

Social Security Reform around the World

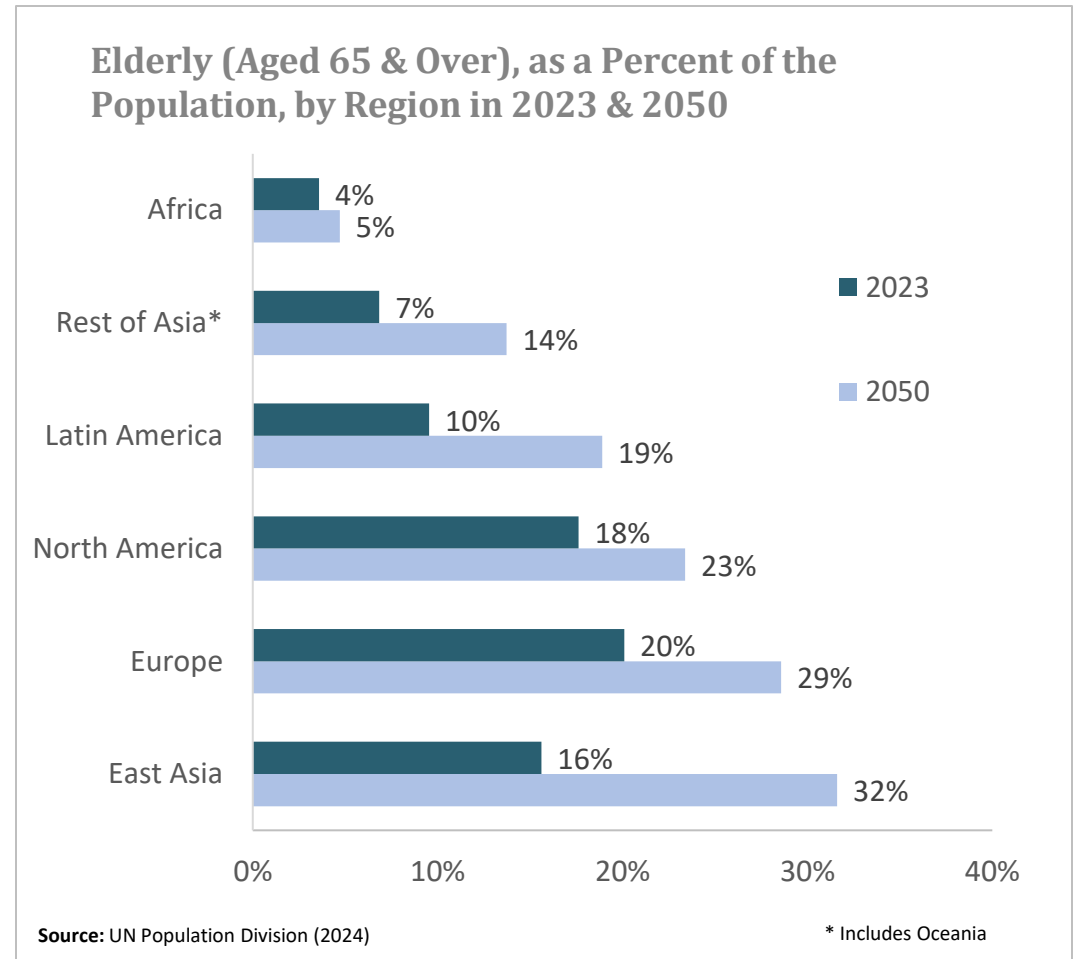
Balancing Adequacy and Sustainability in Aging Societies

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Social Security Subcommittee
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A Stunning Demographic Transformation

- Falling fertility and rising life expectancy are leading to a dramatic aging of populations worldwide.
- The aging trend began in the rich world, but it has now overtaken much of the emerging world as well.
- Population aging is challenging the ability of governments everywhere to ensure the adequacy and sustainability of their retirement systems. The nature of the challenge, however, differs greatly in developed countries and emerging markets.



Two Very Different Retirement Challenges

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DEVELOPED COUNTRIES

How to maintain a high standard of living for the old without imposing a crushing burden on the young

EMERGING MARKETS

How to provide a modicum of income security for the old when most now have none at all

Developed Country Overview

- In the early postwar decades, most developed countries greatly expanded the generosity of government retirement systems, boosting elderly living standards and triggering a mass exodus of older workers from the labor force.
- Although the design of these systems differed significantly from country to country, most were financed on a mainly PAYGO basis.
- Favorable demographics, combined with rapid economic growth, made generous government retirement benefits seem easily affordable.
- Given the high poverty rates, comparatively low educational attainment, and modest life expectancy of the elderly, heavily subsidizing retirement also seemed like enlightened social policy.

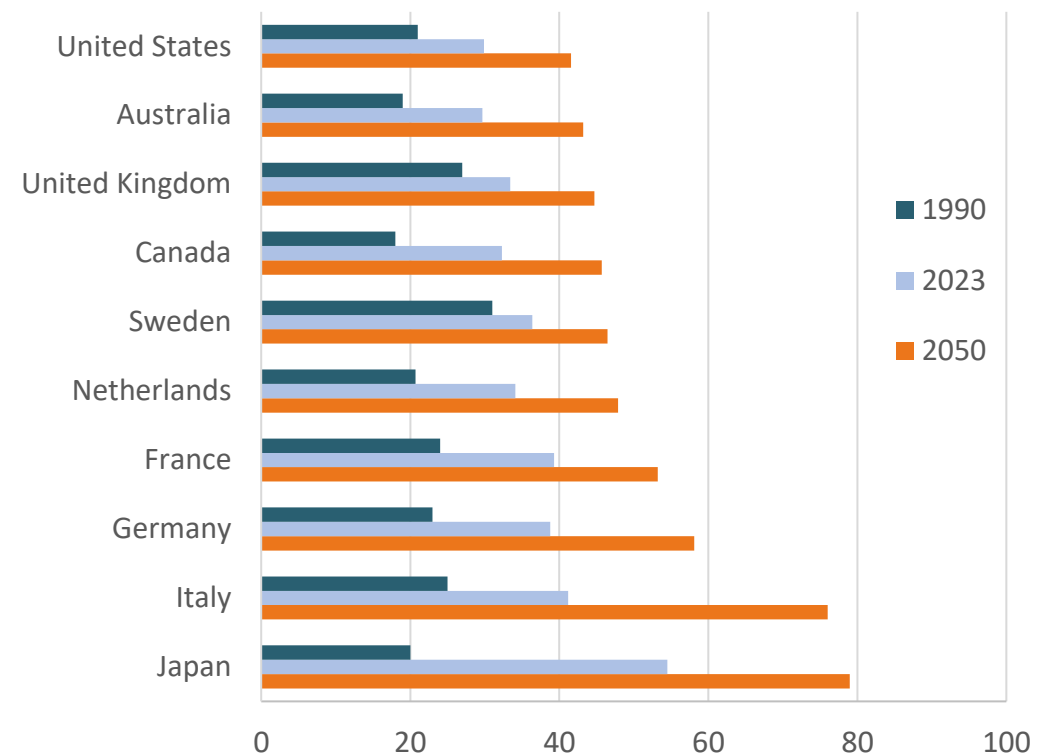
“The beauty about social insurance is that it is *actuarially* unsound...Always there are more youths than old folks in a growing population. More important, with real incomes growing at 3 percent per year, the taxable base upon which benefits rest in any period is much greater than the taxes paid historically by the generation now retired... A growing nation is the greatest Ponzi game ever contrived.”

-- Paul A. Samuelson, *Newsweek* (February 13, 1967)

The End of Samuelson's Chain Letter

- By the 1970s and 1980s, falling birthrates and slowing economic growth began to throw into question the sustainability of government retirement systems.
- At the same time, the rising income, educational attainment, and life expectancy of the elderly rendered the social justification for heavily subsidizing retirement less compelling.
- By the 1990s, most developed countries had shifted their focus from expanding the generosity of government retirement systems to enacting reforms aimed at controlling their mounting cost.

Aged Dependency Ratio (Elderly Aged 65 & Over per 100 Adults Aged 20-64), by Country in 1990, 2023 & 2050



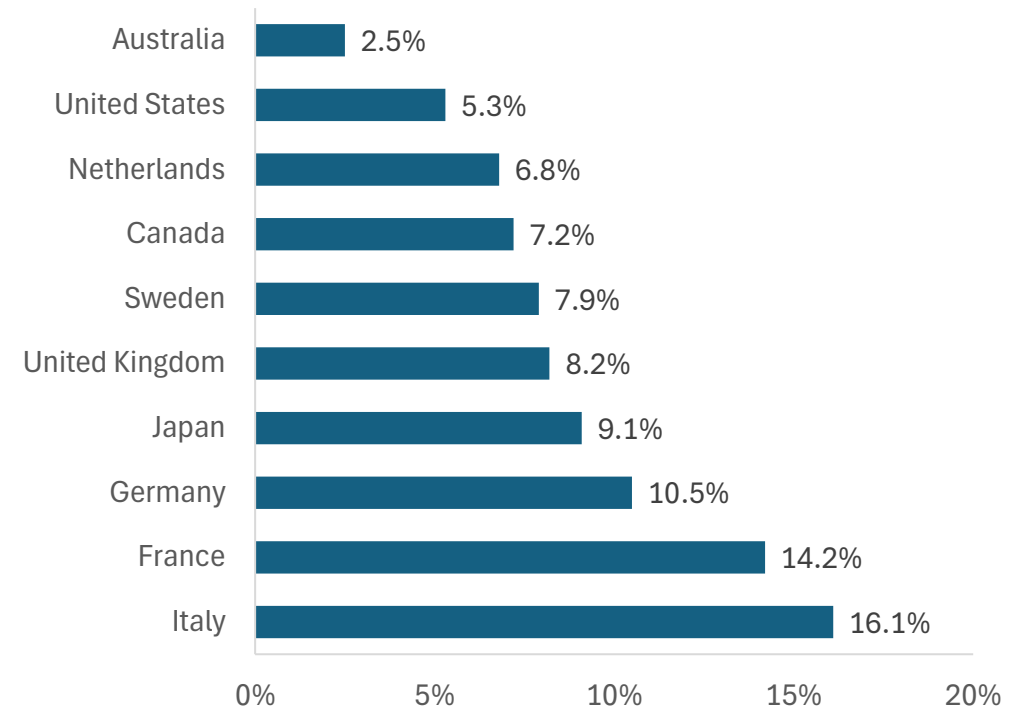
Source: UN Population Division (2024)

Types of Social Security Systems

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- **Earnings-Related Government Systems.** Like the United States, most developed countries have a contributory, earnings-related government pension system financed mainly on a PAYGO basis. Exceptions: Australia, New Zealand, the Netherlands, and the UK.
- **Government Flat Benefits.** In addition to (or sometimes instead) of an earnings-related government pension system, many developed countries have a universal or means-tested flat benefit, usually paid for out of general revenues.
- **Mandatory Employer Systems.** A few developed countries have mandatory or quasi-mandatory employer pension systems that substitute for government earnings-related systems. Examples: Australia, the Netherlands, and Switzerland.

Government Pension Spending,* as a Percent of GDP, in 2025



Source: *Pensions at a Glance 2025* (OECD, 2025)

*Central government spending on retirement, survivors, and disability pensions; data for some European countries include civil service pension programs.

Reducing Costs: Higher Retirement Ages

- Like the United States, most developed countries have raised or are in the process of raising their full-benefit retirement ages. Unlike the United States, many have also raised their early retirement ages.
- The shift toward higher retirement ages has been especially dramatic in Europe, where until recently some countries allowed early retirement in the late fifties or early sixties with no actuarial reduction in benefits.
- After bottoming out in the mid-1990s to early 2000s, labor-force participation rates at older ages have risen substantially in most developed countries. In many of them, so has the age of first pension receipt.

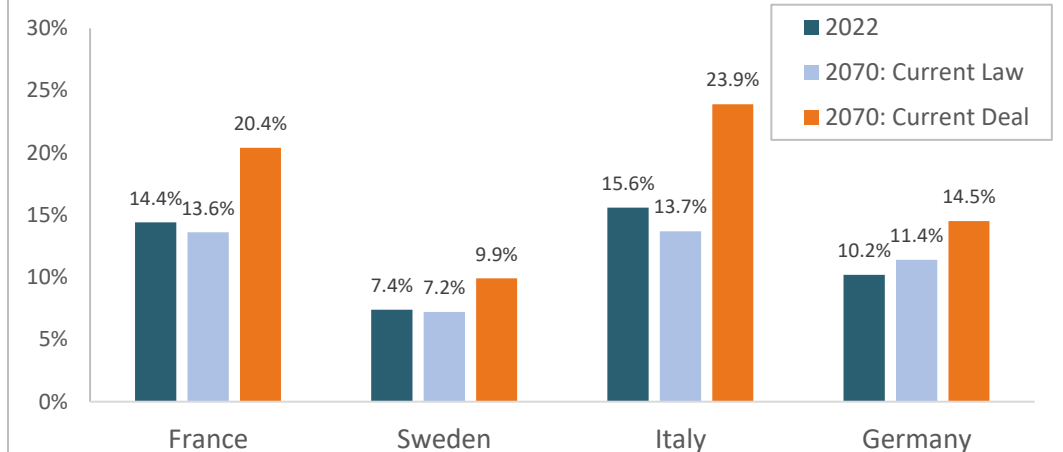
Labor-Force Participation Rate of Older Men, by Age and Country, in 1970, 1995 & 2024						
	Age 60-64			Age 65 & Over		
	1970*	1995	2024	1970*	1995	2024
Australia	77%	47%	68%	22%	9%	20%
Canada	67%	43%	65%	15%	10%	19%
France	53%	11%	46%	13%	3%	5%
Germany	72%	28%	73%	17%	4%	12%
Italy	48%	31%	59%	n.a.	6%	8%
Japan	81%	75%	87%	49%	37%	35%
Netherlands	74%	21%	79%	11%	5%	19%
Sweden	80%	57%	76%	29%	14%	27%
United Kingdom	n.a.	50%	64%	na	8%	15%
United States	75%	53%	64%	27%	17%	23%
Source: OECD Data Explorer (2025) *Netherlands = 1971, France = 1975, Canada =1976						

Reducing Costs: Benefit Cuts & Automatic Stabilizers

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- In addition to raising full-benefit retirement ages, many developed countries have reduced initial benefit formulas and/or the indexation of benefits in current payment status.
- Some have gone further and added automatic stabilizers to their government pension systems:
 - Ten countries in the EU have indexed their full-benefit retirement ages to life expectancy.
 - A few countries, including Italy and Sweden, are transitioning to NDC systems in which benefits are indexed to both life expectancy and the growth in taxable payroll.
 - Germany and Japan have added stabilizers to their traditional DB systems that have much the same effect.
- In some countries, reforms have entirely offset the impact of population aging on government pension costs.

Government Pension Spending, as a Percent of GDP, by Country in 2022 and EC Projections for 2070



Source: 2024 Ageing Report (EC, 2024)

* The “Current Deal” projection assumes no change in relative benefit levels, retirement ages, or labor-force participation rates.

Automatic Stabilizers in the Swedish System

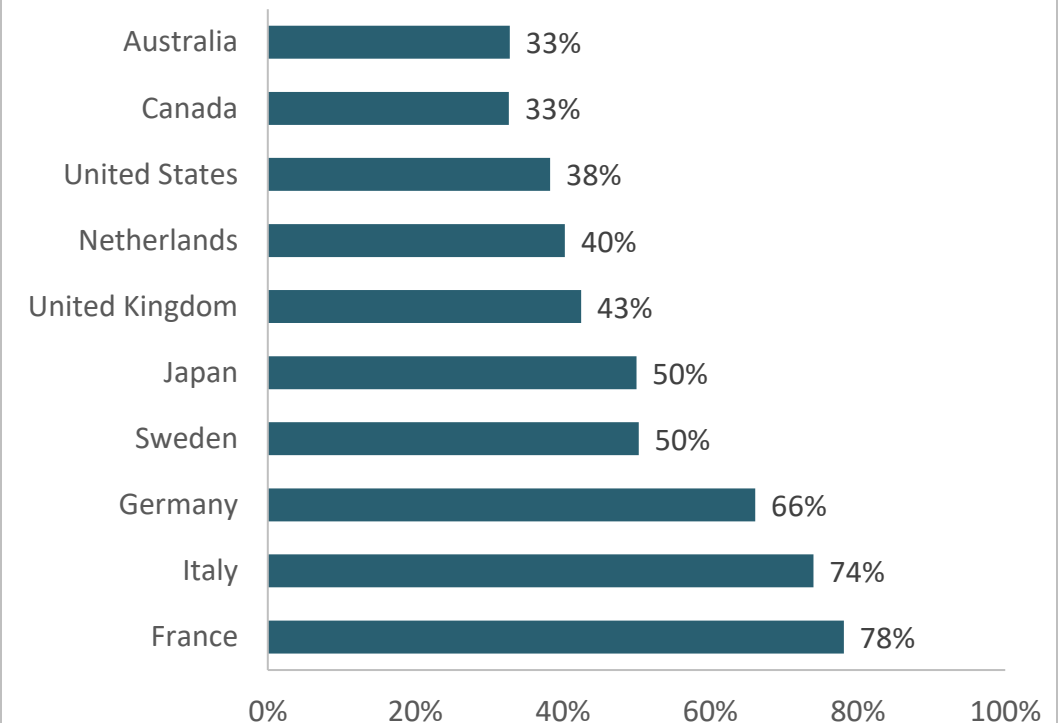
- The notional return on account balances equals average wage growth.
- Annuities are calculated based on cohort life expectancy at retirement.
- An “automatic balancing mechanism” adjusts indexation of annuities if the system drifts out of long-term actuarial balance.

The Imperative of Maintaining Adequacy

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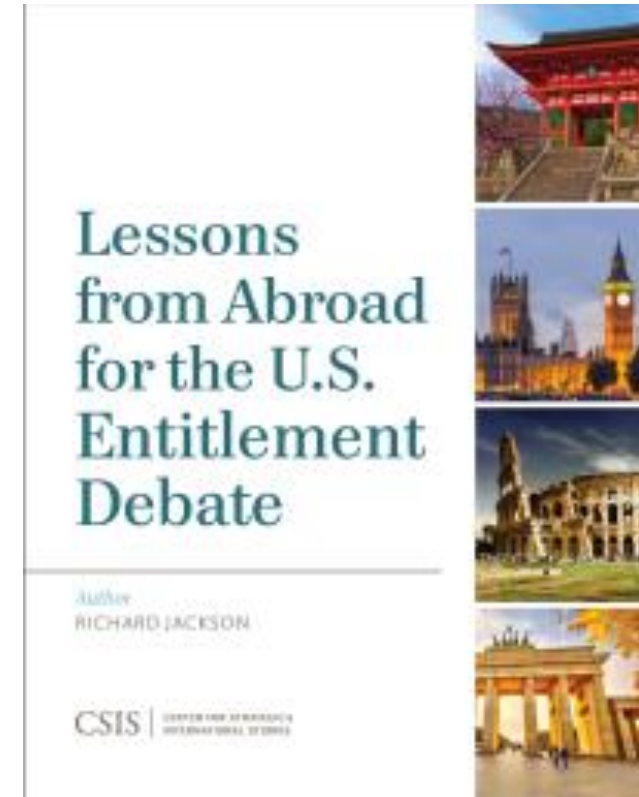
- Given the high level of elderly dependence on government benefits in many developed countries, scheduled pension reforms could result in deep reductions in the relative living standard of the elderly.
- To forestall this, some countries that have relied almost exclusively on PAYGO pension systems are jump-starting new supplemental funded systems (e.g., Germany and Italy), while others with well-established funded systems are expanding them (e.g., Australia, New Zealand, Sweden, and the UK).
- Ensuring a decent standard of living for the elderly is not just a matter of good social policy. In the end, reforms that achieve fiscal sustainability at the expense of income adequacy will face push back from aging electorates and are unlikely to prove lasting.

Government Benefits, as a Percent of the Income of the Elderly (Aged 65 & Over), in 2022 or Most Recent Available Year



Source: *Pensions at a Glance 2025* (OECD, 2025)

- Retirement reforms that focus on fiscal sustainability at the expense of income adequacy are likely to be reversed by aging electorates. (Example: The UK)
- There is no single right approach to retirement reform. Radically different models can succeed in ensuring both fiscal sustainability and income adequacy. (Example: Australia vs. Sweden)
- Government pension systems that are based on social contracts (like those in most European countries), may be easier to reform than systems (like U.S. Social Security) that are dressed up in the contractual language of “entitlements” and “earned rights.”

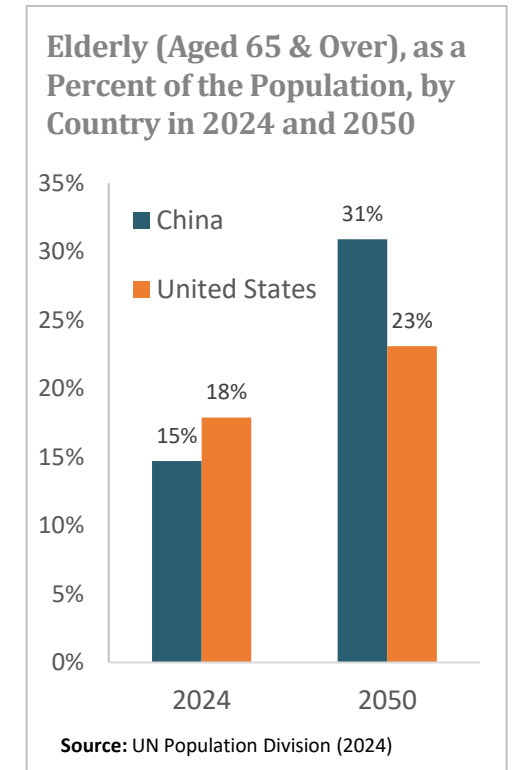
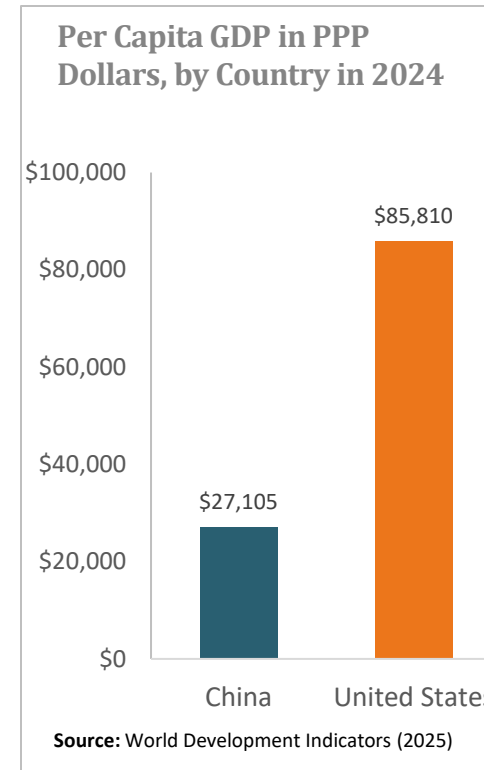


Emerging Market Overview

Growing Old before Growing Rich

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- While today's developed countries became affluent societies before they became aging societies, many emerging markets are growing old while they are still in the midst of development and before they have put in place the full protections of a modern welfare state.
- This premature aging vastly complicates the challenge of building adequate and sustainable retirement systems.

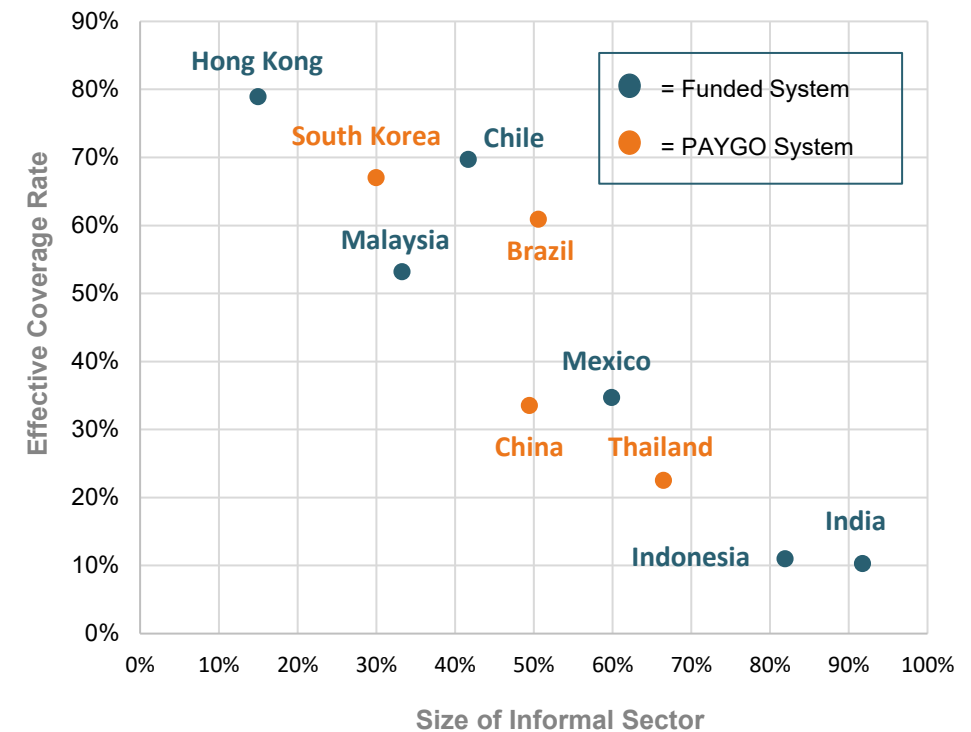


Large Gaps in Pension Coverage

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- The design of government pensions varies greatly across emerging markets, from traditional DB systems (e.g., Brazil and China) to personal accounts systems (e.g., Chile and Mexico) and government provident funds (e.g., India, Indonesia, and Malaysia).
- Yet all emerging markets face a common retirement security challenge. A significant share of workers, and in some countries the great majority of workers, fail to participate in the government retirement system.
- The higher the rate of labor-market informality, the lower the effective coverage rate, regardless of the design of the government retirement system.

Effective Coverage Rate of Mandatory Government Retirement System(s) vs. Size of the Informal Sector



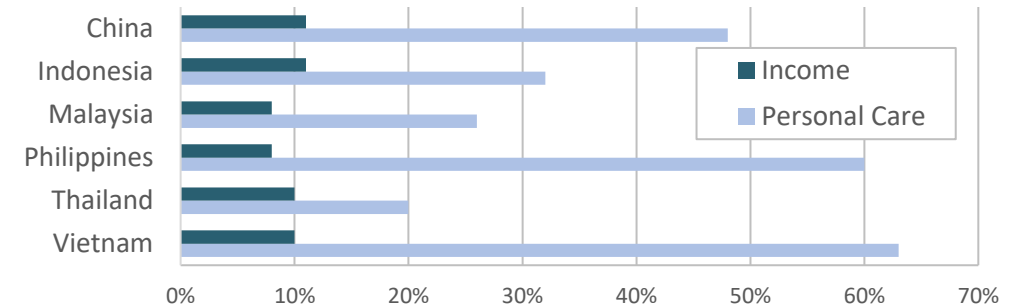
Source: Voluntary Pensions in Emerging Markets (GAI, 2017)

Weakening Family Support Networks

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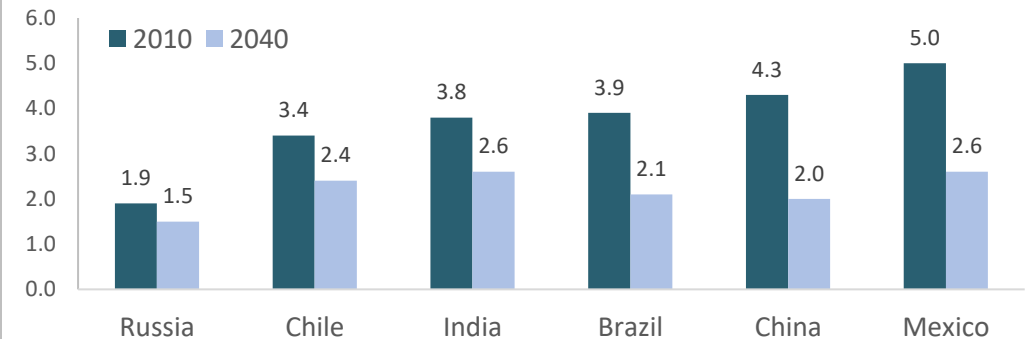
- Until recently, governments in emerging markets could count on the extended family to step in and provide for workers who reached old-age without a pension.
- Traditional family support networks, however, are already under stress from the forces of modernization and will soon come under intense new demographic pressure from declining family size.
- The failure to build more inclusive and adequate retirement systems could result in a humanitarian aging crisis of immense proportions.

Share of Respondents Saying That Grown Children or Other Family Members Should, Ideally, Be Mostly Responsible for Providing Income/Personal Care to Retired People.



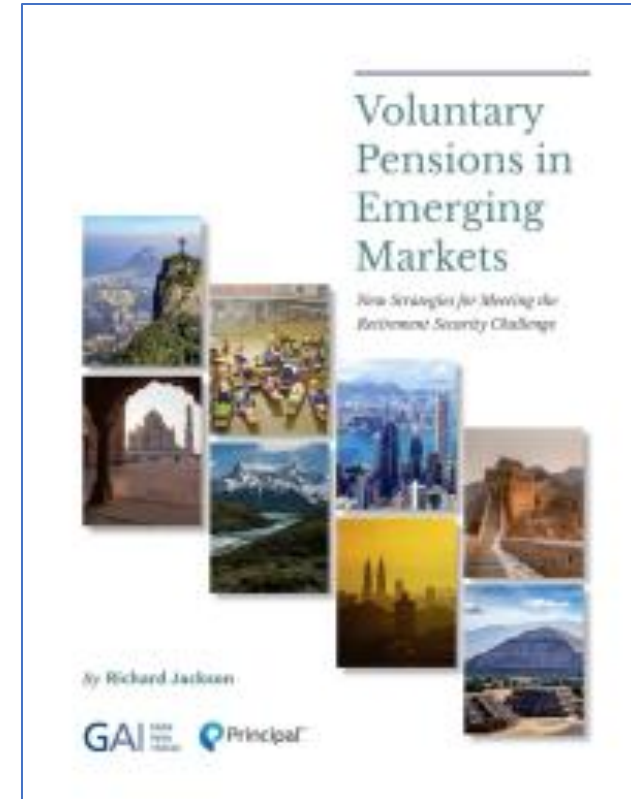
Source: East Asia Retirement Survey: Wave 2 (GAI, 2015)

Average Number of Surviving Children of the Elderly (Aged 60 & Over), by Country in 2010 and 2040



Source: Global Aging Preparedness Index: 2nd Edition (CSIS, 2013)

- Over the past few decades, most emerging markets have tried to address the coverage problem by putting in place some sort of noncontributory “social pension.”
- While social pensions are a near-term necessity, they have two drawbacks: First, they threaten to become prohibitively expensive as societies age. Second, they encourage the very informality that makes them necessary.
- More recently some emerging markets, most notably China and India, have begun to experiment with a promising alternative: voluntary contributory pensions with flexible contribution and withdrawal rules tailored to the needs of informal-sector workers.
- In the long run, the only lasting solution will be to extend the reach of the formal sector itself—and along with it, the reach of mandatory pension systems.





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