TOWARDS SUSTAINABLE PENSION PLANS

Brief assessment of the Dutch pension system
mainly CDC plans

- Strengths
  - Adequacy (with much heterogeneity)
  - Risk sharing (within and between generations)
  - Low execution costs (admin, investments)
- Weaknesses
  - Nominal DB/CDC is not inflation proof
  - Intransparancy due to redistribution mechanisms
  - Not fit for current labour market patterns (e.g. self employed)
  - Limited freedom of choice; one size fits all approach

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TOWARDS SUSTAINABLE PENSION PLANS

Trends that are likely to erode the surrent system:

- Demographic transition
  - Double greying, de-greening
- Declining returns on financial markets
  - Reversion to the mean? Which mean?
- Labour market changes
  - Transitional careers, temporary contracts, self-employed
- Societal changes
  - Individualisation, solidarity, freedom of choice, time horizon

Several reports (1994-) + societal debate (2014)

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TOWARDS SUSTAINABLE PENSION PLANS

Design of prototype pension plan by SER
(SER: Social and Economic Council of the Netherlands)

- Accumulation: personal pension pots
  - Life cycling
- Decumulation: collective pension pot
  - Continued investment

- Sharing of investment risks
- Sharing of micro longevity risk
- Sharing of macro longevity risk
- Buffer mechanism strictly defined

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TOWARDS SUSTAINABLE PENSION PLANS

Buffer rules

- Buffer >0
- Returns above px of expected returns: buffer in (e.g. x=95)
  - Fixed income excluded (e.g. low interest, high returns, no buffer feeding)
- Returns below py of expected returns: buffer out (e.g. y=5)
- Buffer is not owned by members → not transferred
- Buffer <M% of ∑ individual pots (e.g. M=20)

This makes the contract more complete than CDC, e.g. pensions are cut if buffer is depleted (no decision required)

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TOWARDS SUSTAINABLE PENSION PLANS

Why is this prototype plan more sustainable?

- Fair: less intergenerational solidarity
  - Life cycle investing
- Realistic: financial returns determine result
  - But volatility dampened by buffer
- Flexible: individual bookkeeping
  - Personal pots allow for labour market mobility
- Modern: accomodating societal trends
  - More clarity about “the deal”
- Transparent: clear rules
  - Easier to communicate and explain
  - Enhances trust in the pension system

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TOWARDS SUSTAINABLE PENSION PLANS

Transition

- Complicated, e.g. uniform contribution and accrual system
  - Compensation of middle cohorts → financing issue
- Double transition: the above + conversion to personal pots
  - Makes financing easier, but more uncertainty during buffer accumulation
- Legal issues, e.g. mandatory industry wide pension plans
- Impact differs across pension funds
- Big bang practically impossible → transition phase required

Still, these issues don't seem prohibitive.

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TOWARDS SUSTAINABLE PENSION PLANS

So where are we now?

- Social partners
  - Plenty of support by SER, Pension Federation, CPB, etc.
  - Could not reach agreement… up till now
- Cabinet formation
  - Limited consensus among political parties
  - New government is going to do something…
- And the trends, they continue
  - Struggle for survival
  - European developments (e.g. PEPP)

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TOWARDS SUSTAINABLE PENSION INVESTMENTS

Awareness and commitment increase

- Sustainable investment
  - Sustainable Pensions Investment Lab (www.spilplatform.com)
  - Several ESG policies by larger pension funds (e.g. ABP, PFZW)
    - Investment in sustainable housing (SARE&F)
  - Active support by the central bank (DNB)
  - In progress: covenant on international sustainable business (IMVO) www.internationalrbc.org
- Long Term Investment
  - Newsroom: Shift to Long Term Investing (www.shiftto.org)
  - Focussing Capital on the Long Term (www.fcltglobal.org)

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WILL 'THE TWAIN' EVER MEET?

Combination very well feasible

- Increased demand for sustainable investment
  - E.g. tobacco, child labour, food industry
- SER prototype is meant to gain societal acceptance
  - Lifecycle investment allows for different asset mixes

However:

- SER prototype is not invidual plan, like e.g. NEST
- Collective investment makes voice mechanism relevant
- Outcome will differ across pension funds

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Questions & discussion
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