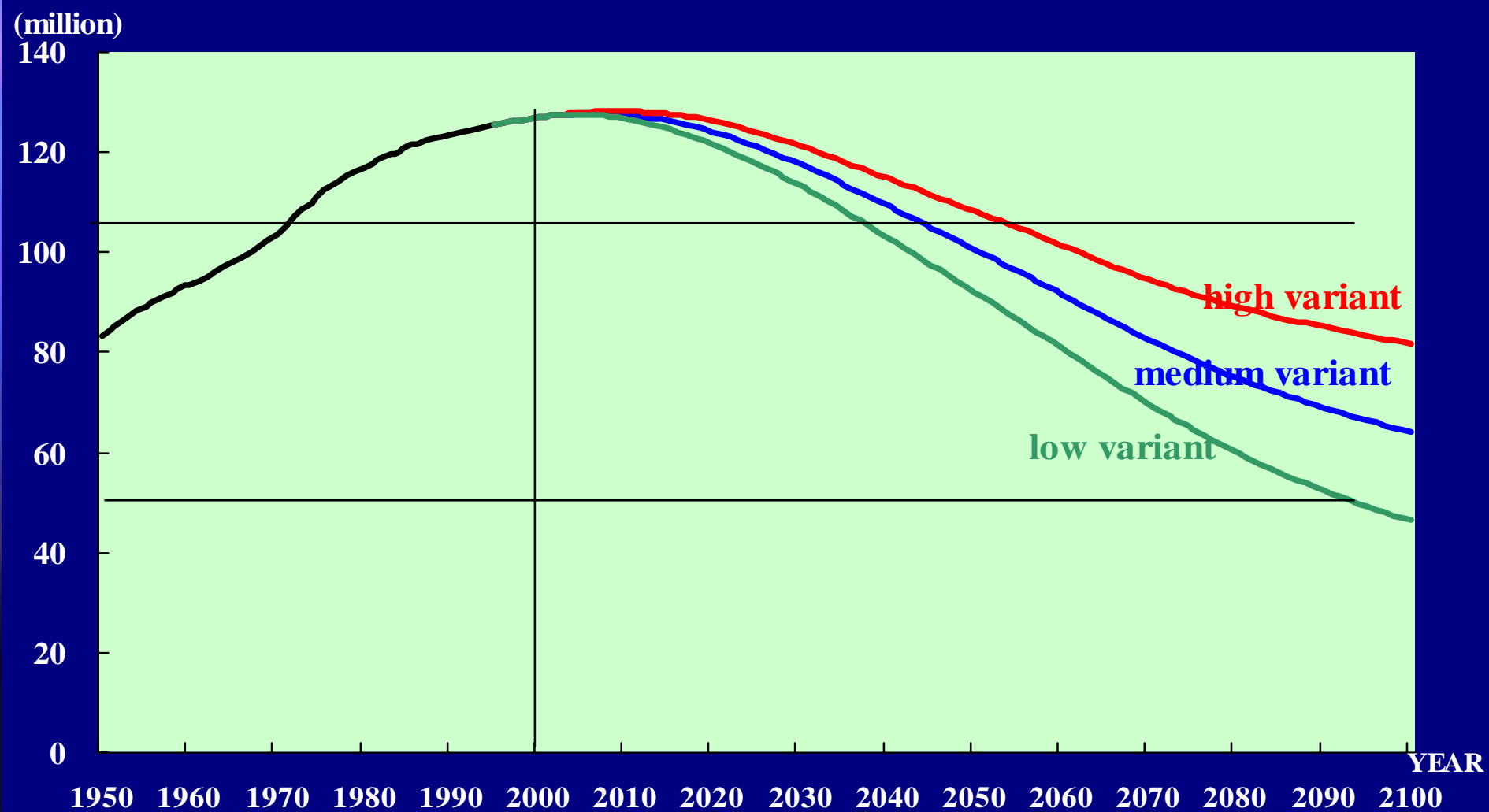
**Proportion of 65+**

# Trends in the Total Fertility Rate of Japan



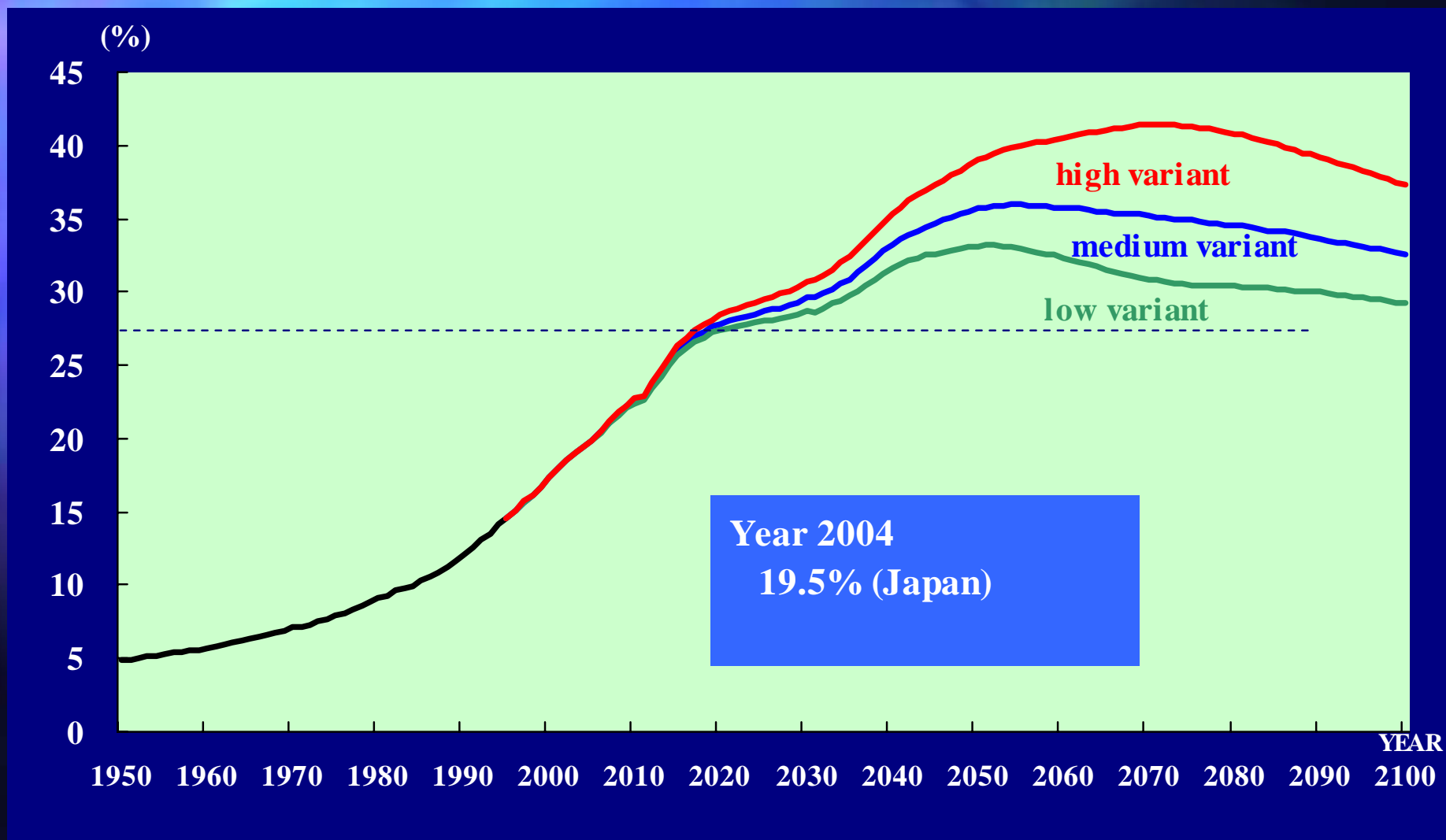


# Actual and Projected Population of Japan



Source: National Institute of Population and Social Security Research (2002), *Population Projections for Japan: 2001-2100*

# Proportion of the Elderly (+65) in Japan



Source: National Institute of Population and Social Security Research (2002), Population Projections for Japan: 2001-2100

# Basic Facts

**Deficit in Current Account**

**Balance Sheet:**

**Huge Excess Liabilities**

**SS Pension Contributions:**

**Heavy Burdens Outstanding**

**Too Much Income Transfers between  
Generations**

**Increasing Drop-out**

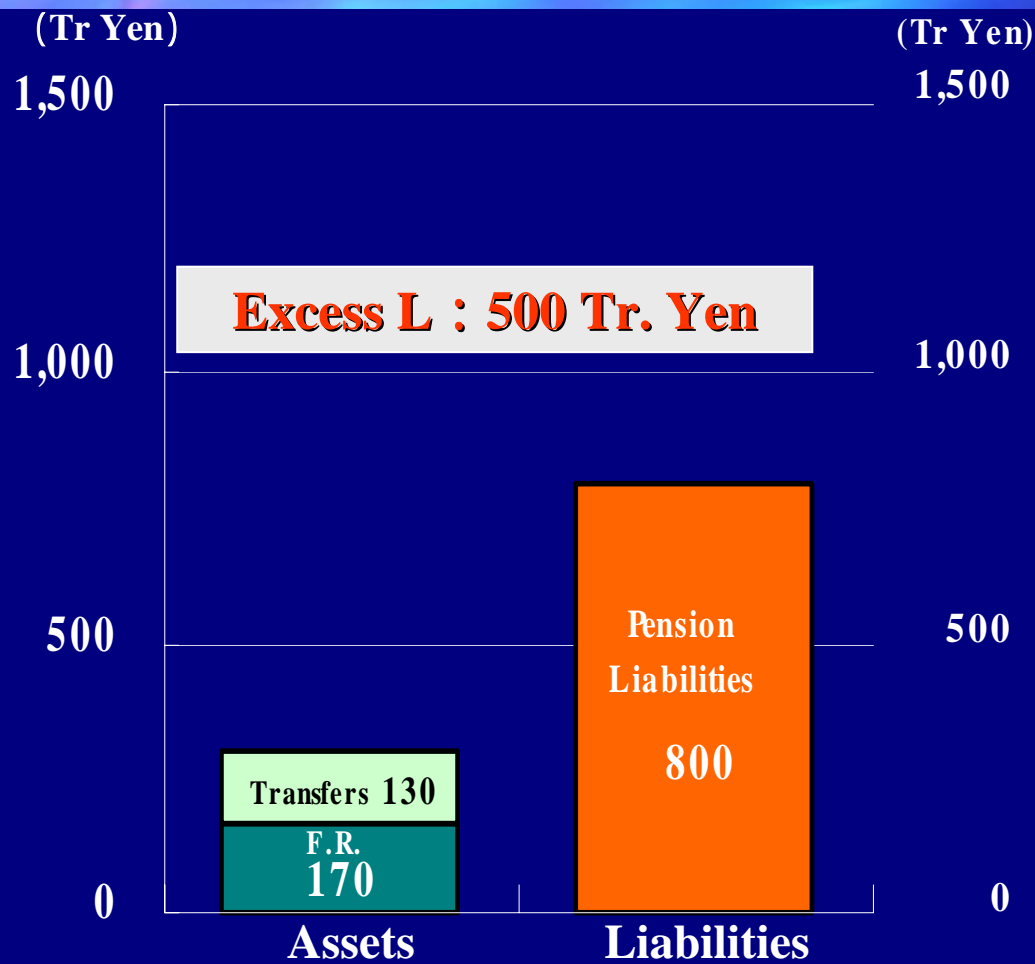
# Current Account of the KNH

(trillion yen)

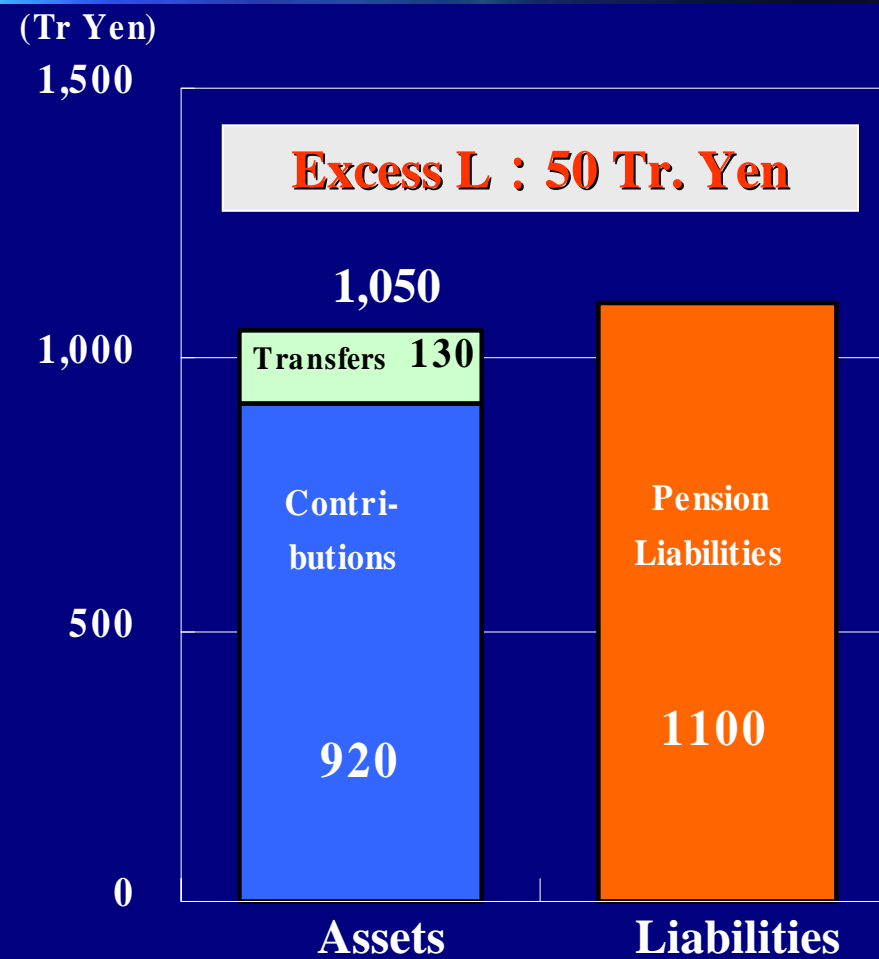


# KNH Balance Sheet: Before Reform

(as at 31<sup>st</sup> March 2005)



Part One (PAST)

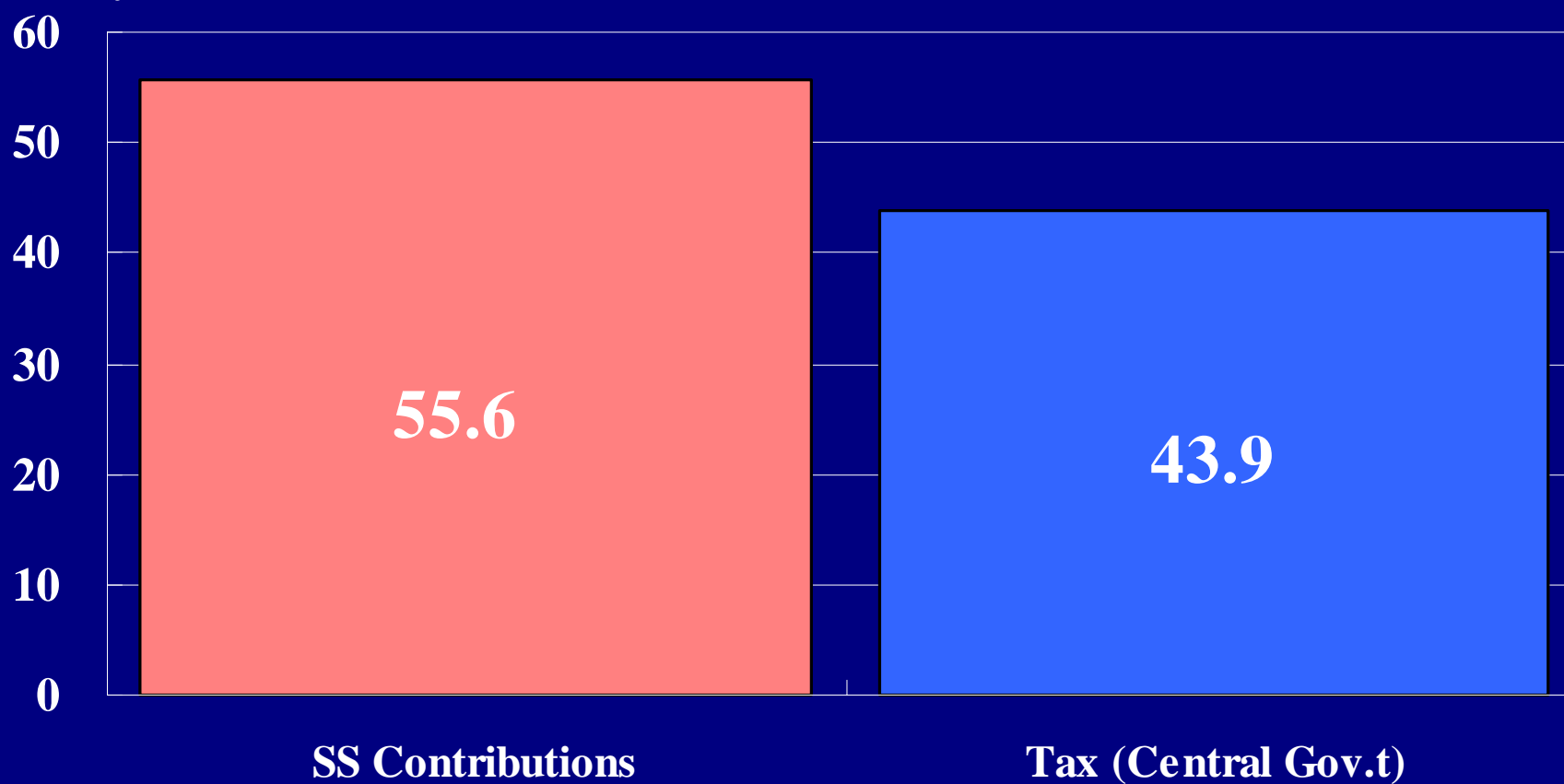


Part Two (FUTURE)

# Which Is More, SS Contributions or Tax Revenues?

FY 2003 National Budget, Japan

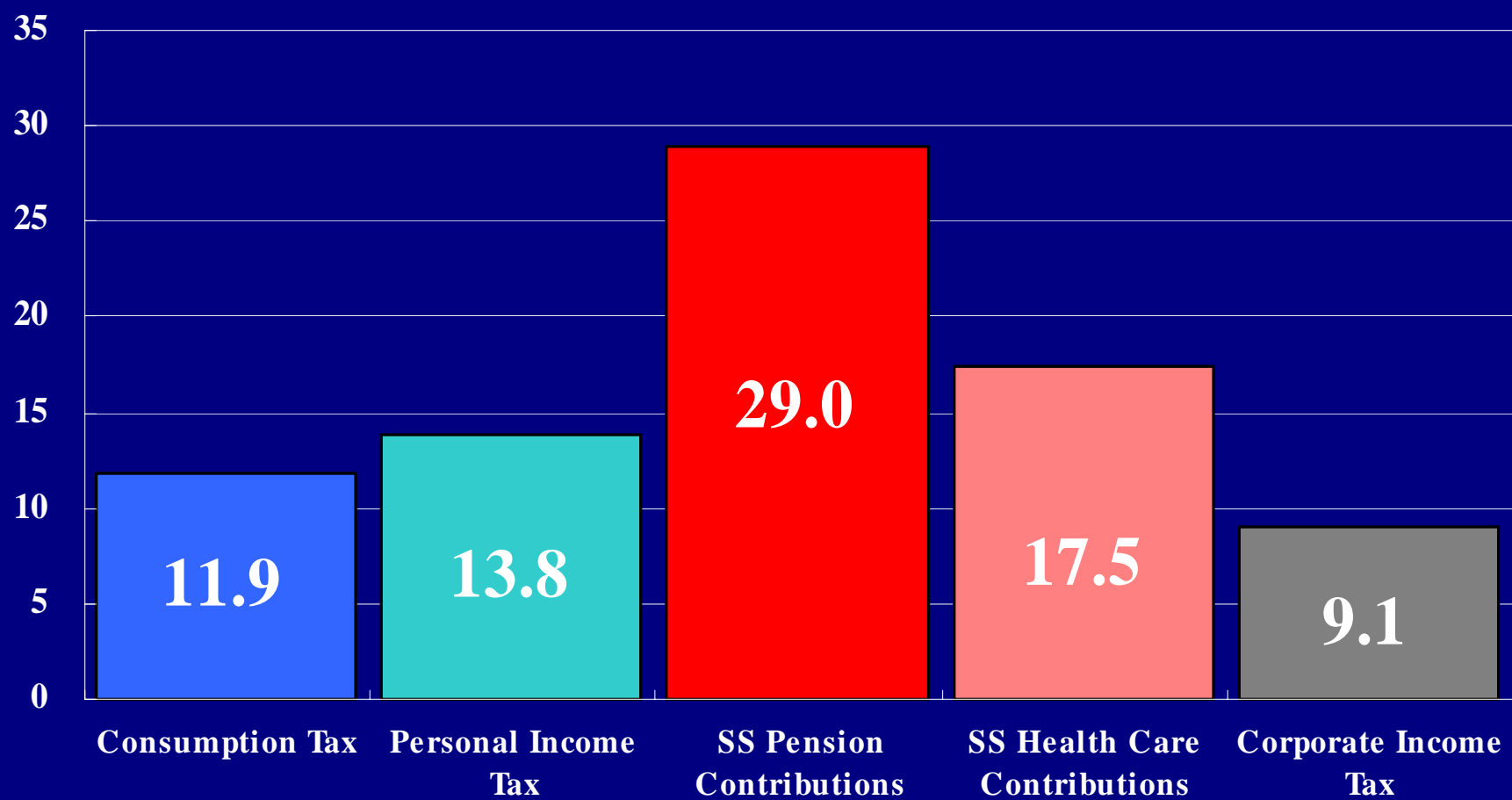
(trillion yen)



# Main Income Sources of Japan's Central Government

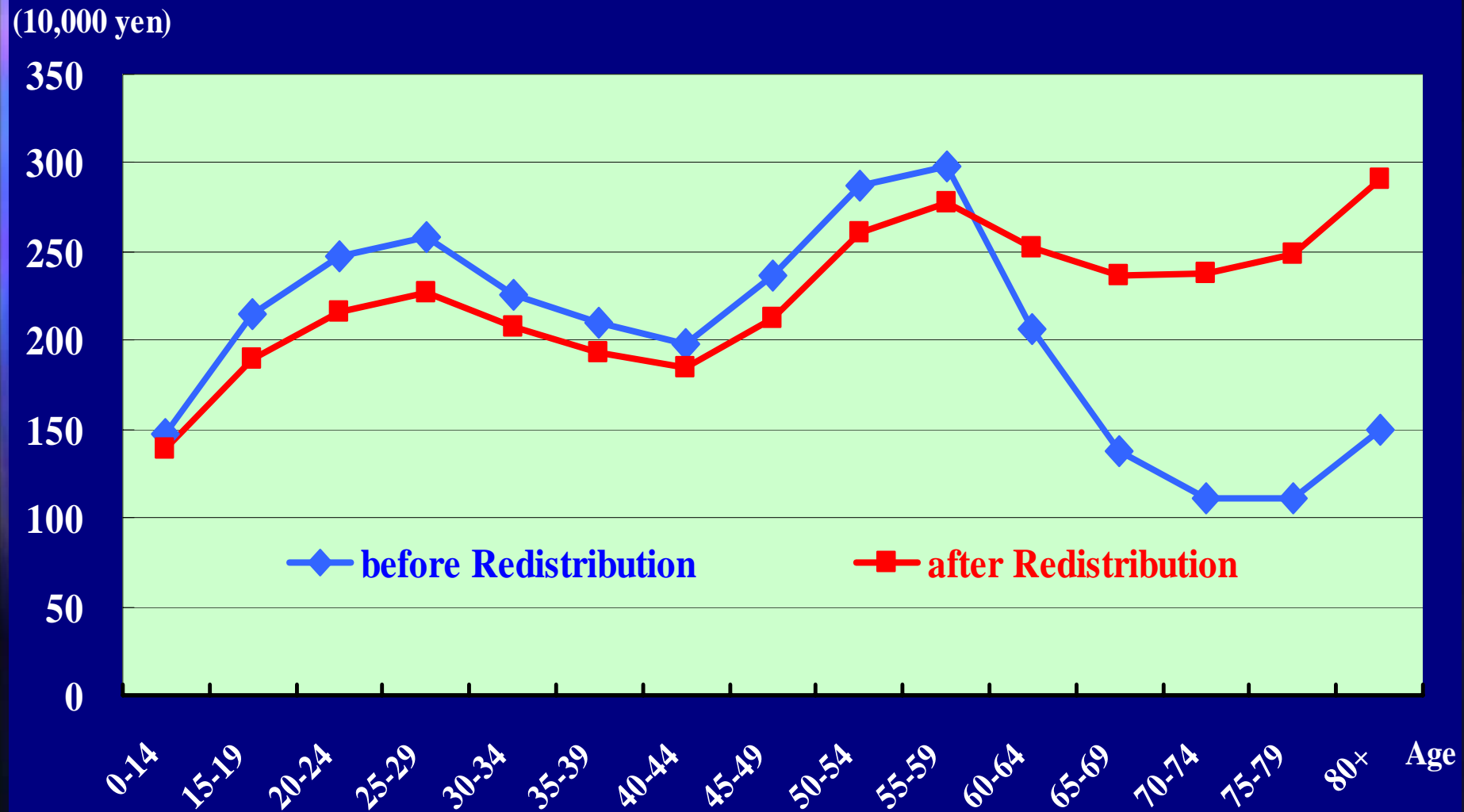
FY 2003 National Budget, Japan

(trillion yen)



# Per-capita Income by Age in Japan

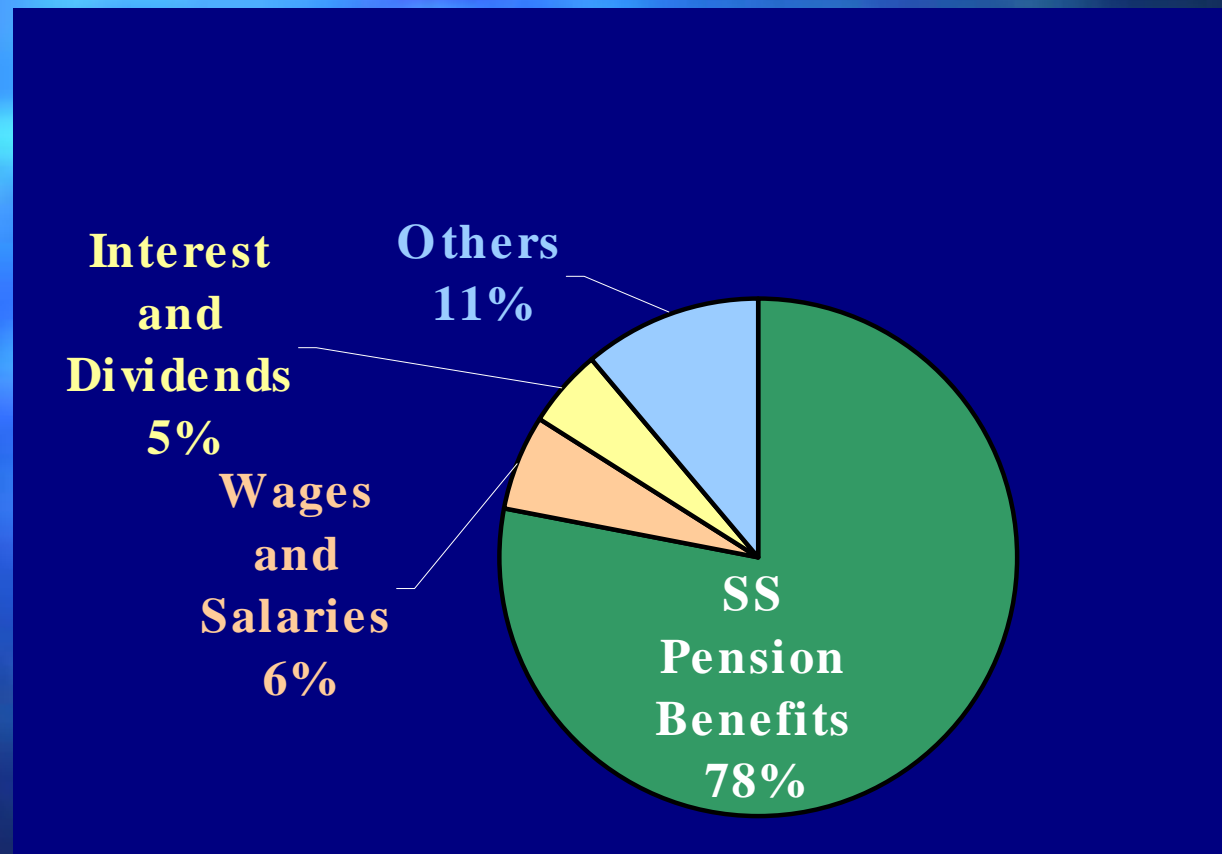
16



Source: Ministry of Health and Welfare, *The 1996 Income Redistribution Survey*



# SS pension benefits are the major source of retirement income

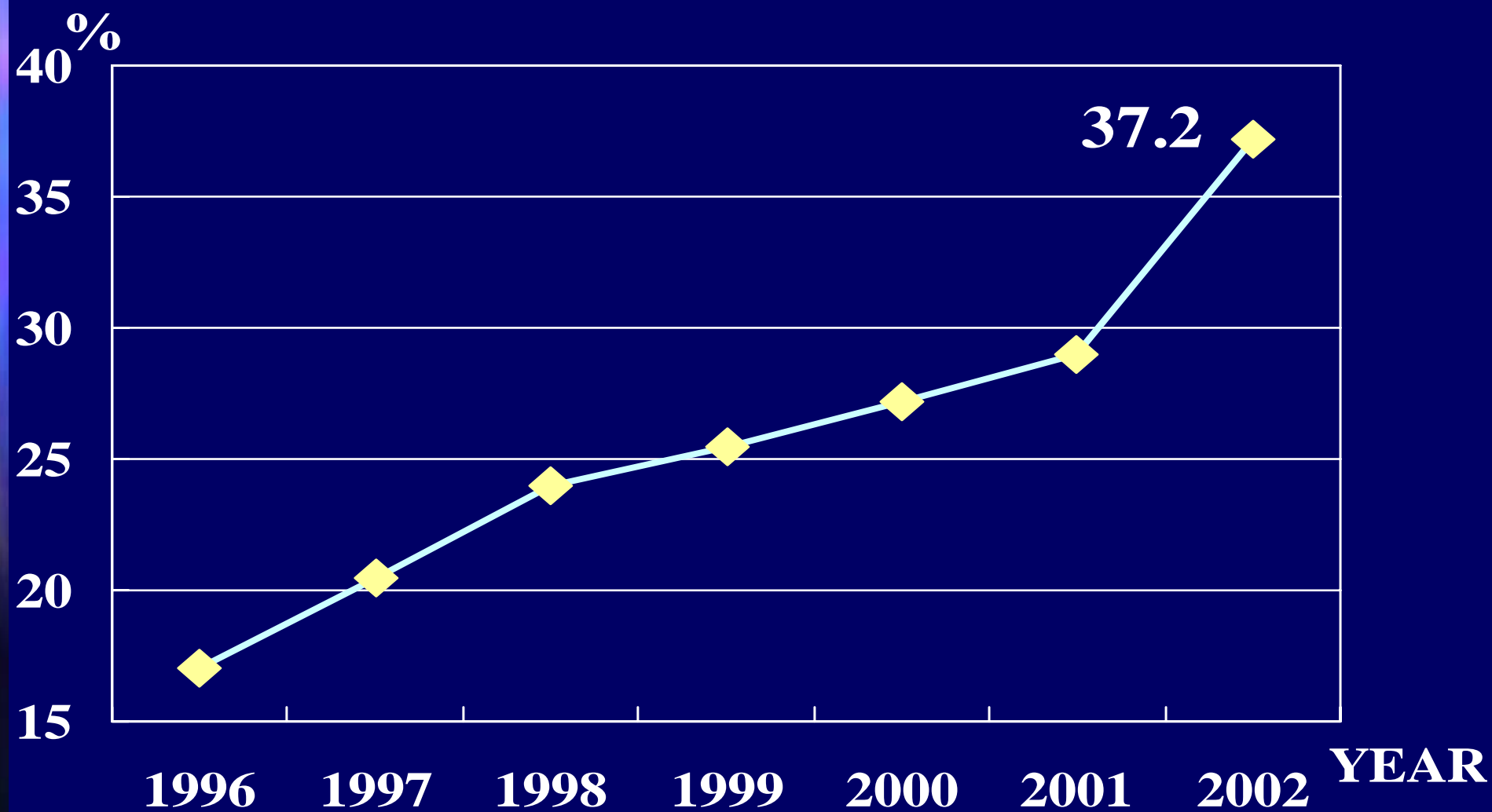


median income: 3.38 million yen

Source: *The 1989 NSFIE* (elderly couples: median income group)

# Drop-out from SS Pensions (Non-employees)

## Delinquency in Paying Pension Contributions



# The 2004 Reform Bill (1)

## Increasing Contributions

by 0.354 point Every Year

18.30% from 2017 onwards

by 280 yen Every Year

16,900 yen from 2017 onwards

## Increasing Subsidies

Flat-rate Basic Benefits (1/3 1/2)

## The 2004 Reform Bill (2)

### Reducing Benefits by Considering “Demographic Factors” in Indexing Benefits between 2005 and 2023

#### Replacement Rate for a “Model” Couple

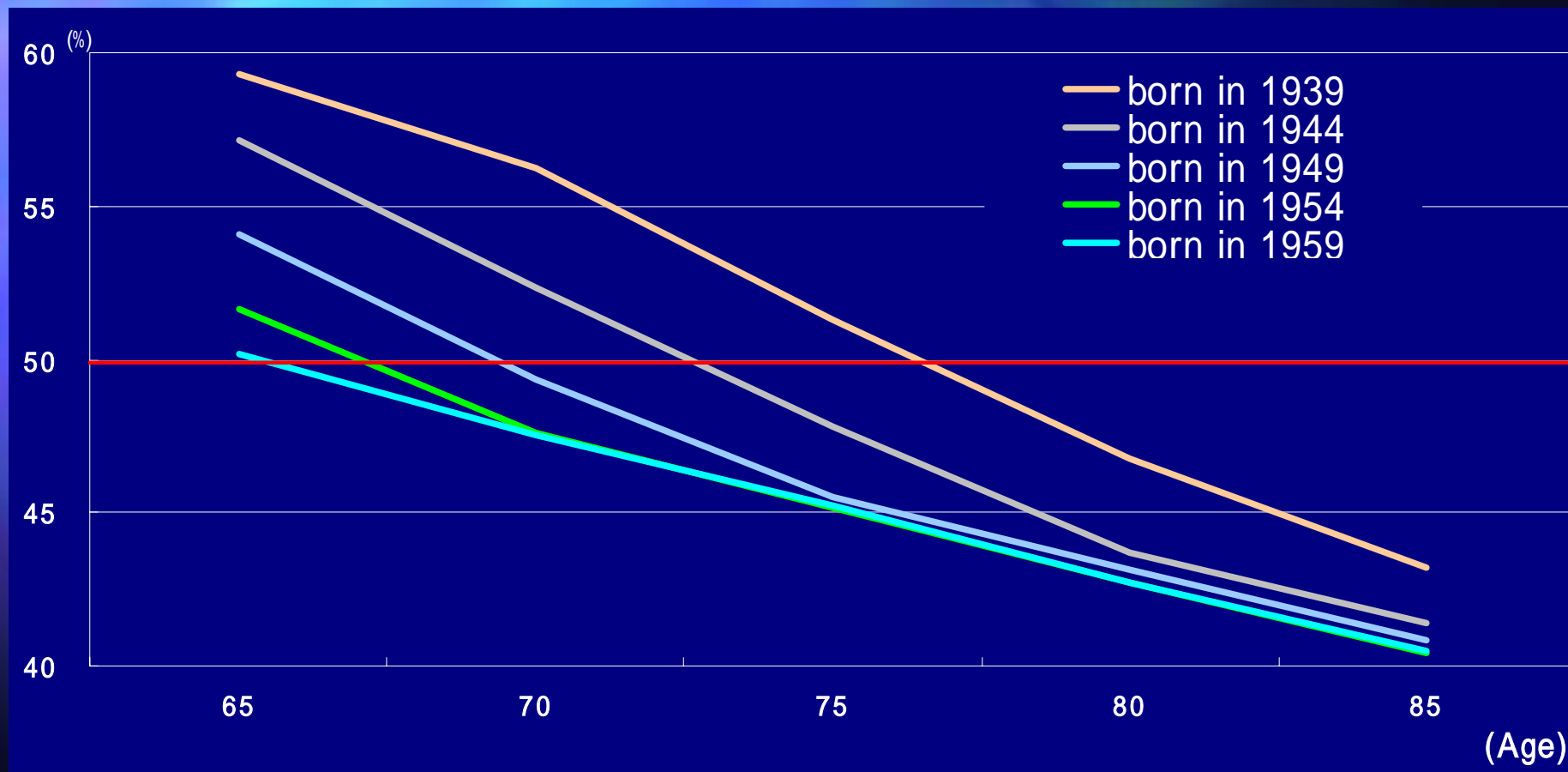
##### Benefits at Age 65:

60% (2004)      50% (2023)

##### Current Pensioners:

60% (Age 65)      43% (Age 84)

# Replacement Rate



# The 2004 Reform Bill (3)

**Relaxing the Earnings-test**

**Earnings-split between Husband & Wife**

**Non-Employees:**

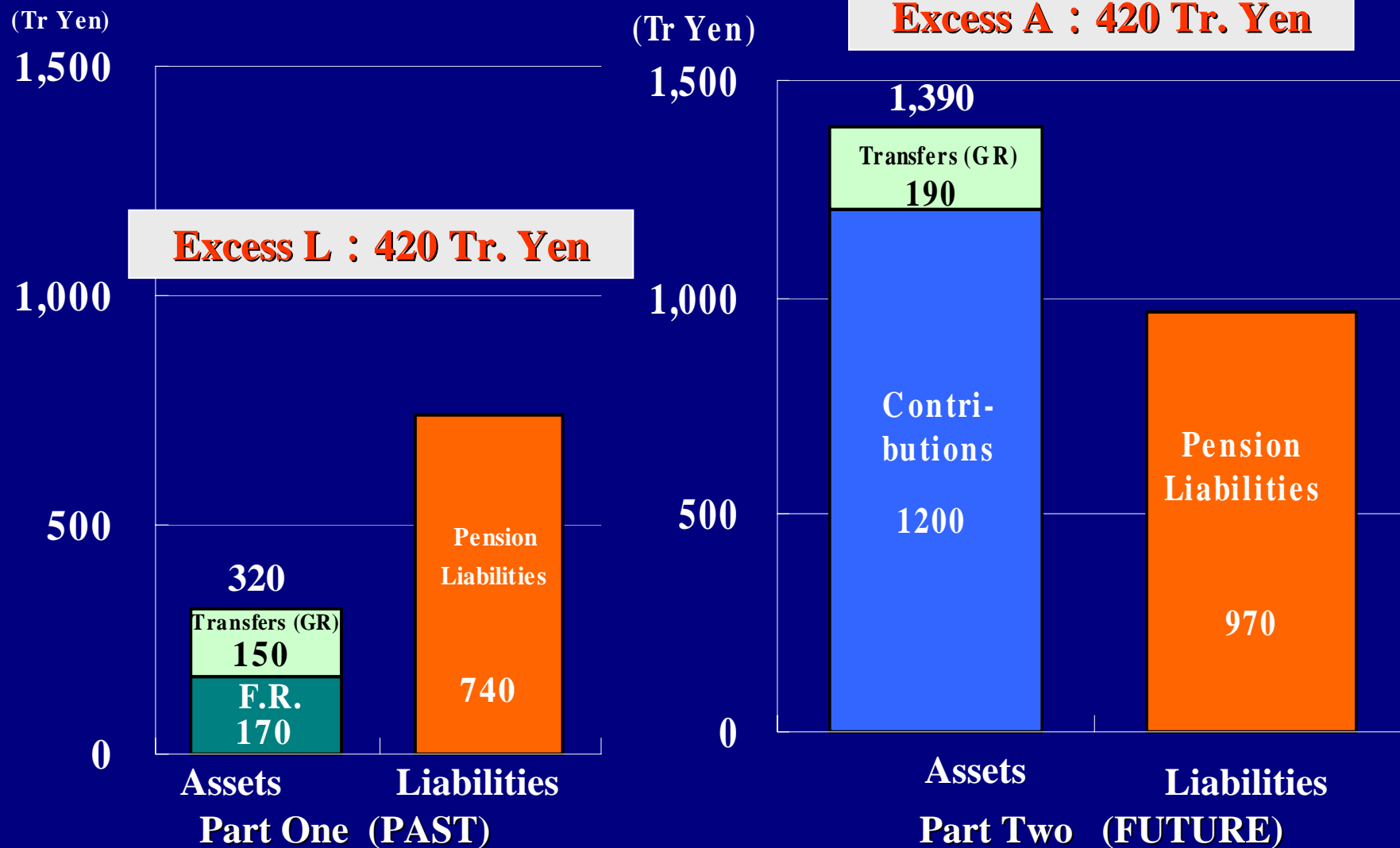
**Shift to Income-related Contributions**

**Strengthening Private Initiatives**

# KNH Balance Sheet: After Reform

## Incentive-compatible?

(as at 31st March 2005)



# Sensitivity

**The Discount Rate**

**The Accounting Period**

**Others**



# Is the Balance Sheet Healthy?

(units: trillion yen)

period	discount rate 2.1%				discount rate 3.2%				discount rate 4.0%			
	2005 ~ 2040	2005 ~ 2080	2005 ~ 2100	2005 ~ infinity	2005 ~ 2040	2005 ~ 2080	2005 ~ 2100	2005 ~ infinity	2005 ~ 2040	2005 ~ 2080	2005 ~ 2100	2005 ~ infinity
<b>(Assets)</b>												
<b>Past</b>												
FR	170	170	170	170	170	170	170	170	170	170	170	170
TGR	150	190	190	190	130	150	150	150	120	130	130	130
<b>sub-total</b>	320	360	360	360	300	320	320	320	290	300	300	300
<b>Future</b>												
Contri.	840	1,510	1,750	2,370	720	1,100	1,200	1,350	620	870	920	970
TGR	60	250	330	520	50	150	190	230	40	110	120	140
<b>sub-total</b>	900	1,760	2,080	2,890	770	1,250	1,390	1,580	660	980	1,040	1,110
<b>Total</b>	1,220	2,120	2,440	3,250	1,070	1,570	1,710	1,900	950	1,280	1,340	1,410
<b>(Liabilities)</b>												
<b>Past</b>												
FR	750	870	870	870	660	740	740	740	590	640	640	640
TGR	370	1,280	1,650	2,530	290	820	970	1,180	240	580	650	730
<b>sub-total</b>	1,120	2,150	2,520	3,410	950	1,560	1,710	1,920	830	1,210	1,290	1,370
<b>(EL)</b>												
<b>Past</b>												
FR	430	510	510	510	360	420	420	420	300	340	340	340
TGR	-530	-480	-430	-360	-480	-430	-420	-400	-420	-400	-390	-380
<b>sub-total</b>	-100	30	80	150	-120	-10	0	20	-120	-60	-50	-40

Notes: FR= Funded Reserve, TGR=Transfers from General Revenue, EL= Excess Liabilities

# Benefit/Contribution Ratio

	discount rate (%)		
	2.1	3.2	4.0
<b>1. year: 2005 ~ 2100</b>			
Benefits , tri. yen	1,650	970	650
Contributions , tri. yen	1,750	1,200	920
/ , %	94.3	80.9	70.7
<b>2. year: 2005 ~ infinity</b>			
Benefits , tri. yen	2,530	1,180	730
Contributions , tri. yen	2,370	1,350	970
/ , %	106.8	87.5	75.3

# Future Policy Options

## Strengthening Incentive-Compatibility

Shift to NDC

## Handling Legacy Pensions

Diminishing Excess Liabilities

# Strengthening Incentive-Compatibility

## Shift to NDC

**Direct Link between Contributions  
and Pension Benefits**

**“Every Yen Counts”**

**Increased Credibility**

# Handling Legacy Pensions

## Three Options

**Reducing Benefits**

**Increasing Contributions**

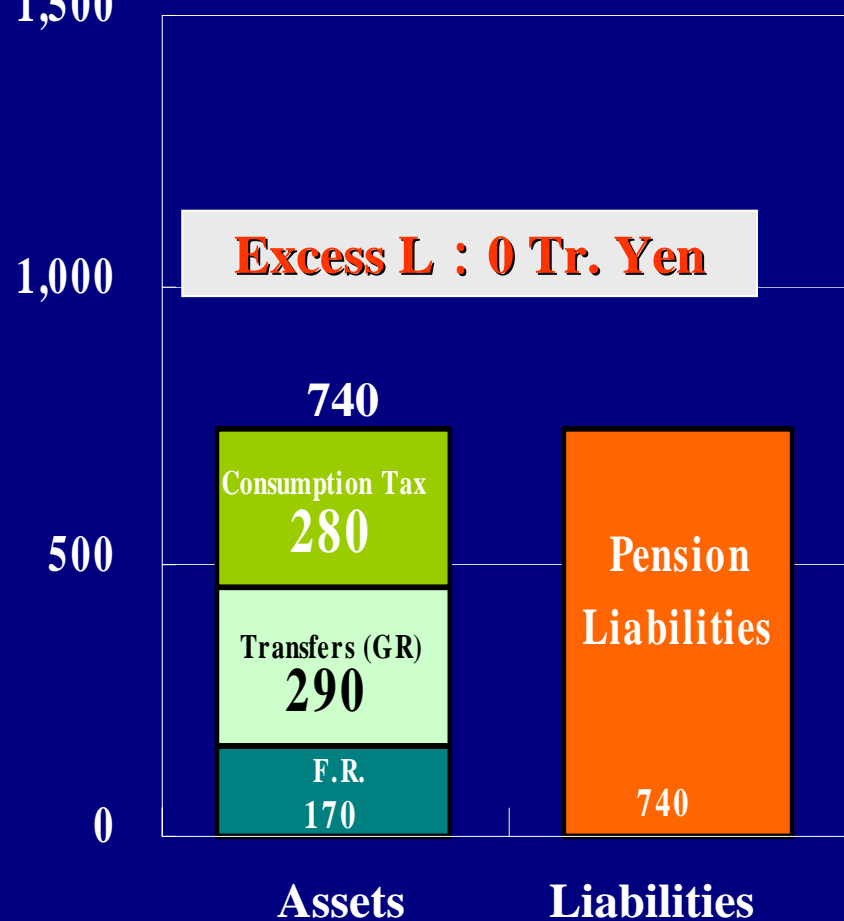
**Increasing Subsidies**

# KNH Balance Sheet :

## Alternative Reform

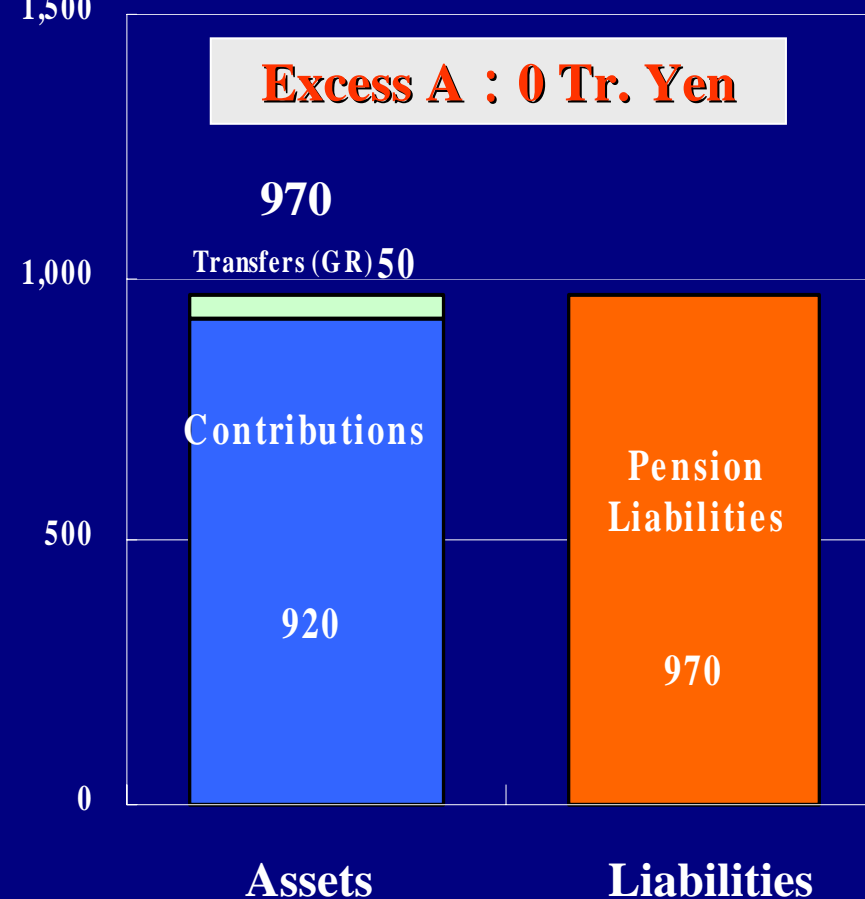
(as at 31st March 2005 )

(Tr Yen)  
1,500



Part One (PAST)

(Tr Yen)  
1,500



Part Two (FUTURE)

# Conclusions: BS of SS Pensions (1)

**describe the current financial situations**

**imply how smoothly SS benefits are  
financed in the future**

**assess impacts of alternative policy  
measures on future financing**

# Conclusions: BS of SS Pensions (2)

## Lacking is Common Methodology

What kind of assets and liabilities are to be taken into account?

The accounting period

The discount rate

Other demographic/economic assumptions

How much excess liabilities are acceptable?