

A Balance Sheet Approach to Reforming Social Security Pensions in Japan

by

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Organization

Brief Outline of Current Provisions

Demography

Basic Facts:

Identifying Main JPN Problems

Future Policy Options

The 2004 Reform Bill

Concluding Remarks

Brief Outline of Current Provisions

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 (230,000 yen = USD 2,200)

CPI Indexation

The NRA: 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 415 billion in 2003
(9% of Japanese GDP)

cf. The Automobile Industry

40 tr. Yen (Domestic Output in 2000)

Rapidly Growing

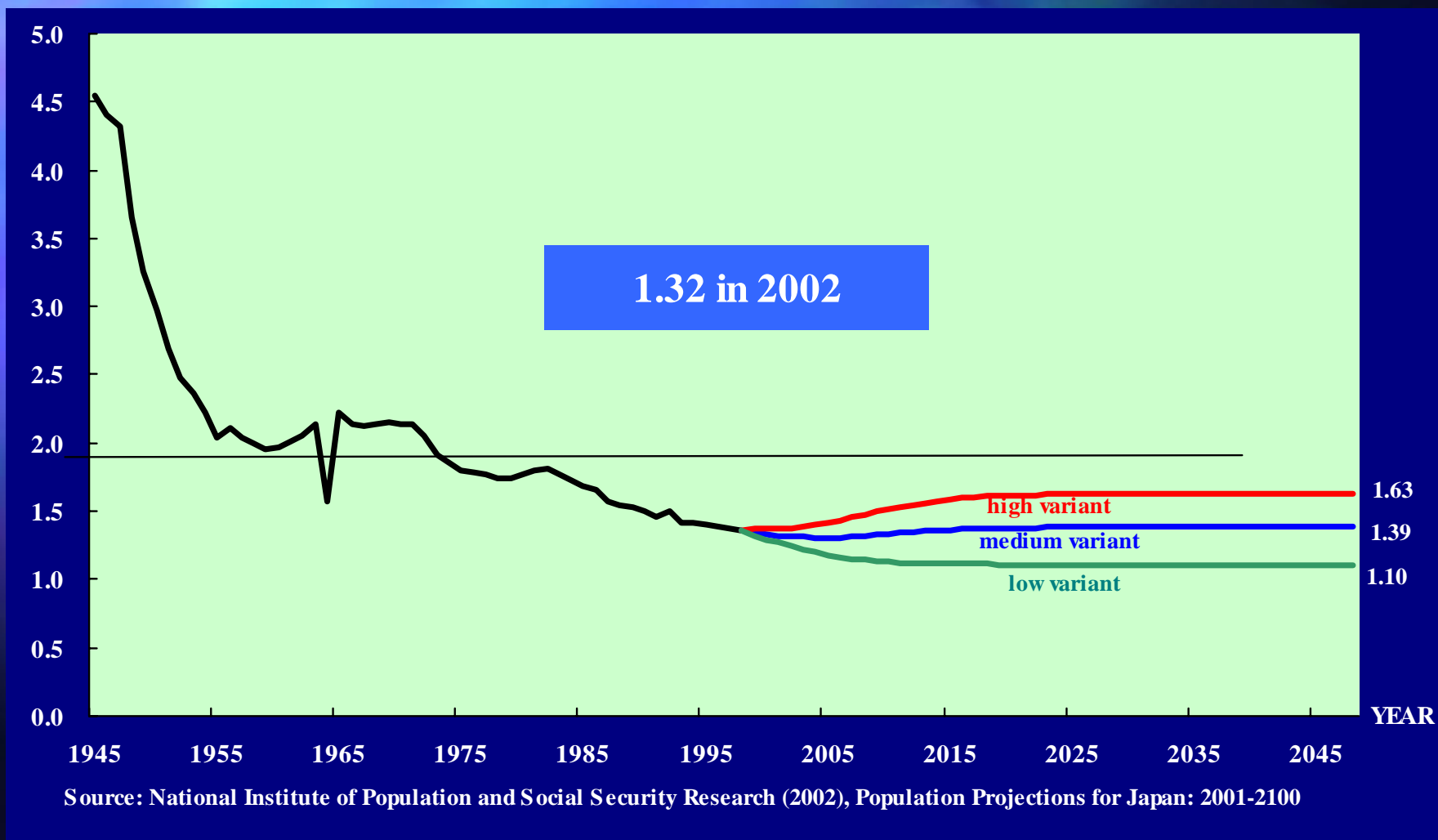
Demography

TFR

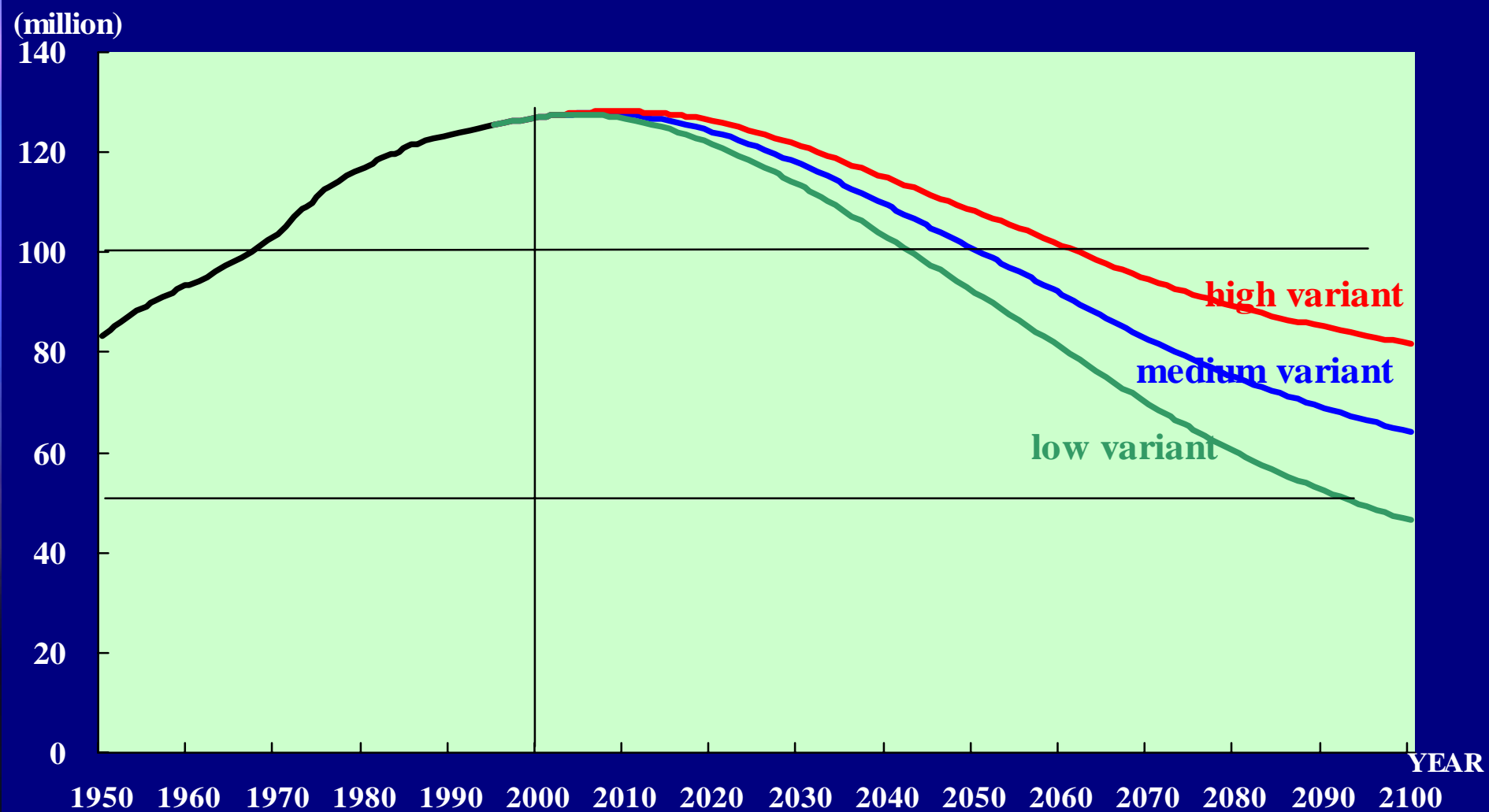
Total No. of Populations

Proportion of 65+

Trends in the Total Fertility Rate of Japan

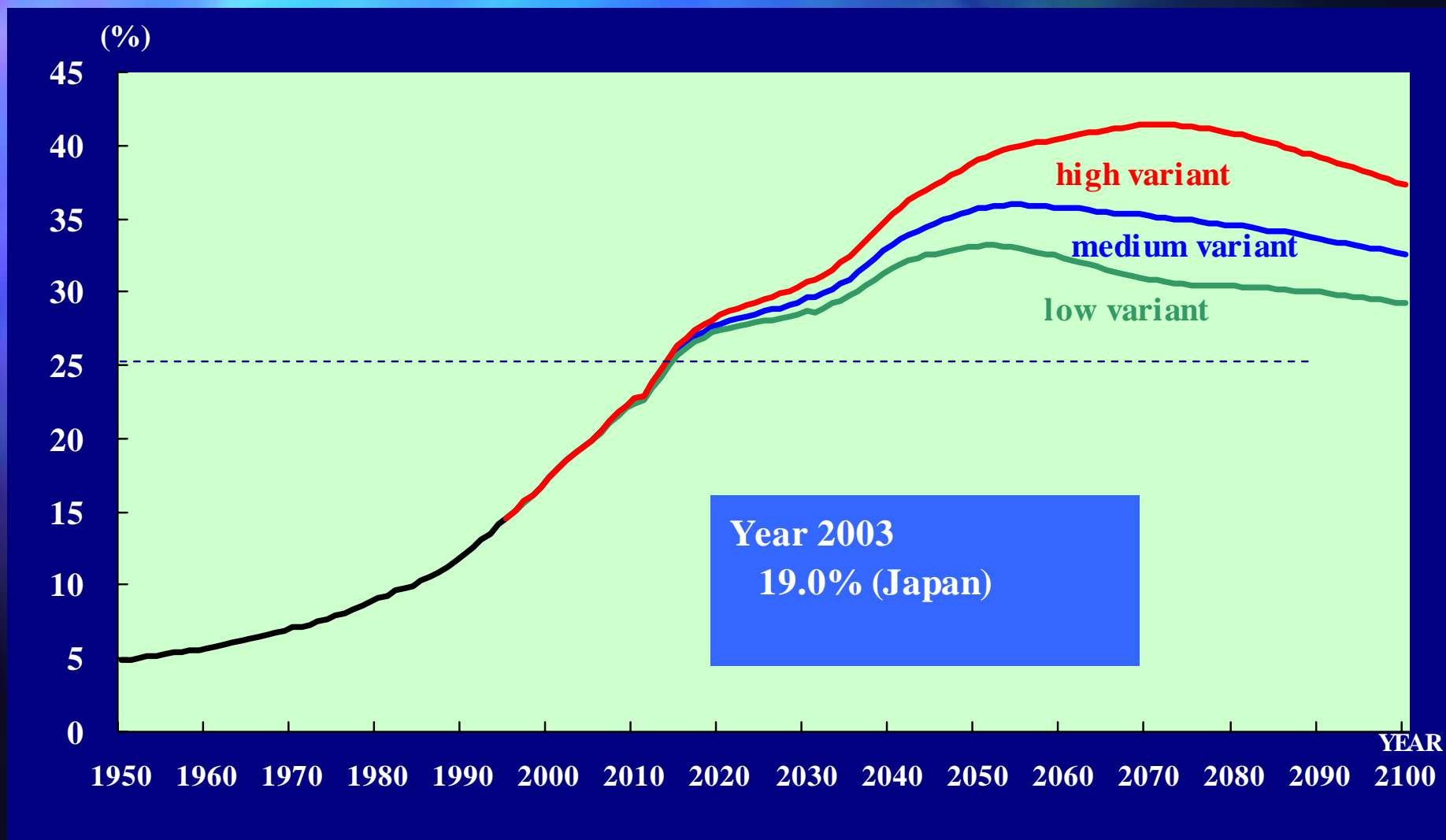


Actual and Projected Population of Japan



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:

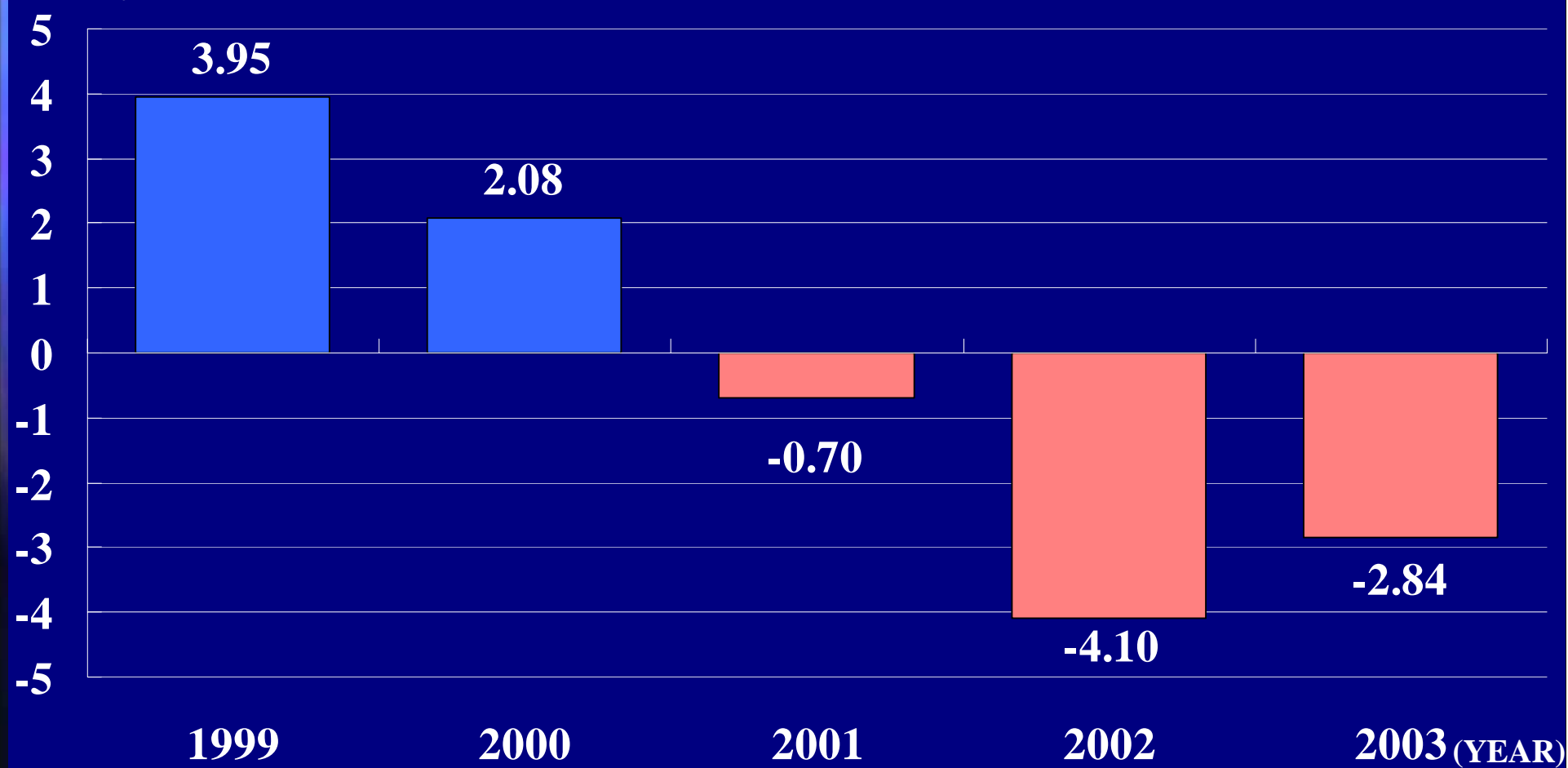
Heavy Burdens Outstanding

**Too Much Income Transfers between
Generations**

Increasing Drop-out

Current Account of the KNH

(trillion yen)



Balance Sheet of the KNH

(as at the 31st MAR 2000)

(trillion yen)

2,500

Excess Liabilities: 530 tr. yen

2,000

1,500

170 F. Reserve

280 Transfers (GR)

1,000

Contributions

500

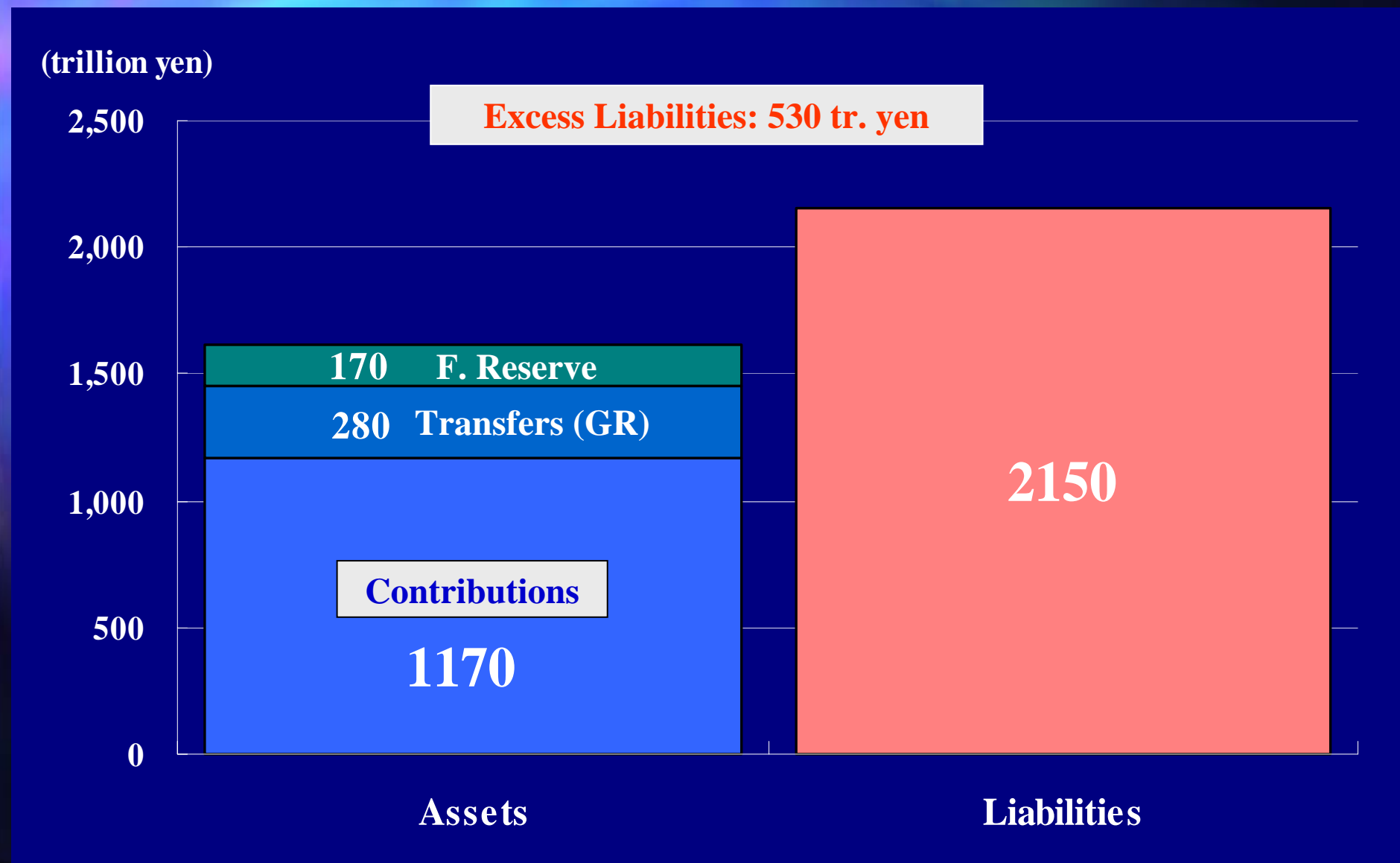
1170

2150

0

Assets

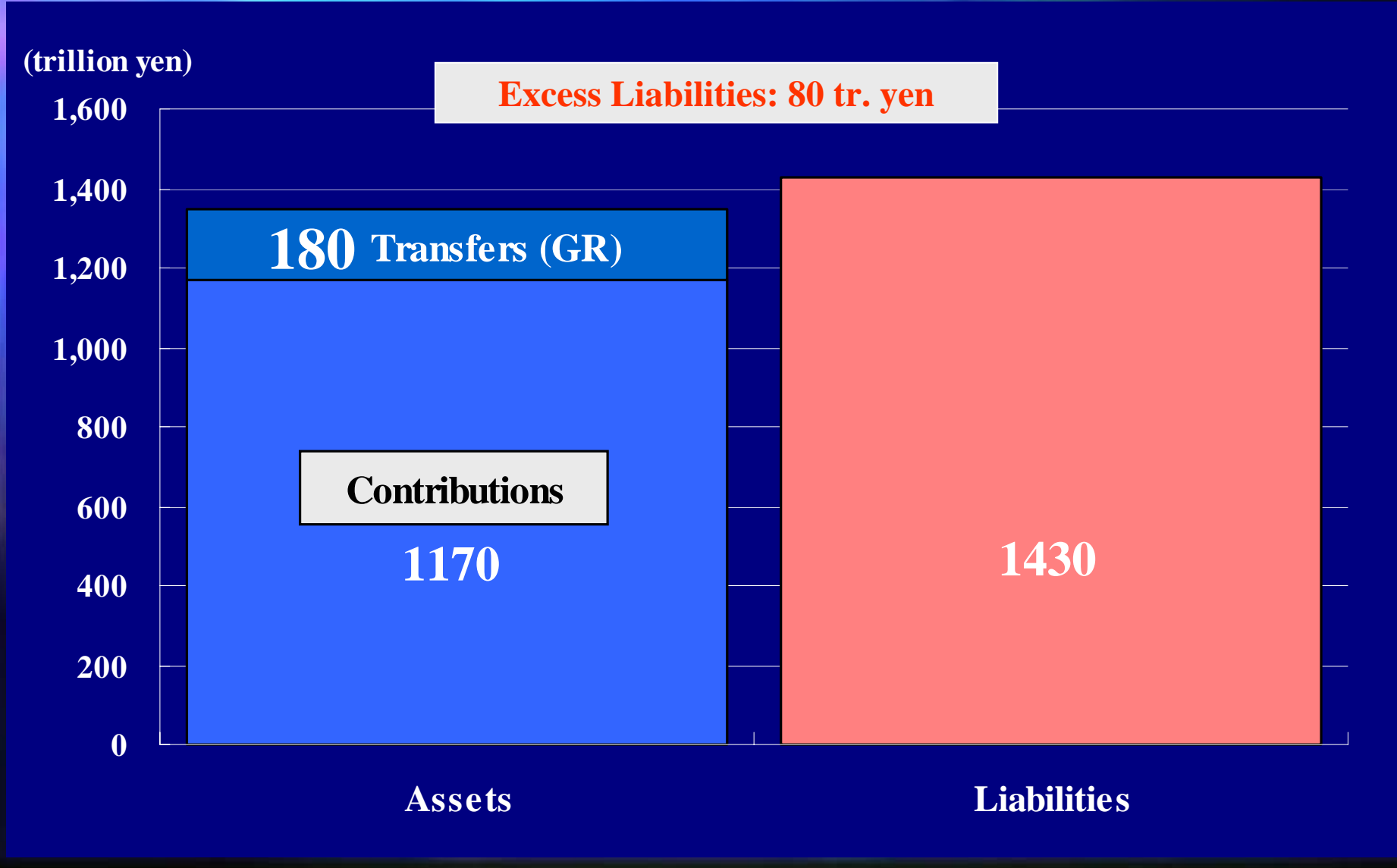
Liabilities



Balance Sheet of the KNH (Part 1)

(as at the 31st MAR 2000)

Pension Liabilities Accrued from **FUTURE** Contributions



Balance Sheet of the KNH (Part 2)

(as at the 31st MAR 2000)

Pension Liabilities Accrued from **PAST** Contributions

(trillion yen)

800

700

600

500

400

300

200

100

0

Excess Liabilities: 450 tr. yen

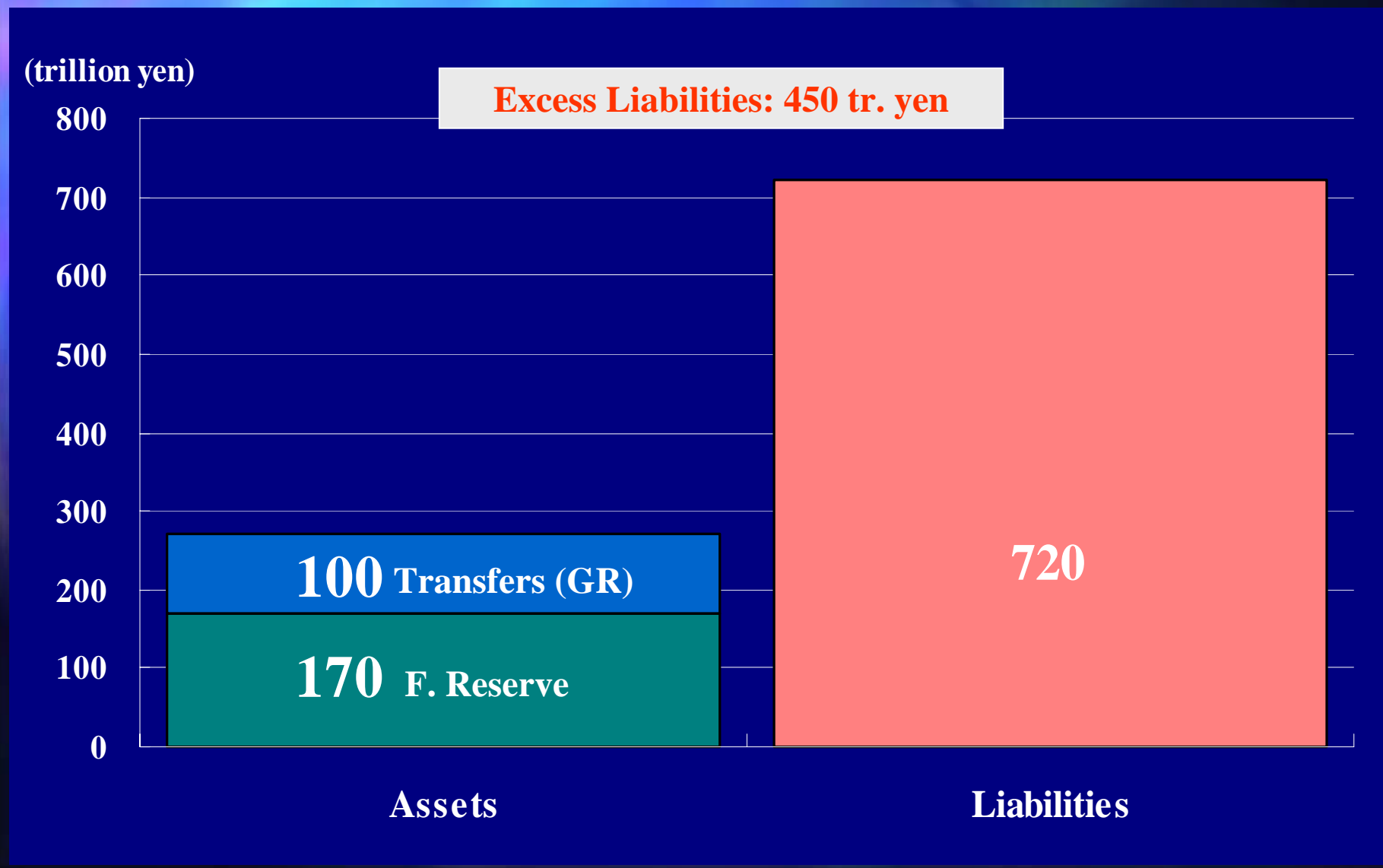
100 Transfers (GR)

170 F. Reserve

720

Assets

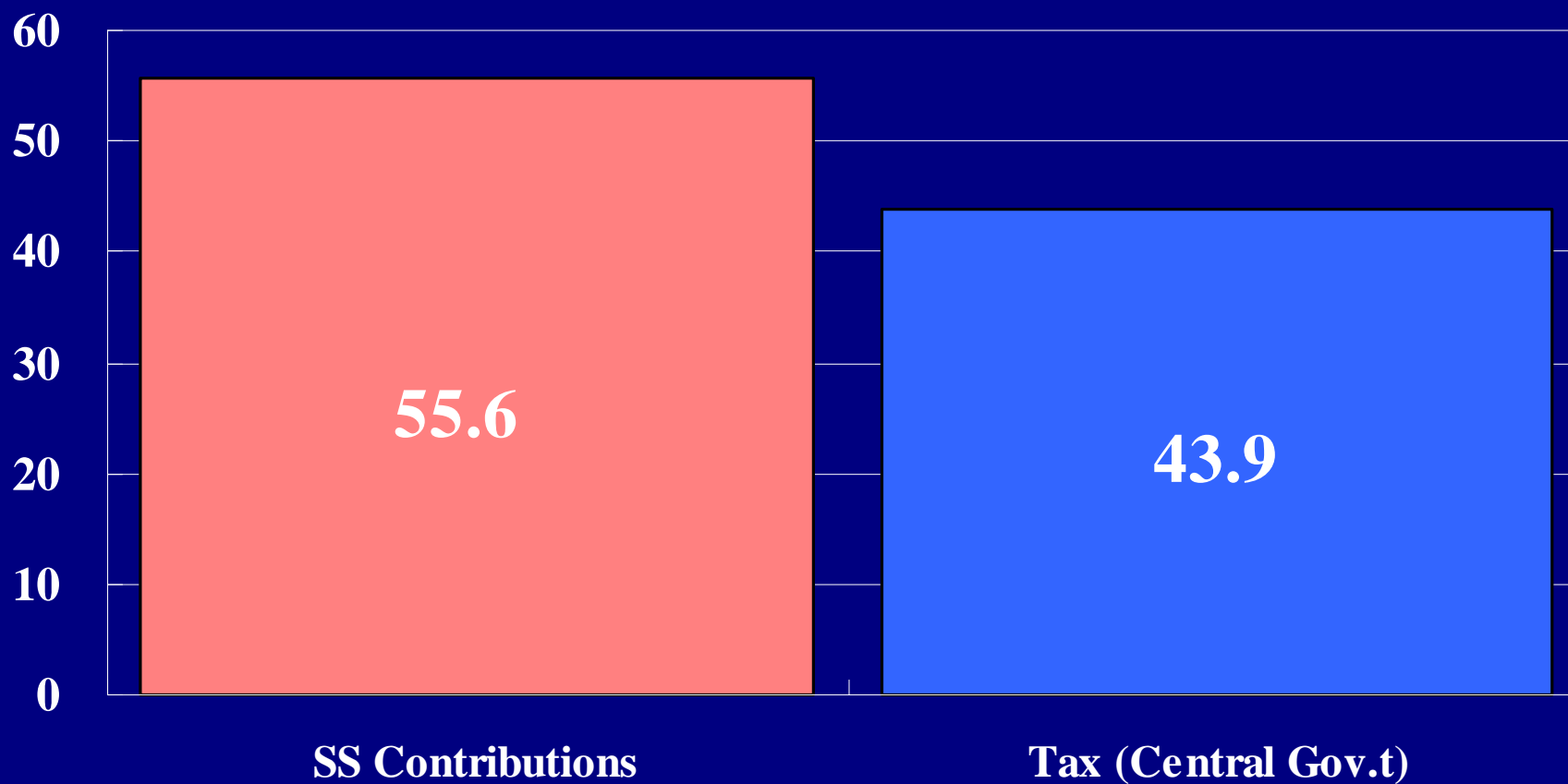
Liabilities



Which Is More, SS Contributions or Tax Revenues?

FY 2003 National Budget, Japan

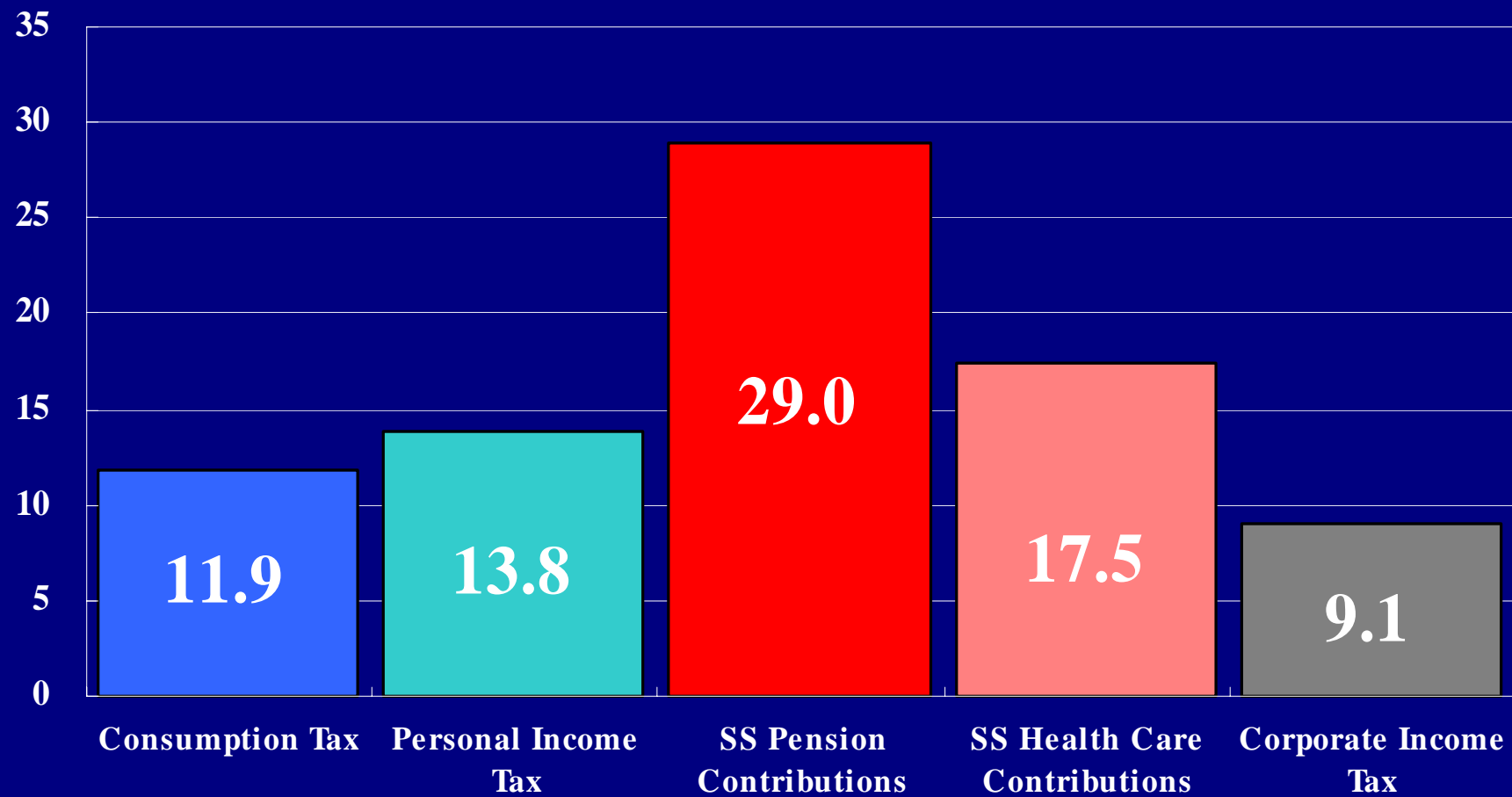
(trillion yen)



Main Income Sources of Japan's Central Government

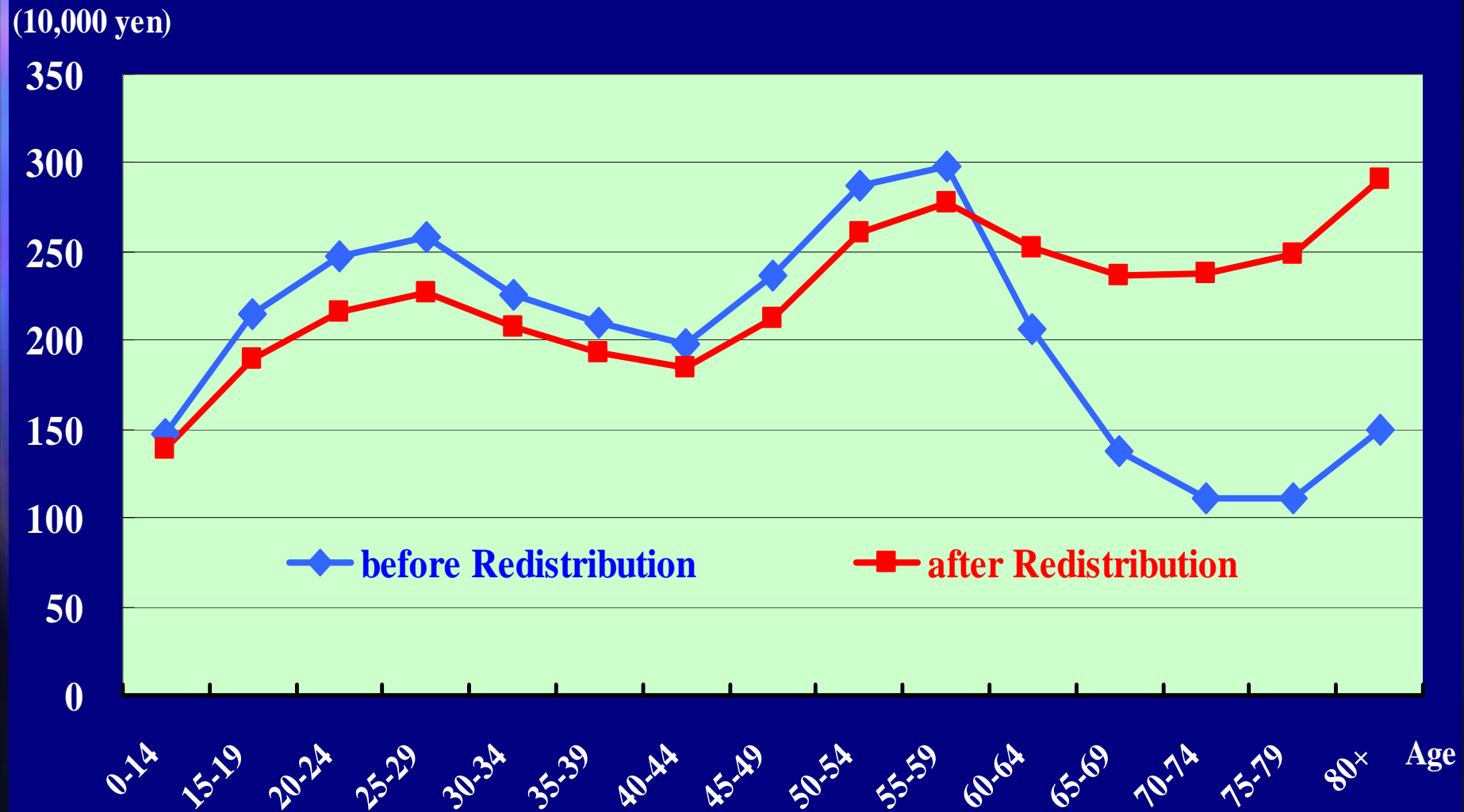
FY 2003 National Budget, Japan

(trillion yen)



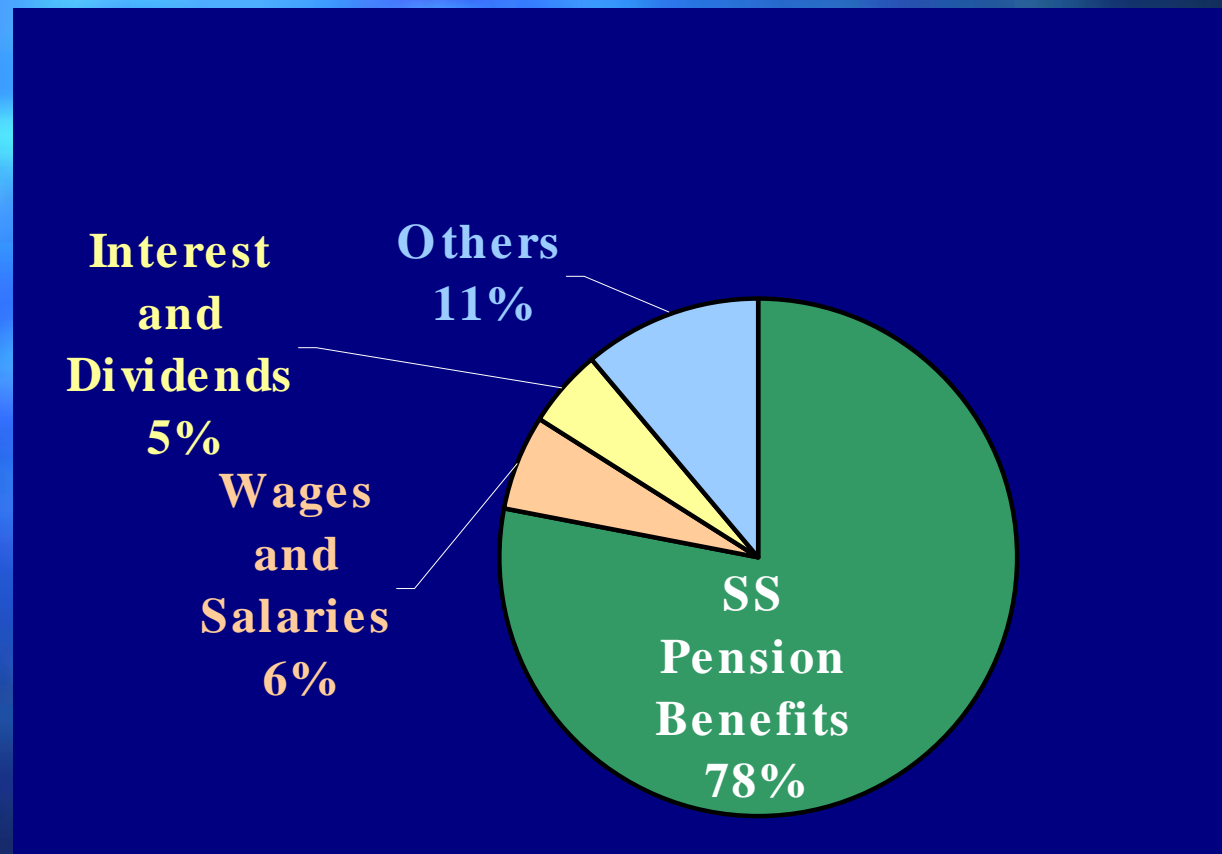
Per-capita Income by Age in Japan

18



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

SS pension benefits are the major source of retirement income

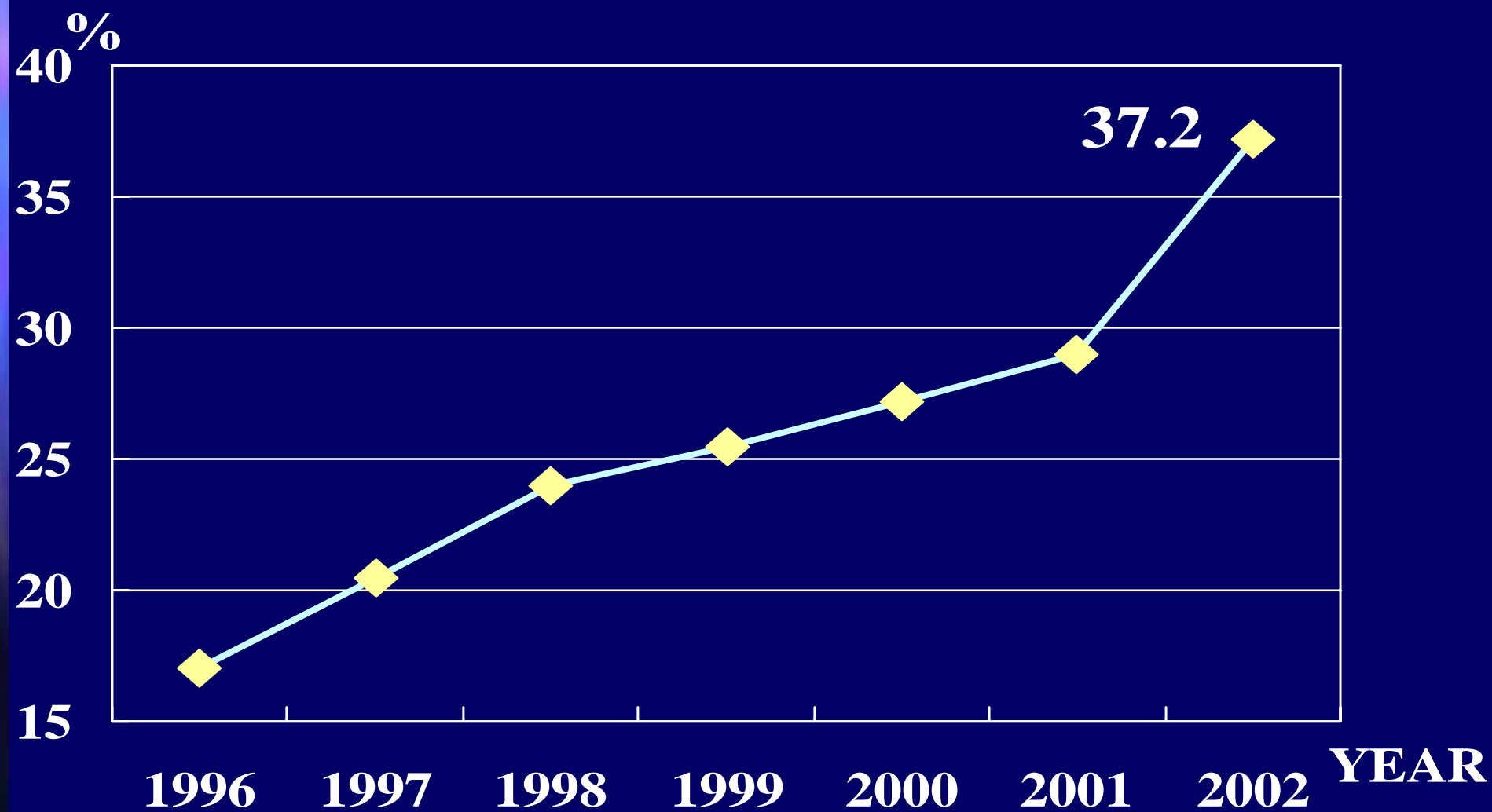


median income: 3.38 million yen

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

Drop-out from SS Pensions (Non-employees)

Delinquency in Paying Pension Contributions



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

Option 1: Reducing Benefits

Deflation-Indexing

A Clawback System

**Benefits Indexation Reflecting
Macroeconomic Conditions**

Increasing the NRA to 67

Deducting Contributions for Health Care

More Taxes on Benefits

Option 2: Increasing Contributions

Incentive-compatible?

What Matters is **Taste of Pie**

Penalties on Employment

Non-neutral & Regressive

Income Tax Revenues

Option 3: Increasing Subsidies

Where to Go:

Flat-rate Basic Benefits ($1/3$ $1/2$) or
Guaranteed Pensions or
Legacy Pensions?

What Funding Source:

Consumption Tax or Income Tax or
Cutting Other Public Expenditure?

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)

Changes in Balance Sheet of KNH after the 2004 Reform²⁸ Bill

(as at 31st MAR 2000)

(Tr Yen)
2,000

Excess L : 390 Tr. Yen

1,500

1,000

500

0

Transfers (GR)

120

F. R.

170

Assets

(PAST)

Pension
Lia-
bilities

680

Liabilities

(Tr Yen)
2,000

1,500

1,000

500

0

Excess A : 480 Tr. Yen

Transfers

270

Contri-
butions

1500

Assets

(FUTURE)

Pension
Lia-
bilities

1290

Liabilities

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:

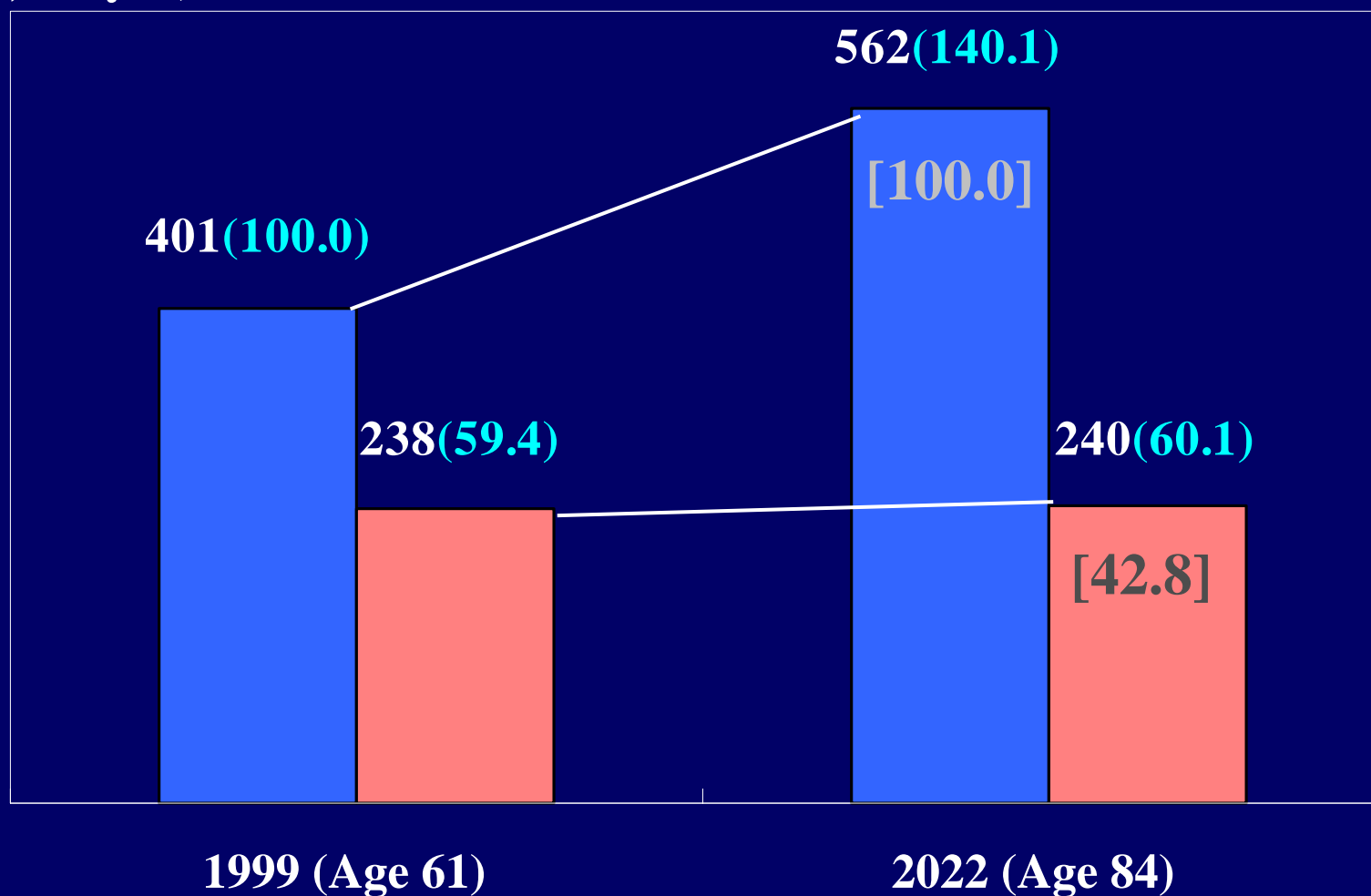
60% (2004) 50% (2023)

Current Pensioners:

60% (Age 65) 43% (Age 84)

Benefits for Current Pensioners

(1,000 yen) ■ Take-home Pay ■ Pension Benefits



The 2004 Reform Bill (3)

Relaxing the Earnings-test

Earnings-split between Husband & Wife

Non-Employees:

Shift to Income-related Contributions

Strengthening Private Initiatives

Concluding Remarks

Balance Sheet : So Informative Tools

Greater Significance on Incentives and Compliance

Burden-Sharing: How It Will Be

Separating Legacy Pensions from Newly Qualified Pensions **Recommended**

Minimize Adverse Effects on the JPN Economy

Automatic Stabilizers Still Lacking