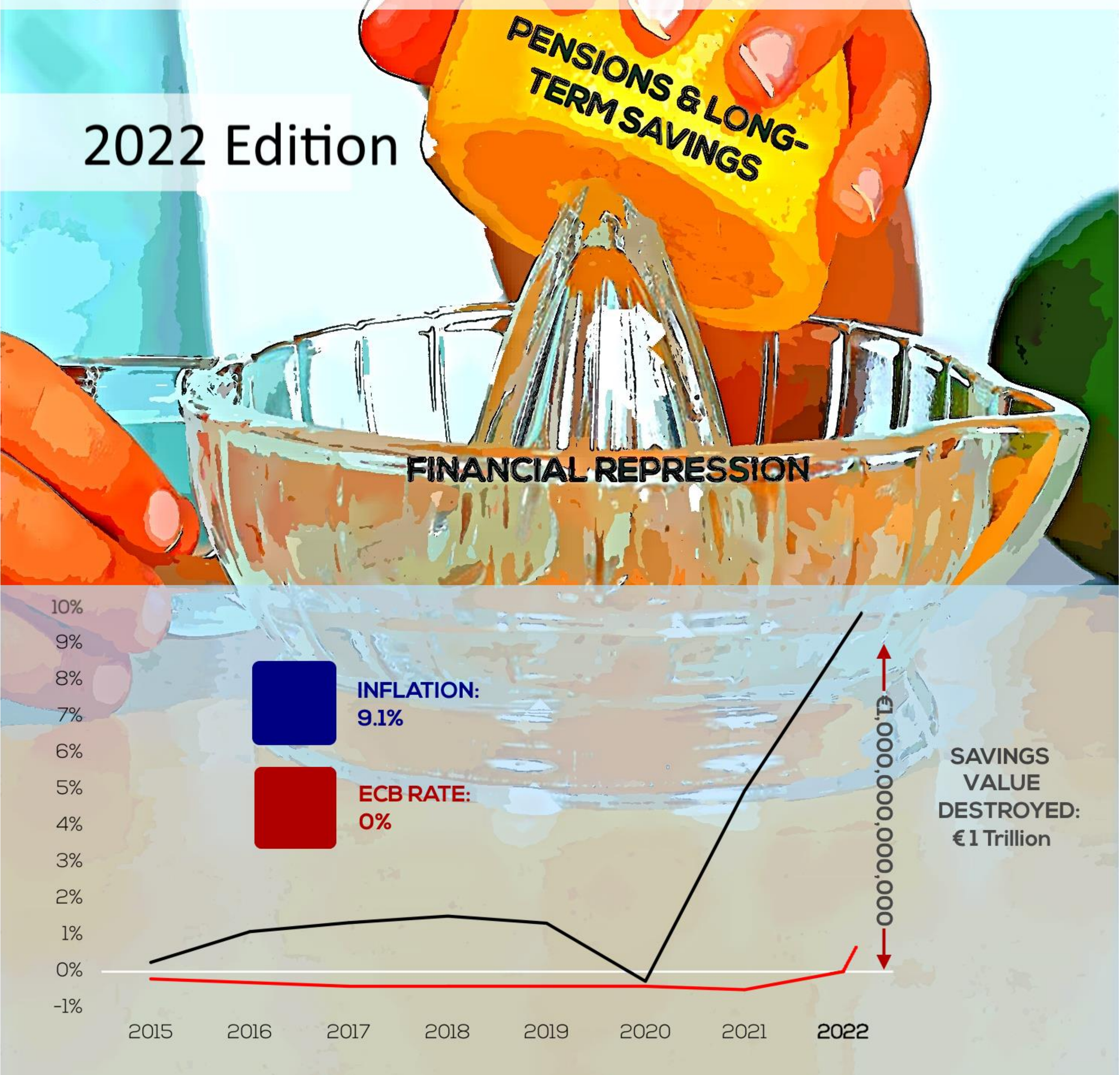
BETTER FINANCE

The European Federation of Investors and Financial Services Users
Fédération Européenne des Épargnants et Usagers des Services Financiers

# Long-Term & Pension Savings | The Real Return

## 2022 Edition



# Pension Savings: The Real Return

## 2022 Edition

**A Research Report by BETTER FINANCE**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# Pension Savings: The Real Return

## 2022 Edition

## *Executive Summary*

> *"With the two of three worst financial meltdowns of the past hundred years occurring in the past 12 years, can our societies rely on financial markets to deliver decent retirement outcomes for millions around the world?"*[1]

### Strong equity returns in 2021 slowed down by inflation, which is here to stay

***How much did pension savers earn on average?***

In this report, we aim to provide pension comparisons on every front possible. The aggregate summary return tables compare the annual average rates of returns between occupational/collective (Pillar II) pension schemes and between voluntary/individual ones (Pillar III) on 5 periods: 1, 3, 7, 10 years. These standardised periods eliminate inception and market timing biases, allowing to "purely" compare performances between different pension schemes. For information purposes, we also show the average return since data is available (last column).

| Aggregate summary return table | Pillar II | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 1 year | | 3 years | | 7 years | | 10 years | | max. available* |
| | 2021 | 2020 | 2019-2021 | 2018-2020 | 2015-2021 | 2014-2020 | 2012-2021 | 2011-2020 | |
| Austria*** | 3.08% | 1.40% | 4.12% | 1.23% | 1.92% | 2.35% | 2.68% | 1.79% | 1.56% |
| Belgium | n.a | n.a | n.a | n.a | n.a | n.a | n.a | n.a | n.a |
| Croatia | 2.55% | 8.06% | 3.38% | 2.81% | 4.76% | 4.99% | 4.82% | 4.10% | 3.25% |
| Denmark | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| Estonia | 1.30% | 7.97% | 4.60% | 2.10% | 1.61% | 2.13% | 2.35% | 1.31% | 0.75% |
| France | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| Germany | n.a. | 3.53% | n.a. | 2.23% | n.a. | 2.63% | n.a. | 2.46% | 2.35% |
| Italy | 1.44% | 7.30% | 3.96% | 1.85% | 1.97% | 2.81% | 3.30% | 2.66% | 0.86% |
| Latvia | 2.21% | 8.43% | 4.22% | 1.12% | 1.15% | 1.54% | 2.30% | 1.45% | 0.05% |
| Lithuania | 5.97% | 14.92% | 8.60% | 4.72% | 3.95% | 4.07% | 4.60% | 3.52% | 1.95% |
| Netherlands | 0.85% | 6.23% | 6.58% | 5.01% | 3.84% | 5.79% | 5.00% | 5.26% | 2.80% |
| Poland | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| Romania | -2,58% | 2,59% | 1,64% | 1,81% | 1,23% | 2,68% | 2,83% | 2,95% | 2,04% |
| Slovakia | 3.38% | 5.37% | 3.13% | 0.70% | 1.59% | 1.50% | 1.43% | 0.79% | 0.21% |
| Spain | 1.52% | 2.10% | 2.25% | 2.40% | 3.02% | 3.86% | 2.56% | 2.86% | 0.86% |
| Sweden | 13.50% | 6.45% | 17.44% | 8.23% | n.a. | n.a. | n.a. | n.a. | 10.59% |
| UK | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |

*Source: BETTER FINANCE own composition; *whole reporting period differs between countries; **UPF data used as proxy for Pillar II; ***Pension funds used as proxy for Pillar II, 2021 data is estimated; data for Netherlands Pillar II is only occupational pension funds*

[1] Amin Rajan (Crate Research), 'Coronavirus Crisis Inflicts a Double Blow to Pensions' (FT.com, 15 April 2020) available at: https://www.ft.com/content/bd878891-4f20-46c3-ab23-939162a85d9c.

Voluntary pension products vary in market share based on the jurisdiction: in some cases, insurance-based products are more prevalent, whereas in some countries pension funds are preferred. The table below shows the average real net returns for supplementary pensions by standardised holding periods.

| Aggregate summary return table | Pillar III | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | 1 year | | 3 years | | 7 years | | 10 years | | whole reporting period* |
| | 2021 | 2020 | 2019-2021 | 2018-2020 | 2015-2021 | 2014-2020 | 2012-2021 | 2011-2020 | |
| Austria* | 0.44% | 1.27% | 0.96% | 2.65% | 1.29% | 3.09% | 1.50% | 3.30% | 1.95% |
| Belgium | n.a | n.a | n.a | n.a | n.a | n.a | n.a | n.a | n.a |
| Croatia | 2.00% | -1.41% | 2.97% | 2.13% | 3.48% | 4.57% | 4.41% | 3.75% | 3.51% |
| Denmark | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| Estonia | 6.30% | 4.51% | 8.14% | 2.37% | 3.04% | 3.19% | 4.00% | 2.04% | 1.78% |
| France* | 0.37% | 1.13% | 1.55% | 0.65% | 1.07% | 1.43% | 1.63% | 1.47% | 1.47% |
| Germany** | -3.72% | 2.68% | -0.16% | 1.30% | 0.64% | 1.62% | 1.11% | 1.64% | 1.20% |
| Italy | 1.92% | 0.03% | 3.04% | 1.18% | 2.18% | 2.58% | 3.18% | 2.49% | 1.91% |
| Latvia | -1.01% | 2.14% | 3.18% | 0.82% | 0.59% | 1.75% | 2.17% | 1.58% | 1.34% |
| Lithuania | 0.54% | 4.83% | 4.65% | 2.29% | 2.17% | 2.85% | 3.37% | 1.98% | 1.03% |
| Netherlands | -2.29% | 1.83% | -0.04% | 1.39% | 1.19% | 1.14% | 0.33% | 0.27% | 0.02% |
| Poland | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| Romania | -3,07% | 0,99% | 0,60% | 0,35% | 0,22% | 1,53% | 1,90% | 1,91% | -1,00% |
| Slovakia | 1.92% | 1.30% | 3.03% | 0.08% | 0.92% | 1.00% | 1.39% | 0.44% | 0.71% |
| Spain | 2.10% | 0.86% | 1.58% | 1.33% | 2.20% | 3.08% | 2.26% | 1.60% | 0.35% |
| Sweden | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |
| UK | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. | n.a. |

*Source: BETTER FINANCE own composition; *whole reporting period differs between countries; ** Riester pension insurances contracts. Acquisition charges are included and spread over 5 years*

Unfortunately, due to unavailability of data breakdowns, for some country cases (UK, Belgium, Denmark, Poland) we were not able to calculate the annual real average returns by Pillar. Nevertheless, the results by retirement provision vehicle are available in Graphs 19 and Table 20 in the *General Report* and on an annual basis (nominal, net and real net return) in each country case).

*Note: For a few pension systems analysed in the report, the data available on retirement provision vehicles clearly distinguishes between Pillar II and Pillar III (such as Romania or Slovakia). In other countries, where pension savings products may be used for both Pillars, the categorisation is more difficult since return data is not separated as such. However, for reasons of simplicity and comparability, the authors of the report have put in all the necessary efforts to correctly assign each product according to the pillar it is, or should be, used for.*

## Taxation

### *What happens to investment returns after charges and inflation are deducted?*

Charges, investment strategies, and inflation influence earnings, but the actual sum the pension saver will be able to withdraw and spend at retirement will depend on the *taxation regime*. In other words, when and how much do savers lose of their pensions due to taxes?

The actual taxation rates (in %) are highlighted in Table GR10 and in the *Taxes* sub-section of each individual country case. The purpose of the "pillar"-system is to stimulate pension savings by giving tax incentives (exemptions, lower taxes, deductibility, subsidises etc).

The table below shows whether the three pension saving steps (contribution – *what you pay for your pension*; returns – *what your investments earn*; and pay-outs – *what you will withdraw*) are **exempt (E)** or **taxed (T)** in each country under review.

| Taxation of pension savings | | | | | | |
|---|---|---|---|---|---|---|
| | Contributions | | Returns | | Pay-outs | |
| | Pillar II | Pillar III | Pillar II | Pillar III | Pillar II | Pillar III |
| Austria | E | E | E | E | T | T |
| Belgium | E | E | E | E | T | T |
| Bulgaria | E | E | E | E | E | E |
| Croatia | E | E | E | E | T | T |
| Denmark* | T | T | T | T | T | T |
| Estonia | E | E | E | E | T | T |
| France | E | E/T | T | T | T | T |
| Germany | T | T | E | T | T | T |
| Italy | E | E | T | T | T | T |
| Latvia | E | E | E | E | T | T |
| Lithuania | E | E | E | E | E | E |
| Netherlands | E | E | E | E | T | T |
| Poland | T | E/T | E | E | E | E/T |
| Romania | E | E | E | E | T | T |
| Slovakia* | E/T | E | E | E | E | T |
| Spain* | E | E | E | E | T | T |
| Sweden | E | E | T | T | T | T |
| UK | E | E | E | E | T | T |

**There are rules and exceptions based on the type of pension vehicle. For details, see the relevant country case; Source: BETTER FINANCE own composition*

## Pension plan types: defined contribution on top

### *Who bears the risk of adequate pensions at retirement?*

Originally, the level of pension (*benefit*) would be pre-defined by the provider of the pension plan, usually based on a formula that used some standard variables for each saver (income/salary, inflation, etc). As such, the pension plan provider bears the risk of obtaining the necessary resources (money) to pay out this ***defined benefit*** pension to the saver at retirement age.

Nowadays, most private pension plans (Pillar II and III) use a ***defined contribution*** rule. This means that the saver only knows how much he can pay for his future pension, but the actual amount and income level at retirement will depend on external factors and will be subject to capital market fluctuations, just as any other investment. In other words, the risk of obtaining an adequate pension at retirement depends on the investment decisions made by the saver, where the provider is only obliged to pay-out the ***real net returns***, before tax, earned during the investment period.

| Pension scheme type (*who bears the risk?*) | | | | |
|---|---|---|---|---|
| | Provider (defined benefit) | | Saver (defined contribution) | |
| | Pillar II | Pillar III | Pillar II | Pillar III |
| Austria | X | | X | X |
| Belgium | X | X | X | X |
| Bulgaria | | | X | X |
| Croatia | X | | | X |
| Denmark | X | X | X | X |
| Estonia | | | X | X |
| France | X | | X | X |
| Germany | X | | X | X |
| Italy | | | X | X |
| Latvia | | | X | X |
| Lithuania | | | X | X |
| Netherlands | X | | X | X |
| Poland | | | X | X |
| Romania | | | X | X |
| Slovakia | | | X | X |
| Spain | X | | X | X |
| Sweden | X | | X | X |
| UK | X | | X | X |

<u>*Source*</u>: BETTER FINANCE own composition

For more details on how this information unfolds, what factors influence pension savings and how Governments tax pension earnings, read the following chapter or the individual country case corresponding to your domicile.

# Pension Savings: The Real Return

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## *Policy Recommendations*

*Value for money, transparent, comparable and simple long term and pension savings products*

### 1. End the sovereign debt and fixed income biases in pension vehicles

Prudential rules hamper long-term investments by imposing a debt, particularly sovereign, bias.

All regulations applying to long-term and pension savings should not discriminate long-term equity investments, in particular life-cycle strategies which adapt risk to the investment horizon of the saver (as is the case of the AP7 Safa fund). Also, the investment risk scale has to be reviewed to stop promoting such asset classes as money market as the safest for pension products

### 2. Stop penalizing taxation of long term and pension products

Taxation on pensions (either contributions, returns, or pay-outs) should be on **real values**, not nominal. Tax should be levied only after adjusting values by the harmonised consumer price index. To recoup the value of pension pots, at least Pillar II schemes should apply an "EEE" regime. Pillar II contributions should be deductible from the income base tax.

### 3. Urgently improve long-term and pension reporting

This report showcases the growing difficulty to obtain even the net returns of long-term and pension savings. On charges, it is an almost impossible task.

EU law should take the example of the certain national competent authorities which are required, by law to adequately report figures on a monthly basis, and constantly publicly report and update: the assets under management and net assets under management; the unit value; the asset allocation; the number of participants of all supervised vehicles in the area of long-term and pension savings.

EU authorities should follow-up on the High-Level Forum on the Future of the Capital Markets Union (HLF CMU) recommendations to establish individual pension tracking systems.

### 4. Provide simple, intelligible, and comparable reporting on long-term and pension products across the EU

Obtaining information on long-term and pension vehicles, as well as monitoring them, should not be difficult for non-professional savers. This implies also reinstating standardised actual cost and past performance disclosure, and in <u>real terms alongside the less relevant nominal ones.</u>

## 5. Harmonise and reinforce rules to curb the conflicts of interests in the distribution of long-term and pension saving products

In certain cases – showcased in our report – savers are directed to fee laden and often poorly performing products, mostly due to biases in the distribution process of investment products. Value for Money should be enforced in this service as well and the incentive of distributors should be aligned with those of their clients.

## 6. Improve the European Supervisory Authorities' (ESAs – ESMA, EIOPA) reports on cost and performance of retail investment products

Currently, the data and coverage of these reports – on markets under their supervision – are incomplete and based on commercial databases or surveys. Regulatory reporting should be the main source of these reports.

## 7. Improve the governance of collective long-term and pension schemes

In order to drive long-term **real** outperformance, the governing bodies of these schemes must have independent members representing the interests of beneficial owners.

## 8. Allow savers to defer contributions to pension products without penalties

## 9. Introduce auto-enrolment in occupational pensions

Romania, Sweden and Slovakia serve as *best practice* examples: the active labour force should be enrolled automatically in a default pension fund, with the free choice to withdraw or switch providers at no additional cost. This was also a recommendation of the HLF CMU report.

## 10. Urgently establish harmonised insurance guarantee schemes in the EU

EU citizens are partially covered against the default of product manufacturers through Deposit Guarantee Schemes ("DGS" Directive 2014/49/EU) and Investor Compensation Schemes ("ICS" Directive 97/9/EC). However, many pension savers across the EU lack an appropriate protection for insurance-based pension products. This is all the more important as these products (such as life insurances) are predominant in some EU pension systems (France for instance).

BETTER FINANCE calls on the EU co-legislators to revamp the project for a Regulation on Insurance Guarantee Schemes, which should mimic the rules from the DGS Directive, and urgently harmonise protection against insurance defaults at a minimum level across the EU.

## 11. Provide clear intelligible information on sustainability of European long-term retirement savings and investments

More and more retail investors are asking to invest in financial products that take into consideration sustainability criteria considering environmental, social and governance objectives as important factors for their investments.[2]

- Develop a clear, precise and common **taxonomy** established on science and facts focussing on all the three criteria (E, S, G);
- Develop **a well-designed EU-wide Ecolabel** for retail investment products, that avoids the pitfalls of existing national labels;
- **Address the short-termism by e**nsuring the link and consistency between **sustainability** and **long-term value creation** by putting exemplarity with regard to investor protection rules first and ensuring decent returns for individual investors at the very least that the very least do not destroy the value of their savings;
- Combine clear and intelligible ESG disclosures with the financial disclosures, preferably integrated in one document to ensure that savers and investors are able to see the **holistic picture of a** product;
- Require sustainability or ESG-specific knowledge and training of board members in long-term and pension vehicles.

[2] FINANCING A SUSTAINABLE EUROPEAN ECONOMY, Final Report 2018 by the High-Level Expert Group on Sustainable Finance https://ec.europa.eu/info/sites/info/files/180131-sustainable-finance-final-report_en.pdf

# Pension Savings: The Real Return

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## *Country Case: Austria*

## Summarisch

Rund 90% des durchschnittlichen Alterseinkommens in Österreich stammen aus dem öffentlichen Pensionssystem. Damit ist die Altersvorsorge sehr stark auf die erste Säule konzentriert. Die betriebliche Altersvorsorge wird in erster Linie von Pensionskassen und Versicherungsunternehmen getragen. Direktzusagen sind ein alternatives Instrument deren Nutzung seit Jahren stagniert. Die Möglichkeit für beitragsorientierte Pensionspläne in Pensionskassen und über Versicherungen hat die Verbreitung der betrieblichen Altersversorgung in Österreich gestärkt. Während betriebliche Formen der Altersvorsorge im Laufe der Zeit beliebter wurden, dämpften niedrige Zinssätze und die hohe Liquiditätspräferenz die Nachfrage nach individuellen Lebensversicherungsverträgen. In den Jahren 2002 bis 2021 war die Performance der Pensionskassen real und nach Abzug der Verwaltungskosten positiv. Die annualisierte Durchschnittsrendite lag bei 1,5% vor Steuern. Die Lebensversicherungsbranche verfolgt eine deutlich konservativere Anlagepolitik und erzielte eine durchschnittliche reale Nettorendite vor Steuern von 1,9% pro Jahr.

## Summary

With around 90% of the average retirement income received from public pension entitlements, the Austrian pension system is very reliant on the first pillar. Occupational pensions are primarily offered through pension funds and insurance companies. Direct commitments are an alternative vehicle, but their usage stagnates. The option for defined contribution (DC) plans with favourable tax treatment offered either by pension funds or insurance companies boosted the prevalence of occupational pensions in Austria. While occupational pensions have become more popular over time, low interest rates and a high liquidity preference dampened demand for individual life insurance contracts. Over the years 2002 through 2021, the performance of pension funds in real net terms has been positive, with an annualised average return of 1.5% before tax. The life insurance industry followed a distinctly more conservative investment policy and achieved an average annual net real return before tax of 1.9%.

Summary Table Austria. Annualised Performance for Various Holding Periods (in %)

| | Holding period | Nominal return before charges, inflation, and tax | Nominal return after charges, before inflation and tax | Real return after charges and inflation before tax |
|---|---|---|---|---|
| *Pension funds* | In years | In % | | |
| | 1 | 7.62 | 7.51 | 3.71 |
| | 3 | 7.21 | 7.10 | 4.91 |
| | 5 | 4.41 | 4.26 | 2.15 |
| | 7 | 4.07 | 3.92 | 2.03 |
| | 10 | 4.98 | 4.81 | 2.92 |
| | Since 2002 | 3.70 | 3.47 | 1.49 |
| | | | | |
| *Pension insurance* | | | | |
| | 1 | 4.62 | 4.24 | 0.44 |
| | 3 | 3.53 | 3.16 | 0.96 |
| | 5 | 3.44 | 3.07 | 0.95 |
| | 7 | 3.55 | 3.19 | 1.29 |
| | 10 | 3.75 | 3.40 | 1.50 |
| | Since 2002 | 4.28 | 3.91 | 1.95 |

S: Compare Tables AT4 and AT5. Annualised performance corresponds to geometric mean over the holding period.

## Occupational and voluntary personal pension vehicles

Private pensions are divided into voluntary occupational and voluntary personal pensions. About 6.5% of today's retirees receive regular benefits from an occupational or personal pension. This figure is made up by 4% of retirees receiving benefits from an occupational pension and 2.5% of retirees receiving annuities from a personal pension plan (Pekanov - Url, 2017). Given today's numbers of active plan members these shares can be expected to increase substantially over time.

## Occupational pension vehicles (Pillar II)

At the beginning of 2003, the system of severance payments has been replaced by mandatory contributions towards occupational severance and retirement funds (Betriebliche Vorsorgekassen). While the old severance payment regulations continue to apply to existing employment relations, employment contracts established after the end of 2002 feature mandatory contributions of 1.53% of gross wages to these funds. The main characteristics of severance payments have been transferred to the new system, i.e., in case of dismissal the fund will pay out the accumulated amount. Beneficiaries, however, may voluntarily opt to use this instrument as a tax-preferred vehicle for old-age provision. Less than one percent of the beneficiaries use this option. We therefore do not count occupational severance and retirement funds as pension vehicles in the following.

# Country Case: Belgium

## Sommaire

En Belgique, le système de retraite est constitué de trois piliers. Le premier pilier par répartition reste le plus important des trois piliers. Les retraités bénéficient d'un taux de remplacement moyen de 61.9% en 2020. Les piliers 2 et 3 représentent les pensions complémentaires professionnelles et individuelles basées sur les cotisations volontaires des individus. Le nombre d'individus couverts par les véhicules de placements dans ces deux piliers continue de croître rapidement. Respectivement 80% et 68% de la population active est couverte par ces deux piliers. Dans chacun de ces piliers, les véhicules de placements peuvent être soit un fonds géré par une IRP dans le pilier 2 ou une banque dans le pilier 3 ou soit un contrat d'assurance groupe dans le pilier 2 ou un contrat d'assurance vie individuelle dans le pilier 3.

Sur une période de 22 ans (2000-2022), les fonds de pension gérés par les IRP (pilier 2) et les fonds d'épargne retraite (pilier 3) ont eu un rendement réel annuel moyen après charges de 2,27% et 1,9% respectivement. Au sein du pilier 2, tous les fonds à contributions définies gérés par les IRP et tous les contrats d'assurance groupe Branche 21 doivent verser un rendement minimum garanti de 1,75% sur les cotisations des employeurs et des employées. Avec la baisse des rendements des obligations d'Etat à 10 ans, les sociétés d'assurance ont revu à la baisse le rendement minimum garanti offert sur les nouvelles cotisations versées sur les contrats d'assurance groupe Branche 21. Cependant, les sociétés d'assurance continuent de garantir les anciens rendements sur les cotisations passées jusqu'au départ à la retraite. Les provisions passées sont toujours rémunérées avec des rendements garantis oscillant entre 3.25% et 4.75%. En 2018, le rendement garanti moyen était légèrement inférieur à 3%. En raison, du manque d'informations publiques, il est plus difficile de fournir des informations sur les rendements des contrats d'assurance-vie individuels souscrits dans le cadre du pilier 3.

## Summary

The Belgian pension system is divided into three pillars. The first PAYG pillar is still important among the three pillar and provides on average a replacement rate of 61.9% in 2020. Pillar II and Pillar III are both based on voluntary contributions. Numbers of individuals covered by pillar II and pillar III pension schemes continue to grow rapidly. Respectively 80% and 68% of the active population is covered by these pillars. In both pillar II and pillar III, pension scheme

can take the form of a pension fund (managed by an IORP in pillar II and by a bank in pillar III) or can be an insurance contract ("Assurance Groupe" contracts in pillar II and individual life-insurance contracts in pillar III).

Over a 22-year period (2000-2022), occupational pension funds managed by IORPs (pillar II) and pension savings funds (pillar III) had annualized real performance after charges of 2.27% and 1.9% respectively. Within the pillar II, all Defined Contributions plans managed either by IORP and "Assurance Groupe "Branch 21 contracts are required to provide an annual minimum guaranteed return of 1.75% on both employee and employer contributions. With the decline in the return on the Belgian 10-year government bonds, insurance companies were forced to decrease the minimum guaranteed return offered to new contributions on "Assurance Groupe" Branch 21 contracts. However, insurance companies continue to guarantee the previous returns on the past contributions until the retirement. Past reserves continue to have guaranteed returns range from 3.25% to 4.75%. In 2018, the average guaranteed return was slightly under 3%. Due to a lack of information, it is more difficult to provide return information on individual life-insurance contracts subscribed in the framework of pillar III.

years (2019-2021), 7 years (2015-2021), 10 years (2012-2021), and since the earliest data available.

| Summary Table BE1 – Real net returns of Belgian pension vehicles | | | | | |
|---|---|---|---|---|---|
| | Pillar II | | Pillar III | | |
| | IORP | "Assurance Groupe Branch 21" | Pension savings funds | Life Insurance Branch 21 contracts | Life Insurance Branch 23 contracts |
| 2021 | 3.07% | na | 4.8% | na | na |
| 2019-2021 | 7.05% | na | 6.7% | na | na |
| 2015-2021s | 3.48% | na | 3.0% | na | na |
| 2012-2021 | 5.07% | na | 4.8% | na | na |
| Since the earliest data available | Since 1985 (source Pensio Plus): 4.63% | 2002-2014: 2.54% | 1996-2021 (source BeAma): 5.9% | 2002-2014: 1.94% | 2005-2014: 1.57% |

Source: Tables BE13-BE19

# Pension Vehicles

## Pillar II: Occupational pension plans

The second pillar refers to occupational pension plans designed to raise the replacement rate. Savings in these plans are encouraged by tax incentives. The second pillar is based on the capitalisation principle: pension amounts result from the capitalisation of contributions paid by the employer and/or employee in the plan or by self-employed individuals. There are three types of occupational pension plans in place:

- Company pension plans;
- Sector pension plans (CBAs);
- Supplementary pension plans for self-employed individuals, company directors and an additional pension agreement for self-employed as individuals (PLCI, PLCDE, PLCIPP).
- Supplementary pension plan for employees (PLCS)

In the following section devoted to occupational pension plans, the available data reported in Tables BE2 to BE5 were provided by the Financial Services and Markets Authority (FSMA), Assuralia and the National Bank of Belgium (NBB).

The FSMA annually reports detailed information on Institutions for Occupational Retirement Provision (IORP, the EU law term for non-insurance regulated occupational pension products

# Country Case: Croatia

## Croatian summary

Hrvatska je stvorila tipični mirovinski sustav s tri stupa, gdje se državni organizirani mirovinski stup na temelju PAYG-a (preraspodjela doprinosa radno sposobnog starijeg stanovništva) nadopunjuje obveznim financiranim mirovinskim sustavom (II. Stup) i subvencionira se (izravno kao i neizravno) dobrovoljni mirovinski sistem štednje (III. stup).

Povećavajući omjer obuhvata radnog stanovništva od strane II. stub nadoknađuje slaba pokrivenost unutar III. stup. To bi moglo donijeti rastući problem niskog životnog standarda za umirovljenje populacije u budućnosti, jer I. stup pruža samo 30% stopu zamjene, a preostala dva stupa neće moći dodati značajne izvore za pojedince tijekom umirovljenja. Iako su izvedbe oba financirana stupa prilično solidne, prilično mali doprinosi i nizak omjer pokrivenosti III. Stup postavlja pitanja o adekvatnosti mirovinskog sustava u Hrvatskoj.

## Summary

Croatia has created typical 3-pillar pension system, where the state organized pension pillar based on PAYG (redistribution of contributions from working to elderly population) is supplemented by mandatory funded pension scheme (II. pillar) and subsidized (directly as well as indirectly) voluntary pension saving scheme (III. pillar).

Increasing coverage ratio of working population by the II. pillar is offset by low coverage within the III. pillar. This might bring the increasing problem of low living standard for retiring population in future as the I. pillar provides only 30% replacement rate and remaining two pillars will not be able to add significant sources for individuals during retirement. Even if the performance of both funded pillars is quite solid, rather small contributions and low coverage ratio of the III. pillar raises questions about the adequacy of the pension system in Croatia.

## Introduction

Croatian pension system is since 2002 designed on conventional World bank 3-pillar model. Croatian pension system was as of 1 January 1999 reformed by introducing a mixed public-private pension system consisting of three pillars of pension insurance:

I. **pillar** – compulsory pension insurance based on generational solidarity;
II. **pillar** – compulsory pension insurance based on individual capitalized savings;
III. **pillar** – voluntary pension insurance based on individual capitalized savings.

The collection of funds within the framework of III. pillar of pension insurance is carried out through voluntary pension funds, while pay-outs of pensions are made by pension insurance companies, and, exceptionally, pension companies, that may carry out temporary pension pay-outs from voluntary pension funds. Pension reform, which entered into force on January 1, 2019, has also introduced the possibility of pension payments by the life insurance companies.

There are no limitations on membership. Also, there are no time restrictions on the duration of membership. A member may choose the amount, duration, and dynamics of payments to the fund. Payments are not compulsory and depend solely on payer's current capabilities. The membership in the fund is not terminated by termination of payments or irregular payments. All paid funds are personally owned by a member, no matter who their payer is, and they can be inherited in full. The only condition for using the funds is reaching 50 years of age.

The Act on Voluntary Pension Funds[66] regulates the establishment and operation of voluntary pension funds, while the Act on Pension Insurance Companies regulates the establishment and operation of pension insurance companies, pension schemes and pensions and their distribution. HANFA provides supervision over the business of pension insurance companies.

Overall, the returns of II. and III. pillar pension funds over different holding periods are presented in the table below.

Table HR.02 Average nominal and real net returns of Croatian II. pillar pension funds

| Holding Period | Net Nominal Annualized Performance | Real Net Annualized Performance |
|---|---|---|
| 1-year | 7.75% | 2.55% |
| 3-years | 5.40% | 3.38% |
| 5-years | 4.90% | 3.24% |
| 7-year | 6.01% | 4.76% |
| 10-years | 6.16% | 4.82% |
| Since inception | 5.28% | 3.25% |

Source: Own elaboration, 2022

66 https://www.zakon.hr/z/709/Zakon-o-dobrovoljnim-mirovinskim-fondovima

| Table HR.03 Average nominal and real net returns of Croatian III. pillar pension funds | | |
|---|---|---|
| Holding Period | Net Nominal Annualized Performance | Real Net Annualized Performance |
| 1-year | 7.20% | 2.00% |
| 3-years | 4.99% | 2.97% |
| 5-years | 3.91% | 2.25% |
| 7-year | 4.73% | 3.48% |
| 10-years | 5.75% | 4.41% |
| Since inception | 5.54% | 3.51% |

Source: Own elaboration, 2022

## Pension Vehicles

### II. pillar – Mandatory Pension Funds

There have been 4 mandatory pension asset management companies operating in Croatia in 2021 (HANFA, 2022):

1. Allianz ZB d.o.o. društvo za upravljanje obveznim i dobrovoljnim mirovinskim fondovima
2. ERSTE d.o.o. - društvo za upravljanje obveznim i dobrovoljnim mirovinskim fondovima
3. PBZ CROATIA OSIGURANJE d.d. za upravljanje obveznim mirovinskim fondovima
4. Raiffeisen društvo za upravljanje obveznim i dobrovoljnim mirovinskim fondovima dioničko društvo

There are 12 mandatory pension funds offered to savers, while each mandatory pension company manages 3 pension funds with different investment strategy:

1. Type "A" mandatory pension fund with riskier investing strategy. Members of this fund can be persons who are at least 10 years old until the age requirements for acquiring the right to an old-age pension are met. At least 30% of the fund's net assets are invested in bonds of the Republic of Croatia, EU or OECD countries. Maximum 55% of the fund's net assets are allocated in shares of issuers from the Republic of Croatia, EU member states or OECD countries and at least 40% of the fund's net assets are denominated in Kuna.
2. Type "B" mandatory pension fund – balanced investment strategy. Initially, all members will be members of this fund, unless they choose Fund A or C themselves. At least 50% of the fund's net assets are invested in bonds of the Republic of Croatia, EU or OECD countries. Maximum 35% of the fund's net assets are invested in shares of issuers from the Republic of Croatia, EU member states or OECD countries and at least 60% of the fund's net assets are denominated in Kuna.

# Pension Savings: The Real Return

## 2022 Edition

## *Country Case: Denmark*



### Danish Summary

Det danske pensionssystem er et veludbygget 3-søjle-system. De tre søjlers betydning har gradvist ændret sig i løbet af de sidste 30 år. PAYG-systemet i søjle 1 (folkepensionen) er fortsat den væsentligste indkomstkilde for de fleste pensionister, men arbejdsmarkedspensionerne spiller en stadig større rolle. Mere end 80 pct. af arbejdsstyrken er medlem af en eller flere arbejdsmarkedspensioner. Den gennemsnitlige dækningsgrad er på et niveau omring 75%, og forventes at stige i de kommende år.

Det danske pensionssystem er karakteriseret ved en høj grad af forudgående opsparing og ved en klar arbejdsdeling mellem de offentlige, skattefinansierede pensioner og de private, opsparingsbaserede pensionsordninger. Den samlede pensionsopsparing udgør ved udgangen af 2020 5.500 mia. DKK svarende til det dobbelte af BNP.

I international sammenligning skille det danske pensionssystem ud ved, at der er meget få økonomiske fattige pensionister og pensionernes dækningsgrader er høj. Sytemet er finansielt sammehængene, og de offentlige finanser er holdbare i forhold til en aldrende befolkning. Der er således ingen aktutte reformbehov, den grundlæggende struktur er hensigtsmæssig. Der er imidlertid udfordringer knyttet til incitamenterne til opsparing og senere tilbagetrækning, og der er også fortsat en restruppe, der kun har en beskeden pensionsopsparing.

Arbejdsmarkedspensionerne er i de senere år ændret i retning af markedsbaserede produkter, hvor opsparene mere direkte bærer risikoen knyttet til blandt andet afkast variationer. Det har skabt mulighed for højere afkast, men rejser spørgsmål om risikoniveauer og risikodeling. Historisk har afkastene været høje, på gennemsnit tæt på et realt afkast på 5% efter skat over de sidste godt 10 år.  Pensionssektoren har også kunnet håndtere store kriser som fx den finansielle krise og coronakrisen. En ny normal med lave afkast udfordrer mulighederne for at levere afkast på det samme niveau som set historisk.

### Summary

The Danish pension system is a well-established 3-pillar system. The role of the pillars has changed gradually within the last 30 years. The PAYG- system of Pillar I still provides the basic income for most elderly, but occupational DC pension schemes play an increasingly important role. More than 80% of the Danish labour force is enrolled in one or more occupational

schemes. The average replacement ratio is expected to increase in the years to come from today's level at around 75%.

The Danish pension system is characterized by a high degree of funding and clear roles for the tax-based public pensions of Pillar I and the privately funded pensions. The total value of funded pension schemes in 2020 is close to €740 billion DKK,[67] about twice the Danish GDP.

In international comparison the Danish pension system stands out. There are few pensioners falling below the poverty line, and replacement rates are generally high. The system is financially viable, and public finances satisfy sustainability criteria taking into account an ageing population. There is thus no urgent need for reforms, the basic structure is sound. However, there are challenges not least in ensuring sufficiently strong incentives for savings and for later retirement, and there remains a so-called residual group with low or no pension savings.

The occupational pension schemes have in recent years changed in the direction of so-called market-based products, where the saver more directly carries the risk arising e.g., due to return variations. This has created room for higher returns but raises questions on levels of risk and risk diversification. Historically returns have been high with an average after-tax real return about 5 % over the last decade. The pension sector has also handled crises, including the financial crisis and the corona crisis. A new normal with lower rates of returns challenges the possibilities of reaching returns at the levels seen in the past.

## Introduction

The Danish pension system is in a transition from being largely based on defined-benefit tax financed pensions to a larger role of defined contribution, funded occupational pensions. The latter have been expanded to most of the labour market in the 1990s and will mature in two or three decades. This arrangement both serves to ensure decent pensions for all retired, and pension adequacy in terms of high replacement rates. The system is financially robust and prepared for an ageing population.

In international comparisons, the Danish pension system stands out by low poverty rates among the old and high replacement rates. The financially viability against the backdrop of large demographic shifts is ensured. This position is reflected in a consistently by ranked in the top A-tier in the Melbourne Mercer Global Pension Index.[68].

The challenges for the system include how to ensure an incentive structure supporting savings and later retirement. The sustainability of the system depends critically on retirement ages

[67] Denmark participates in ERM 2 at a central rate of 746.038 DKK per 100 euro, and this exchange rate I used to convert all numbers in DKK into euro.
[68] Melbourne Mercer Global Pension Index, https://www.mercer.com.au/our-thinking/global-pension-index.html#contactForm

increasing alongside increases in longevity. The heterogeneity in work career and health has raised debates on more flexible exit routes from the labour market. Moreover, it remains a challenge that groups are not covered by occupational pension arrangements.

## Description of the pension system

- The Danish pension system is a three-pillar system: the aim of the **first pillar** (Pillar I) is to prevent poverty in old age. Pillar I provides all Danish pensioners with a minimum pension. The pension schemes of the Pillar I are compulsory and regulated by law.
- The **second pillar** (Pillar II) is based on collective agreements in the labour market or employment contract ensuring that the individual contributes to a defined contribution, funded pension scheme. Collective agreements determine the contribution rates, and the pension therefore depends on income earned throughout the work career. Pillar II aims to secure a standard of living reflecting the level of income before retirement.
- The **third pillar** (Pillar III) provides individual opportunities for supplementary saving based on individual needs both in explicit pension saving schemes with special tax treatment and in general voluntary savings.

**Table DK1. Pension System Overview**

| Pillar I | Pillar II | Pillar III |
|---|---|---|
| Base pension plus means-tested supplements, tax-financed | Occupational Pension; DC, funded schemes | Voluntary Personal Pension |
| Poverty prevention in old age | Ensures a standard of living reflecting the level of income before retirement | Supplementary saving based on individual needs |
| | More than 80% of Danish labour force is enrolled in one or more occupational schemes. | Voluntary pension savings is declining in important due to the growing role of occupational pensions |
| An individual entitlement (residence requirement) regulated by law | Determined by collective agreements, but contribution is mandatory for the individual | Voluntary |
| **Quick facts** | | |
| Danish pension system has been top ranked (no 2) in the Melbourne Mercer Global Pension Index | | |
| The average replacement ratio is about 75% | | |
| | The total value of funded pension schemes exceeds is close to euro 740 billion, about twice the Danish GDP | |
| | Period 2007-2021 the average annual after-tax real rate of return for private pension schemes was close to 5% | |

*Source*: BETTER FINANCE own composition

# Pension Savings: The Real Return

## 2022 Edition

## *Country Case: Estonia*

## Kokkuvõte

Eesti pensionisüsteem on tüüpiline Maailmapanga mitmesambaline süsteem, mis põhineb personaalsetel pensionikontodel. Aastat 2021 ilmestasid kerkivad aktsiaturud ja kiirenev hinnatõus, eriti aasta teises pooles. Teise samba fondide kaalutud keskmine tootlus oli nominaalselt 13,33% ja kolmanda samba sama näitaja oli 18,34%. Tulenevalt tarbijahindade kiirest tõusust 2021. aasta lõpus, kujunes teise samba fondide inflatsiooniga korrigeeritud reaaltootluseks 1,3%. Kolmanda samba reaal-tootlus oli 6,3%.

Teise samba fondide pikaajaline kaalutud keskmine reaaltootlus aastatel 2003-2021 oli 0,75% aastas. Kolmanda samba fondide puhul oli see näitaja samal perioodil 1,78% aastas.

Alates 2016. aasta lõpust on Eesti turule lisandunud mitmeid madalate tasudega passiivselt juhitud pensionfonde (nn. indeksfonde), mis on kiirelt võitnud kliente ja suurendanud turuosa. Madalate tasudega fondide lisandumine turule on sundinud fondivalitsejaid ka teiste fondide tasusid alandama. Nüüdseks pakuvad kõik Eestis tegutsevad pensionifondide valitsejad oma valikus vähemalt üht indeksfondi.

Aastal 2020 jõustunud vastuoluline pensionireform muutis Eesti II pensionsamba vabatahtlikuks ja võimaldas pensionkogujatel oma II samba säästud enne pensioniiga reliseerida. Selle tulemusena lunastati 2021. aasta septembris ja 2022. aasta alguses ligi veerand II sambasse kogunenud pensionivarast.

Lisaks tundub käesoleva raporti kirjutamise seisuga, et 2022 võib kujuneda pensionivara ostujõu siesukohalt võrreldavaks 2008. aasta krahhiga. Põhjuseks nii langevad aktsiaturud kui kiire inflatsioon.

Need kaks hiljutist arengut panevad suure küsimärgi alla Eesti praeguse pensionisüsteemi võimekuse tagada Eesti tänastele töötajatele adekvaatne sissetulek pensionieas.

## Summary

The Estonian Pension system is a typical World Bank multi-pillar (three-pillar system) based on individual (personal) pension savings accounts. 2021 saw on average high nominal returns for both the second and third pension pillars, with Pillar II recording average returns of 13.33% and Pillar III funds averaging returns of 18.34%. After adjusting for inflation, which was the

highest it had been in decades, the real returns were: 1.3% for Pillar II funds and 6.3% for Pillar III funds. This meant that the long-term (since 2003) real returns of Pillar II funds ultimately stayed positive, albeit low, at an asset-weighted average real return since inception of 0.75%, while Pillar III funds have achieved a more respectable average real return of 1.78% over the same period.

Low-cost passively managed pension funds introduced since 2016 have forced providers to further decrease the fees charged in Pillar II as well as Pillar III pension funds, with all pension fund providers offering at least one low-cost passive fund as part of their range by mid-2021.

The year 2021 also saw almost a quarter of all pension savings withdrawn from the II pillar, after a controversial change to the pension system from the year before was implemented

Looking forward to 2022, a combination of galloping inflation and falling stock markets look likely to make it the worst year for pension savers in Estonia since the global stock market crash of 2008.

These two factors mentioned above present a huge challenge to policymakers if they wish to find ways to ensure current workers in Estonia will have adequate pensions when they retire.

## Introduction

The Estonian old-age pension system is also based on the World Bank multi-pillar approach, which consists of three main pillars:

- Pillar I – State pension organised as a mandatory Pay-As-You-Go (PAYG) scheme;
- Pillar II – Funded pension, which was previously organised as a mandatory funded defined contribution (DC) scheme, starting from January 1, 2021, it has been possible to opt-out of the II pillar funded pensions scheme;
- Pillar III – Supplementary pension organised as a voluntary individual pension scheme.

The Estonian multi-pillar pension reform began in 1998 with the introduction of the third (voluntary) pension pillar in legislation. The formerly mandatory second pillar, which finances individual private retirement accounts with matching contributions from workers and the government, was introduced in 2001 and became operational on July 1, 2002. It became possible to opt-out of the second pillar pension and to liquidate any previous savings held under it, from January 1, 2021.

inform the population that relying only on the first pillar pension will inevitably result in relative poverty upon retirement.

The authorities also need to consider that as the population ages, a large percentage of pensioners and people close to pension age being at risk of poverty might create irresistible political pressure to rapidly increase the funding for the first pillar. In the context of what is likely to be a very old population, this would put the sustainability of state finances in jeopardy.

Table EE2. Summary returns table - Estonia

| | Pillar II | | Pillar III | |
|---|---|---|---|---|
| | Nominal | Real | Nominal | Real |
| 1-year (2021) | 13,33% | 1,30% | 18,34% | 6,30% |
| 3-years (2019-2021) | 8,88% | 4,60% | 12,34% | 8,14% |
| 5-year (2017-2021 | 5,49% | 1,52% | 7,05% | 3,12% |
| 7-year (2015-2021) | 4,75% | 1,61% | 6,11% | 3,01% |
| 10-years (2012-2021) | 5,12% | 2,35% | 6,75% | 4,00% |
| Since inception (2003-2021) | 4,44% | 0,75% | 5,60% | 1,78% |

*Source: BETTER FINANCE own composition based on Pensionikeskus.ee data, 2022 (data as of 31.12.2021)*

## Pillar I – State Pension

The coverage ratio of Pillar I pensions comprises nearly 100% of the economically active population.

The state pension (Pillar I) should guarantee the minimum income necessary for subsistence after retirement. It is based on the Pay-As-You-Go (PAYG) principle of redistribution, i.e., the social taxes paid by today's employees cover the pensions of today's pensioners.

Legislatively, the state pension is governed by the State Pension Insurance Act. The act is part of the pension system reform, which came into force on January 1, 2002. Since then, the act has been amended more than 30 times. Employers pay 33% of the salary of each employee as social tax, 13% of which is for health insurance, and 20% (16% in case of participation in Pillar II) is for the pensions of today's pensioners.

There are two kinds of state pension: the pensions that depend on work contributions (the old-age pension, the pension for work incapacity and the survivor's pension) and the national pension. Estonians are entitled to the state old-age pension if they have been employed for at least 15 years in Estonia. If the period of employment is shorter, they are not entitled to the old-age state pension and might fall under the national pension system.

The **national pension** (also called National Pension Rate – NPR) provides a minimum pension for those who are not entitled to a pension that depends on work contributions, provided that they have lived in Estonia for at least five years before applying for a pension. The amount of the national pension as of April 1, 2022 (Social Insurance Board, 2022) is €275.37 (up from

# Pension Savings: The Real Return

## 2022 Edition

## *Country Case: France*

### Résumé

Le système français de retraite continue à reposer majoritairement sur les régimes d'assurance vieillesse de base et complémentaire par répartition (Piliers I et II), avec un taux moyen de remplacement du revenu d'activité de 48% en 2020,[112] et une valeur totale des actifs représentant 11.1% du PIB en 2021.[113] Malgré une allocation d'actifs plutôt dynamique, les plans d'épargne-retraite entreprise ont eu un rendement réel de +4.26% en 2021 et +0.96% en 22 ans entre 2000-2021 (+23.4% en cumulé). L'assurance vie – le produit individuel de loin le plus utilisé pour l'épargne retraite par les Français – a eu une performance très contrastée : +37.3% (+1,45% en moyenne annuelle) pour les fonds en euros (à capital garanti) encore dominants, mais -8.4% (-0,4%) pour les contrats en unités de compte qui sont davantage promus et se développent plus rapidement. Les produits individuels dédiés spécifiquement à l'épargne retraite (PERP, Préfon, Corem, etc.) sont beaucoup moins développés, et ont des performances plus opaques et le plus souvent plus mauvaises.

### Summary

The French pension system continues to rely heavily on the mandatory "pay as you go" Pillar I and Pillar II income streams, with an aggregate replacement ratio for pensions of 48%,[114] and a total value of retirement assets of 11.1% of the French GDP in 2021.[115] Despite a rather dynamic asset allocation, corporate pension plans had an annual real net return of +4.26% in 2021 and +0.96% average annual for the 22 years between 2000-2021 (+23.4% cumulative). Life insurance products - by far the most widely used personal product for pension purposes by French savers - had very contrasted long-term pre-tax real returns: +37.3% (+1.45% annual average) for the still dominant capital guaranteed ones, but -8.4% (-0.4%) for the more promoted and faster growing unit-linked ones, despite very positive listed stocks and bonds returns. The personal products specifically dedicated to pensions (PER, PERP, Préfon, Corem, etc.) are much smaller, and their performances are less transparent and most often poorer.

[112] Voir Report GR9(B) du General Report, dans la section concernant la France - *aggregate replacement ratio for pensions*, selon les données d'Eurostat.
[113] Voir Report GR10 du General Report, selon les données d'OECD *Preliminary Data* 2021 (10 Juin 2022).
[114] See Table GR9(B) in the General Report, in the section concerning France – *aggregate replacement ratio for pensions*, according to Eurostat data.
[115] See Table GR10 of the General Report, based on OECD Preliminary Data for 2021 (10 June 2022).

# Introduction

Using the World Bank multi-pillar structure, the French pension system mainly relies on:

- **Pillar I** – the public pension, a defined benefit (DB) Pay-As-You-Go (PAYG) scheme, which is managed by the State and comprises the basic pension insurance;
- **Pillar II** – the occupational retirement provision (complementary component), also DB and privately managed and funded by both employer and employee contributions, to which participation and contribution rates are mandatory;
- **Pillar III** – composed of the voluntary retirement savings plan, also privately managed, to which participation is optional, and which can be set up by the employer (voluntary occupational plans) or by providers for the pension saver on his own (voluntary personal plans).

| Introductory table: French Pension System Overview | | |
|---|---|---|
| **Pillar I** | **Pillar II** | **Pillar III** |
| Mandatory State Pension | Mandatory Private Pension | Voluntary Personal & Occupational Pension |
| Basic pension insurance | Supplement of the 50% pre-retirement income target of Pillar I | Divided into different financial retirement savings products |
| Divided into multiple sub-categories of pensions regimes for private sector, private service and special professions. | The complementary component contributions are collected by different designated paritarian institutions, depending on the sector. | Voluntary pension products are tax-incentivised in order to support participation in the third pillar and are mostly defined contribution |
| DB PAYG | DB PAYG | DC |
| Quick facts | | |
| A relatively high old-age dependency ratio of 34.3% (2021) | | |
| An average pre-retirement income replacement ratio of 48% (2020) | | |

*Sources: Table GR9(B) in the General Report*

| Summary return table - Average real net returns of French pension savings (before tax) | | | | | |
|---|---|---|---|---|---|
| Average real net returns | 1 year 2021 | 3 years 2019-2021 | 7 years 2015-2021 | 10 years 2012-2021 | whole reporting period |
| Life insurance - CG | -4.19% | -1.14% | 0.01% | 0.46% | 1.45% |
| Life-insurance - UL | 3.41% | 1.00% | 1.71% | 3.17% | -0.40% |
| Corporate plans | 4.21% | 4.38% | 1.78% | 2.68% | 0.96% |

*Sources: Tables FR3, FR5, FR7; CG = capital guaranteed; UL = unit-linked; PS = pension schemes;*
** return proxy measure*

## Country Case: Germany

## Zusammenfassung

Das deutsche Rentensystem gehört zu jenen, in denen das System der gesetzlichen Rentenversicheurng (Säule I) eine relativ wichtige Rolle für das Alterseinkommen der deutschen Rentner spielt. Die Bruttorentenersatzrate aus dem obligatorischen öffentlichen System beträgt 41,5% des individuellen Einkommens (gegenüber durchschnittlich 42,2% im Durchschnitt der OCED-Länder), während die Ersatzrate aus freiwilligen Systemen (Säule II und Säule III zusammen) 14,1% beträgt. Die Riester- und Rürup-Reformen von 2002 und 2005 zielten auf eine stärkere Beteiligung deutscher Arbeitnehmer an betrieblichen und individuellen Altersversorgungssystemen ab, da die akkumulierten Ansprüche relativ gering waren.

## Summary

As in most EU countries, the German pension system is among those where the mandatory public scheme (Pillar I) plays an important role in retirees' old-age income, though the replacement rate from mandatory public scheme remains lower than in many other European countries including France and especially Italy and Spain. The average gross pension replacement rate from mandatory public scheme for a full-career average earner is equal to 41.5%[166] of individual earnings (against 42.2% on average in OCED countries, 60.2% in France, 73.9% in Spain and 74.6% in Italy), while the replacement rate from voluntary schemes (Pillar II and Pillar III together) is 14.1%. With a relatively low level of accumulated entitlements, the *Riester reform (in 2002)* and the *Rürup* reform (in 2005) were aimed at increasing participation in occupational and individual pension schemes for German workers.

[166] OECD (2021), Pensions at a Glance 2021: OECD and G20 Indicators, OECD Publishing, Paris

boost personal pension savings, followed by The *Rürup* pension in 2005 to further complement personal pension plans.

| Table DE1. Introductory Table - Pension System Overview | | |
|---|---|---|
| **Pillar I** | **Pillar II** | **Pillar III** |
| Mandatory State Pension Insurance: | Voluntary Occupational Pensions: | Voluntary Personal Pensions: |
| all persons subject to social security charges contributed 18.7% of their gross income to the scheme | employees have the right to a deferred compensation arrangement - employers the right to choose the scheme | supplement to the statutory pension insurance |
| | Occupational retirement schemes that can be divided into two sub-pillars: 1) direct pension promise - 2) external occupational pension schemes | Riester pension or Rürup pension or life insurance |
| Mandatory for all employees who are subject to social insurance contributions | Voluntary or by tariff agreement | Voluntary |
| PAYG | DB and hybrid | DC |
| Quick facts | | |
| Coverage (active population): 90% | About half of today's retirees receive income from a private pension | |
| Gross replacement rate: 41.5% | Gross replacement rate: 14.1% | |
| | 16.5 million contracts recorded by the German Insurance Association | 16.2 million *Riester* contracts |

*Source: BETTER FINANCE own composition*

In the table below we present the annualized real net rates of return for retirement provision vehicles in Germany.

| Aggregate summary annualised return table - After charges, inflation and before tax | | | | |
|---|---|---|---|---|
| | | Pillar II | Pillar III (1) | Pillar III (2) |
| 1 year | 2021 | n.a. | -3.72 | -3.55 |
| | 2020 | 3.53 | 2.68 | 2.78 |
| 3 years | 2019 - 2021 | n.a. | -0.16 | -0.05 |
| | 2018 - 2020 | 2.23 | 1.30 | 1.36 |
| 7 years | 2015 - 2021 | n.a. | 0.64 | 0.73 |
| | 2014 - 2020 | 2.63 | 1.62 | 1.68 |
| 10 years | 2012 - 2021 | n.a. | 1.11 | 1.18 |
| | 2011 - 2020 | 2.46 | 1.64 | 1.70 |
| Whole reporting period* | | 2.35 | 1.20 | 1.84 |

**maximum available in this report*

*(1) Riester pension insurances contracts. Acquisition charges are included and spread over 5 years.*
(2) Classic pension insurance products or life insurance products. Acquisition charges are included and spread over 5 years.

# Pension Savings: The Real Return

## 2022 Edition

## *Country Case: Italy*

## Sommario

Il sistema pensionistico italiano ha avuto una spesa pubblica del 17% del PIL nel 2020, 0,2 p.p. aumento rispetto al 2019 (16,8% del PIL). La riforma del sistema pensionistico italiano nel 2011 ha creato un solido regime di primo pilastro, con un tasso di sostituzione aggregato delle pensioni del 73% nel 2019, uno dei più alti tra i casi nazionali presi in esame in questo Rapporto. Considerando anche il tasso di partecipazione relativamente basso delle famiglie italiane ai mercati dei capitali, l'incentivo a indirizzare il reddito disponibile verso il risparmio previdenziale privato oi prodotti di investimento è basso. Complessivamente il 67,3% dei pensionati italiani percepisce una sola pensione e il 24,7% percepisce due pensioni (quindi pensioni pubbliche e private). Ciò risulta evidente se si considera la percentuale del patrimonio dei fondi pensione italiani, pari al 10% del PIL, nonché il tasso di copertura del secondo pilastro del 20% e del terzo pilastro del 14,2% della forza lavoro.

Per quanto riguarda le performance, i fondi pensione contrattuali hanno restituito x% annuo in media negli ultimi 21 anni (2000-2020). I fondi pensione aperti hanno restituito in media x% annuo nello stesso periodo., PIP (Piani Individuali Pensionistici) con utili realizzati in media x% annuo negli ultimi 13 anni, mentre i PIP unit-linked hanno registrato % annua in media nello stesso periodo. Tutti i rendimenti sono espressi al netto di oneri e inflazione.

## Summary

The Italian general government's public expenditure on old-age pensions increased over the last 21 years from 11.4% to 15.1% of GDP. The Italian pension system reform in 2011 created a strong Pillar I scheme, with an aggregate replacement ratio for pensions of 72% in 2020 (second highest of the country cases analysed in this report) and 77% in 2021 (highest based on available data). Considering also the relatively low participation rate of Italian households in capital markets – which however increased over 2020 and 2021 - the incentive to direct available income to the private retirement savings or investment products is low. A total of 67.3% of Italian pensioners receive just one pension, and 24.7% received two pensions (meaning public and private pension income). This becomes apparent when looking at the percentage of Italian pension funds' assets, of 10% of GDP, as well as the coverage ratio for Pillar II of 20% and Pillar III of 14.2% of the labour force.

With regards to performances, contractual pension funds returned x% annually on average over the past 21 years (2000-2020). Open pension funds returned -% annually on average over

the same period., PIP (*Piani Individuali Pensionistici*) with-profits experienced % annually on average over the past 13 years, while PIP unit-linked experienced % annually on average over the same period. All returns are expressed net of charges and inflation.

## Introduction

The Italian Pension System is divided into three pillars:

- Pillar I – the public (state) pension scheme;
- Pillar II – the occupational (mandatory) pension arrangements;
- Pillar III – the individual (voluntary) pension schemes.

### Pillar I – State Pension

The first pillar (state and mandatory) is the main pension vehicle in Italy and is made up of two tiers: the zero and first tier. The zero tier consists of a social pension ensuring a minimum level of income for the elderly. The first-tier covers employed individuals and it constitutes a notional defined contribution system for all future generations.[202]

The Italian pension system used to be a Defined Benefit system. Since 1995, it is based on a Notional Defined Contribution system. The Italian state pension system went through intensive reforms. The year 1995 can be seen as a turning point, moving from a defined benefits system towards a defined contribution system. The Dini reform (law 335/1995) is one of the most important reforms towards the restructuring of the Italian pension system. As a result, all workers entering the job market after 1995 have been accruing their pension entitlement according to a defined contributions method, while before 1995 pension entitlements were computed according to an earnings-related system.

The next pension reform came on the background of an ageing population and a massive pension expenditure (relative to the GDP). In 2011, the minister of Welfare and Social Policy under the Monti Government, Elsa Fornero, implemented a state pension reform (law n.214) to bring the system closer to equilibrium. Under the new system, pension eligibility is based on working years rather than age. Earlier retirement is possible, but subject to penalties. The public pension system was thus sustainable. Nevertheless, the Italian Constitutional Court stated in April 2015 that the suppression of indexation of pensions on inflation included in the "Fornero law" was unconstitutional. The indexation of pensions on inflation was estimated to €500 million in unforeseen costs to the first pillar.

Further followed the "Quota 100" measure, which means that if the sum of the age and number of years worked is 100, the worker can retire. Since January 1st, 2019, the new measure offers the opportunity for workers aged at least 62 with 38 years of contributions to retire earlier than the normal retirement age of 67 years. The "Quota 100" was modified to

[202] Since the structural reform implemented by Minister Dini in 1995, the Italian pension system has been re-designed according to the Notional Defined Contribution system, in order to guarantee the stability of public finances.

| Introductory table. Multi-pillar pension system in Italy | | |
|---|---|---|
| PILLAR I | PILLAR II | PILLAR III |
| State Pension | Private, voluntary and collective funded system | Private, voluntary and individual savings |
| | Legislative Decree 124/93 on complementary pension plans implemented in 1993<br>Reform on complementary pension (Legislative Decree 252/2005) | |
| National Social Security Body (INPS) | Pension accumulation companies | Insurance companies |
| Mandatory | Voluntary | Voluntary |
| Publicly managed | Privately managed pension funds | Privately managed pension funds |
| PAYG | Partially or fully funded | Fully Funded |
| Notional Defined Contribution system (NDC) | DC (Defined Contribution scheme) | |
| Quick facts | | |
| Number of old-age pensioners: 9,368,107 | Funds: 277 | Funds (new PIP): 72 |
| Average old-age pension: €1,393 | AuM: €131.9 bn. | Old & new PIP, AuM: €51.3 bn. |
| Monthly household average income (net): €2,492 | Participants in 2021: 5.7 million | Participants in 2021: 3.8 million |
| Aggregate pension replacement rate (2021): 77% | Coverage ratio: 22.8% | Coverage ratio: 15.1% |

*Source*: BETTER FINANCE composition based on COVIP Annual Report 2021 and INPS data for 2020

The real net returns (before taxes) of the main retirement provision vehicles in Italy are presented below based on 6 recommended holding periods: 1 year (2021), 3 years (2019-2021), 7 years (2015-2021), 10 years (2012-2021), and since the earliest data available (22 years for pension funds, 2000-2021, and 14 years for PIP, 2008-2021).

| Summary Table – Real net returns of Italian pension vehicles (before tax) | | | | |
|---|---|---|---|---|
| | Contractual pension funds | Open pension funds | PIP with profits | PIP unit-linked |
| 2021 | 0.72% | 2.16% | -2.74% | 6.57% |
| 2019-2021 | 3.57% | 4.35% | 0.00% | 6.00% |
| 2015-2021 | 1.70% | 1.95% | 0.28% | 2.93% |
| 2012-2021 | 1.90% | 2.05% | 0.77% | 3.51% |
| 2008-2021 | 1.86% | 1.65% | 1.16% | 5.14% |
| 2000-2021 | 1.29% | 0.41% | n.a. | n.a. |

*Source*: Tables IT5 and IT6

# Pension Savings: The Real Return

## 2022 Edition

## *Country Case: Latvia*


## Summary

Funded pension schemes have experienced negative average returns during their existence even the portfolio of pension funds in mandatary pension pillar is conservatively oriented. Pillar II pension funds recorded on average exceptional annual nominal return of 10.11% in year 2021, while Pillar III funds delivered also on average positive nominal return of 6.89%. A positive development could have been seen on the Pillar II market, where the introduction of passively managed funds contributed to further decrease of fees. The fees have decreased also in the Pillar III, however, complex fee structure and still higher fees of Pillar III pension funds play a significant role on the expected accumulated benefits.

## Kopsavilkums

Fondēto pensiju shēmas savas pastāvēšanas laikā ir piedzīvojušas negatīvu vidējo ienesīgumu, pat ja pensiju fondu portfelis obligāto pensiju pīlārā ir konservatīvi orientēts. II pīlāra pensiju fondi 2021 gadā uzrādīja vidēji nelielu gada nominālo ienesīgumu 10.11% apmērā, savukārt III pīlāra fondi uzrādīja arī vidēji pozitīvu nominālo ienesīgumu 6.89% apmērā. Pozitīva attīstība bija vērojama II pīlāra tirgū, kur pasīvi pārvaldīto fondu ieviešana veicināja turpmāku komisijas maksu samazināšanos 2020. gadā. Maksa ir samazinājusies arī III pīlārā, tomēr III pīlāra pensiju fondu sarežģītā maksu struktūra un joprojām augstākas maksas būtiski ietekmē gaidāmos uzkrātos ieguvumus.


## Introduction

Latvia is currently operating a multi-pillar pension system based on three pension pillars. The reform followed World Bank recommendations on creating a pension system with unfunded PAYG and funded pension pillars. Since 2001, the Latvian multi-pillar pension system includes:

- Pillar I (state compulsory PAYG pension scheme);
- Pillar II (mandatory state funded pension scheme) which is financed by a part of the social insurance contributions diverted from Pillar I;
- Pillar III (voluntary private pension scheme).

The introduction of the multi-pillar pension system has aimed its overall functionality on a different approach to each pension pillar operation, but with the overall objective of ensuring

| Table LV 1: Multi-pillar pension system in Latvia | | |
|---|---|---|
| **Pillar I** | **Pillar II** | **Pillar III** |
| **State Pensions** | **State Funded pensions** | **Voluntary private pensions** |
| Mandatory | Mandatory | Voluntary |
| NDC PAYG | Funded | Funded |
| Financed by social insurance contributions | DC | DC |
| Benefits paid via State Social Insurance Agency | Financed by social insurance contributions | Privately managed two types of pension plans: |
| Publicly managed | Individual pension accounts | 1. open (individual), |
| | Privately (and publicly) managed pension funds | 2. closed (quasi occupational) |
| Coverage: generally, all population | Coverage: generally entire working population | Coverage: Cannot be calculated due to missing information about number of participants |

*Gross replacement ratio: 30% (1,435 € average wage; 432 € average old-age pension)*
*Source: Own elaboration, 2022*

## Pillar I – State Pension Insurance

State old-age pension (Pillar I) should guarantee the minimum income necessary for subsistence. It is based on an NDC PAYG principle of redistribution, i.e., the social tax paid by today's employees covers the pensions of today's pensioners. However, the amount of paid contributions for each saver are recorded on individual accounts.

The state old-age pension is paid out of the social insurance contributions. Total level of social insurance contributions is 34.09% of gross salary for employees (employers contributes 23.59% and employees 10.5%; self-employed persons pay 27.52%). Of the total contribution, 14% funded the Pillar I NDC pension and 6% was redirected to the individual's account under Pillar II. The remaining portion of contributions financed social security elements such as disability pension, sickness and maternity benefits, work injury benefits, parent's benefits, and unemployment benefits.

The **statutory retirement age**[208] in Latvia in 2021 is 64 years both for men and women. However, the law stipulates a gradual increase of the retirement age by three months every year until the general retirement age of 65 years is reached in 2025. Early pension is possible in Latvia if two conditions are met: 1) an individual in 2021 reaches the age of at least 62 years (gradually rising by three months a year until 2025) and 2) an individual contributed for a period of at least 30 years.

[208] https://latvija.lv/en/PPK/socialie-pakalpojumi/sociala-apdrosinasana/p311/ProcesaApraksts

# Pension Savings: The Real Return

## 2022 Edition

## *Country Case: Lithuania*

## Santrauka

Lietuva priėmė tipišką Pasaulio banko daugiapakopę sistemą, kurioje PAYG pakopa (valstybinė pensija, I pakopa) vis dar atlieka dominuojantį vaidmenį užtikrinant senatvės pensininkų pajamas. Nuo 2019 m. II pakopos santaupų kaupimas vyksta gyvenimo ciklo pensijų fonduose, kurie patys keičia investavimo riziką pagal dalyvių amžių. Nuo 2019 m. palaipsniui mažinamas valdymo mokestis už kaupimą II pakopos gyvenimo ciklo fonduose. 2019 m. jis sudarė 0,8 proc. ir 2020 m. tapo 0,65 proc. Nuo 2021 m. metinis turto valdymo mokestis dar labiau sumažintas iki 0,5 proc. Turto išsaugojimo fondui turto valdymo mokestis sudarys tik 0,2 proc.

Apskritai 2021 m. abiejų pakopų pensijų fondų veiklos rezultatai visose turto klasėse buvo gražiai teigiami, tačiau pensijų fondų, kurių rizikos ir grąžos profiliai buvo skirtingi, grąža gerokai skyrėsi.

## Summary

Lithuania adopted the typical World-Bank multi-pillar system, where the PAYG pillar (state pension, Pillar I) still plays the dominant role in ensuring the income for old-age pensioners. As of 2019, accumulating savings in Pillar II takes place in life-cycle pension funds, which change investment risk themselves on the basis of participants’ age. Since 2019, management fee for accumulating in Pillar II life-cycle funds is being gradually reduced. In 2019 it was 0.8 per cent and in became 0.65 per cent in 2020. From the year 2021 the annual asset management fee was further decreased to 0.5 per cent. For the asset preservation fund, the management fee will be just 0.2 per cent.

Overall, pension funds’ performance in both pillars were nicely positive in 2021 across all asset classes, however there were significant differences among the pension funds´ returns with different risk-return profiles.

| Table LT 1: Multi-pillar pension system in Lithuania | | |
|---|---|---|
| PILLAR I | PILLAR II | PILLAR III |
| State Pension | Funded pension | Voluntary pension |
| Law on State Social Insurance Pensions | Law on the Reform of the Pension System; Law on Pension Accumulation | Law on the Supplementary Voluntary Pension Accumulation |
| State Social Insurance Fund institutions | Pension accumulation companies | Pension accumulation companies |
| Mandatory | Quasi/Mandatory | Voluntary |
| Publicly managed | Privately managed pension funds | Privately managed pension funds |
| PAYG | Funded | Funded |
| PS (Pointing System - Defined benefit scheme based on salary) | DC (Defined Contribution scheme) | |
| | Individual personal pension accounts | |
| Quick facts | | |
| Number of old-age pensioners: 607,200 | Administrators: 5 | Administrators: 4 |
| Average old-age pension: € 413.77 | Funds: 40 | Funds: 15 |
| Average income (gross): € 1,566 | AuM: € 5,909.61 mil. | AuM: € 220.27 mil. |
| Average replacement ratio: 26.44% | Participants: 1,387,923 | Participants: 79,197 |
| Number of insured persons: 1,455,000 | Coverage ratio: 95.39% | Coverage ratio: 5.44% |

*Source:* Own calculation based on SODRA data (http://atvira.sodra.lt/en-eur/) and Official Statistics Porta (https://osp.stat.gov.lt/en/pagrindiniai-salies-rodikliai), 2022.

The overall coverage of Pillar II, measured as a ratio between the number of participants and the economically active population (number of insured persons in Pillar I), was more than 95% in 2021, while Pillar III covered a little more than 5% of the economically active population. Thus, we can expect that future pension income stream will be influenced mostly by Pillar II pensions, while Pillar III will generate an insignificant part of individuals' income during retirement.

Regarding the income level, Lithuania´s citizens have experienced relatively high rates of income increase during the last 15 years (9.62% annually).

# Pension Savings: The Real Return

## 2022 Edition

## *Country Case: Poland*

## Streszczenie

Dodatkowy system emerytalny w Polsce, który został wprowadzony w 1999 roku, a następnie był kilkukrotnie reformowany (główne zmiany w 2004, 2012 oraz 2018 roku), składa się aktualnie z czterech elementów:

- pracowniczych programów emerytalnych (PPE),
- indywidualnych kont emerytalnych (IKE),
- indywidualnych kont zabezpieczenia emerytalnego (IKZE) oraz
- pracowniczych planów kapitałowych (PPK funkcjonujących od 1 lipca 2019 r.).

Poziom uczestnictwa w wymienionych grupowych i indywidualnych planach oszczędzania na starość (odpowiednio 3,82%, 4,75%, 2,76% i 15,18%) wskazuje, że bardzo nieliczna część Polaków zdecydowała się na oszczędzanie w oferowanych zinstytucjonalizowanych formach gromadzenia kapitału na starość.

PPE mogą być prowadzone w czterech formach: umowy z funduszem inwestycyjnym; umowy z zakładem ubezpieczeń na życie (grupowe ubezpieczenie na życie z ubezpieczeniowym funduszem kapitałowym); pracowniczego funduszu emerytalnego (PFE) lub zarzadzania zewnętrznego. Na koniec 2021 roku w PPE zgromadzono 18,929 mld zł (4,12 mld €).

PPK mogą być oferowane w formie funduszu inwestycyjnego, funduszu emerytalnego i ubezpieczeniowego funduszu kapitałowego (UFK). Ta forma dodatkowych planów emerytalnych została dopiero wprowadzona, tj. funkcjonuje od 1 lipca 2019 r. Aktywa PPK miały wartość 7,67 mld zł (1,67 mld €) na koniec 2021 roku.

IKE i IKZE mogą być oferowane w formie: ubezpieczenia na życie z ubezpieczeniowym funduszem kapitałowym; funduszu inwestycyjnego; rachunku papierów wartościowych w domu maklerskim; rachunku bankowego lub dobrowolnego funduszu emerytalnego (DFE). Aktywa zgromadzone na IKE i IKZE na koniec 2021 roku wyniosły odpowiednio 13,47 mld zł (2,9 mld €) oraz 5,98 mld zł (1,3 mld €).

Pracownicze programy emerytalne (PPE), pracownicze plany kapitałowe (PPK) i indywidualne konta emerytalne (IKE) funkcjonują w reżimie podatkowym TEE (podatek pobierany jest na

etapie opłacania składki), podczas gdy w IKZE podatek pobierany jest na etapie wypłaty środków (reżim EET).

W analizowanym okresie (2002-2021) pracownicze fundusze emerytalne (PFE) wypracowały dość wysokie stopy zwrotu sięgające 17,41% w skali roku. Straty pojawiły się jednak w latach 2008, 2011, 2015 i 2018 w czasie załamania na rynkach finansowych. Realne stopy zwrotu uwzględniające opłaty osiągnięte w 15 z 20 lat są pozytywne. Średnia realna stopa zwrotu za cały analizowany okres wyniosła 3,37%.

Dobrowolne fundusze emerytalne (DFE) osiągnęły natomiast nadzwyczajne wyniki inwestycyjne w początkowym okresie funkcjonowania, głównie z uwagi na hossę na rynku akcji w pierwszym roku ich działalności. W 2013 roku najlepsze DFE wygenerowały nominalny zysk przekraczający 50%. Wyniki te nie zostały jednak powtórzone w kolejnych latach. W 2014 roku część DFE wykazała straty, które jednak zostały pokryte przez zyski w kolejnych latach. Średnia realna stopa zwrotu z uwzględnieniem opłat za lata 2013-2021 wyniosła 3.72%.

## Summary

Starting in 1999, with significant changes introduced in 2004, 2012 and 2018, the Polish supplementary pension market consists of four different elements:

- employee (occupational) pension programmes (*pracownicze programy emerytalne*, PPE),
- individual retirement accounts (*indywidualne konta emerytalne*, IKE);
- individual retirement savings accounts (*indywidualne konta zabezpieczenia emerytalnego*, IKZE) and
- employee capital plans (*pracownicze plany kapitałowe*, PPK).

The coverage ratios (3.82%, 4.75%, 2.76% and 15.18% respectively), show that only a small part of Poles decided to secure their future in old age by joining the occupational pension plan or purchasing individual pension products.

PPE can be offered in four forms: a contract with an asset management company (investment fund); a contract with a life insurance company (group unit-linked life insurance); an employee pension fund run by the employer (*pracowniczy fundusz emerytalny*, PFE) or external management. PPE assets amounted to PLN 18.929 bln (€4.12 bln) at the end of 2021.

PPK can operate as investment funds, pension funds or a unit-linked life insurance. These plans have just started to collect money (introduced in July 2019). PPK assets amounted to PLN 7.67 bln (€1.67 bln) at the end of 2021.

IKE and IKZE can operate in the form of either: a unit-linked life insurance contract; an investment fund; an account in a brokerage house; a bank account (savings account) or a voluntary pension fund (*dobrowolny fundusz emerytalny*, DFE). The total amount of IKE assets

amounted to PLN 13.47 bln (€2.9 bln) and IKZE assets amounted to PLN 5.98 bln (€1.3 bln) at the end of 2021.

PPE, PPK and IKE operate in TEE tax regime while IKZE is run in EET one.

During the period of 2002-2021 employee pension funds (PFE) showed rather positive returns up to 17.41% annually. Negative results appeared only in the years 2008, 2011, 2015 and 2018 when equity markets dropped significantly. Positive after-charges real returns were observed in 15 of 20 years and the average return over the 20-year period is highly positive as well (3.37%).

Voluntary pensions funds (DFE) have obtained extraordinary investment results from their start in 2012. The first years of their operation coincided with the Polish financial market recovery and allowed funds to maximise rates of return from the equity portfolios. The best DFEs reported more than 50% nominal return in 2013. But such returns were impossible to achieve in next years. In 2014, some of DFE even experienced slightly negative returns that were covered by returns in the following years. The average real rate of return after charges in years 2013-2021 amounted to 3.72%.

## Introduction

The old-age pension system in Poland was introduced in 1999 as a multi-tier structure consisting with three main elements:

- Pillar I - a mandatory, Pay-as-You-Go (PAYG) system;
- Pillar II - a mandatory PAYG system with a partial opt-out for funded pension funds; and
- Pillar III - voluntary, occupational and individual pension plans.

Table PL 1. Multi-pillar pension system in Poland

| Pillar I | Pillar II | Pillar III |
|---|---|---|
| Mandatory | Mandatory[1] | Voluntary |
| PAYG | PAYG/Funded (opt-out) | Funded |
| NDC | NDC/DC (opt-out) | DC |
| Basic benefit | Basic benefit | Complementary benefit |
| Publicly managed: | Publicly/Privately managed: | Privately managed: |
| Social Insurance Institution (ZUS) | Social Insurance Institution (ZUS); in opt-out element: Open Pension Funds | Pension savings managed by different financial institutions, depending on the product form, organised by employer or individual |

*Source: own work*

| | Employee pension funds | | | Voluntary pension funds | | |
|---|---|---|---|---|---|---|
| Holding Period | Gross returns | Net Nominal Returns | Real Net Returns | Gross returns | Net Nominal Returns | Real Net Returns |
| 1-year | - | 4.26% | 3.55% | 12.14% | 8.69% | 0.63% |
| 3-years | - | 5.34% | 0.93% | 8.74% | 5.48% | 0.66% |
| 5-years | - | 4.55% | 2.37% | 4.80% | 1.87% | -1.45% |
| 7-year | - | 3.39% | 2.03% | 5.14% | 2.31% | 0.10% |
| 10-years | - | 4.57% | 2.02% | - | - | - |
| Since inception | - | 5.80% | 3.37% | 8.36% | 5.48% | 3.72% |

The first part of the system is contributory and is based on a Non-financial Defined Contribution (NDC) formula. The total pension contribution rate amounts to 19.52% of gross wage (Pillar I + Pillar II) and the premium is financed equally by employer and employee. Out of the total pension contribution rate, 12.22 p.p. are transferred to Pillar I (underwritten on individual accounts of the insured), and 7.3 p.p. to Pillar II. If a person has not opted out for open pension funds (OFE), the total of 7.3 p.p. is recorded on a sub-account administered by the Social Insurance Institution (NDC system). If he/she has opted out for the funded element (open pension funds, OFE), 4.38 p.p. are recorded on a sub-account and 2.92 p.p. are allocated to an account in a chosen open pension fund.[210]

Pillar I is managed by the Social Insurance Institution (ZUS), which records quotas of contributions paid for every member on individual insurance accounts. The accounts are indexed every year by the rate of inflation and by the real growth of the social insurance contribution base. The balance of the account (pension rights) is switched into pension benefits when an insured person retires.

[210] Two years after the change in 2014 that made OFE's voluntary the insured could again decide about opt-out. After 2016 "the transfer window" is open every four years.

# Pension Savings: The Real Return

## 2022 Edition

## *Country Case: Romania*

## Rezumat

Ţinând cont de proporţiile reduse de acoperire a forţei de muncă în sistemele de pensii private din Europa, România se distinge prin obligativitatea aderării la fondurile de pensii administrate privat. Această prevedere constituie, în principiu, un avantaj atât pentru individ, cât şi pentru sistemul public de pensii, reducând presiunea pe cel din urmă si crescând şansele de a genera un nivel adecvat al venitului după pensionare.

Concluziile Înaltului Forum privind Uniunea Pieţelor de Capital (High-Level Forum on the Capital Markets Union, 2020) subliniază necesitatea armonizării, la nivelul Uniunii Europene, a prevederilor privind aderarea automată, cu posibilitatea de retragere, a întregii forţe de muncă ocupate. În acest sens, Romania se află pe traiectoria potrivită pentru consolidarea unui sistem de pensii durabil. Mai mult, fondurile de pensii din pilonul II cad sub incidenţa unei obligaţii de a obţine un randament minim. Din nefericire, acest randament minim este calculat în termeni nominali, nu reali, ceea ce în perioade cu rate foarte înalte ale inflației, cum este și cea din prezent, pot afecta foarte serios participanții în sistemele de pensii administrate privat.

Fondurile de pensii din România au înregistrat randamente nominale nete pozitive in ultimii 15 ani: media anuala pentru pilonul II a fost de 5.38% (calculat in €, cumulat 208%) iar pentru pilonul III 2.63% (calculat in €, cumulat 147%). Însă, după ajustarea la nivelul inflaţiei, fondurile pensii administrate privat au obţinut, în medie, 2.04% (calculat în €, cumulat 132%) iar fondurile facultative -1% (calculat în €, cumulat -14%). Trebuie totuși menționat că aceste rezultate nete pozitive au fost influențate favorabil de faptul că, în momentul crizei financiare din 2008, fondurile de pensii din România erau la început, astfel încât corecțiile majore ale piețelor le-au afectat într-o foarte mică măsură.

Compunerea portofoliilor ambelor tipuri de scheme administrate privat rămâne foarte similară şi, prin urmare, generează randamente brute similare. Cu toate acestea, randamentul net al Pilonului III este influenţat în mod semnificativ de structura costurilor substanţial mai mari (aproape de 4 ori mai mari) şi, astfel, pe termen lung, va genera randamente mai mici decât cele aferente Pilonului II.

Asociaţia Utilizatorilor Români de Servicii Financiare (AURSF), membră BETTER FINANCE, a atras în permanenţă atenţia asupra costurilor mari de administrare și, în special asupra comisionării ex-ante a contribuțiilor virate în conturile participanților. În plus, AURSF a criticat vehement și a contestat, inclusiv în Parlament, decizia autorităţilor de a reduce contribuţiile

virate în contul participanţilor de la 5,1% la 3,75%, care a reprezentat o deturnare inabil mascată a 0,5% din venitul brut al acestora dinspre contul personal de la pilonul II către pilonul I. De asemenea, AURSF a inițiat schimbarea legislativă prin care s-a încurajat opţiunea asumată a participanţilor pentru unul dintre fondurile administrate privat, urmând să monitorizeze dacă obligativitatea de informare impusa angajatorilor începând cu data de 19 iulie 2021 va produce efectele scontate, în sensul diminuării numărului de participanți distribuiți aleatoriu. De asemenea, AURSF a pus în discuție în cadrul Grupului de Dialog Permanent pentru Protecția Consumatorilor organizat la nivelul Autorității de Supraveghere Financiară (ASF) problema afectării grave a randamentelor obținute de fondurile de pensii adminístrate privat, în contextul creșterii ratei inflației și a ratelor de dobânzi, care au afectat negativ randamentele titlurilor de stat, principalul activ deținut de fondurile de pensii adminístrate privat. În plus, AURSF a solicitat explicații și în legatură cu achiziționarea de către fondurile de pensii adminístrate privat a unor obligațiuni ale unei bănci cu capital rusesc.

Eforturile Autorităţii de Supraveghere Financiară (ASF) privind transparenţa vehiculelor de pensii private aflate sub jurisdicţia sa merită o menţiune specială. Coordonatorii acestui raport subliniază că, în general, obţinerea datelor statistice necesare analizelor noastre devine din ce în ce mai grea: randamentele (dacă) sunt publicate cu multă întârziere şi după deducerea costurilor (ceea ce face dificilă raportarea randamentelor brute), iar alte cifre cheie (număr de participanţi, alocarea capitalului, valoarea activelor sub gestiune) sunt fie indisponibile, fie extrase din surse variate.

În schimb, exact cum recomandăm şi altor autorităţi competente, pagina de internet "Date statistice fonduri de pensii" întreţinută de A.S.F. România actualizează, lunar, 89 de tabele privind fondurile de pensii din pilonul II şi pilonul III.

Felicităm A.S.F. România pentru acest demers şi recomandăm ferm completarea tabelelor 5.1 si 4.1 cu randamentele nete ajustate cu indicele inflaţiei (indicele lunar armonizat al preţurilor de consum, publicat de Eurostat).

## Summary

Considering the reduced coverage ratios of the occupied labour force in European private pension schemes, Romania stands out for its mandatory enrolment to privately managed pension funds (Pillar II, occupational). This provision gives an advantage both for the individual and for the public pension system as it reduces pressure on the latter and elevates the chances to achieve pension adequacy.

The High-Level Forum on the Capital Markets Union (2020) concluded the need to harmonise, at EU level, regulations on auto-enrolment, with the choice of withdrawal, of the entire occupied labour force. In this regard, Romania is on the right path to consolidate a sustainable pension system. Moreover, occupational pension funds are required to deliver a minimum return. Unfortunately, this return is calculated in nominal, not real terms, which can

significantly affect privately managed pension fund participants in times of spiralling inflation, as is currently the case.

Romanian pension funds reported positive nominal returns over the past 15 years: the annual average for Pillar II was 5.38% (computed in €, compounded 208%) and for Pillar III 2.63% (computed in €, compounded 147%). However, after adjusting for inflation, privately managed funds returned, on average, 2.04% (computed in €, compounded 132%) and voluntary funds -1% (computed in €, compounded -14%). It is worth mentioning that these performances were positively influence by the fact that, during the 2008 global crisis, the funds were at its inception, thus the impact of market corrections was minimal.

The portfolios of both schemes are very similar and, thus, generate similar gross returns. However, Pillar III returns are heavily influenced by the significantly higher costs (almost four times higher) and, as such, on the long-term it will generate lower returns than Pillar II funds.

The Romanian Financial Services Users' Association (AURSF), member of BETTER FINANCE, has constantly drawn attention to the high administrative costs and, in particular, to applying ex-ante commissions on pension fund participants' contributions to their individual accounts. Moreover, AURSF has firmly criticized, including before the Romanian Parliament, public authorities' decision to reduce the contribution rate from 5.1% to 3.75%, which represented an unsuccessfully masked misappropriation of their gross income from the personal account to Pillar I. In addition, AURSF initiated the legislative reform incentivizing the active choice of participants for one of the privately managed pension funds, which will be subject to monitoring if employers' duty to inform as of 19 July 2021 will reach the aim of reducing the number of default assigned participants. AURSF also tabled the issue of pension funds' performances in times of rising inflation and interest rates, which affected the yield of sovereign instruments, the main asset in pension funds' portfolios. Last, AURSF demanded justifications as to the acquisition of bonds issued by a Russian-capital bank.

The Romanian Financial Supervisory Authority's efforts towards the transparency of private pension vehicles under its jurisdiction deserve a special mention. This report's coordinators highlight that, in general, it's becoming more and more difficult to obtain the necessary statistical data for our analyses: (where applicable) returns are published late and after deducting costs and charges (making it difficult to compute gross returns), and other key figures (number of participants, asset allocation, assets under management) are either unavailable, or aggregated from other various sources.

In contrast, as we have been recommending to other competent authorities as well, the webpage "Date statistice fonduri de pensii" (available only in Romanian) updates, on a monthly basis, 89 tables on Pillar II and Pillar III pension funds.

We congratulate the Romanian FSA for this endeavour and firmly recommend adding to tables 5.1 and 4.1 inflation-adjusted net returns (using the monthly harmonised index of consumer prices, published by Eurostat).

| | | |
|---|---|---|
| Average old-age pension: €336.6 | Custodians: 3 | Custodians: 3 |
| Average salary (gross): €1278.4 | Brokers: 14 | Brokers: 21 |
| Net replacement ratio (state pension): 26.3% | AuM: €18 bln. (89.1 bln. RON) | AuM: €0.69 bln. (3.41 bln RON) |
| | Participants: 7.79 mil. | Participants: 0.56 mil. |
| Average aggregate pension replacement ratio: 38% (2021 – Eurostat) | | |

*Source: Own elaboration based on CNPP, ASF and INSSE data, 2022; Notes: Exchange rate RON/EUR = 4.949; data on average old-age pension and gross salary and data on the number of old-age pensioner are calculated as an average for the year 2021; data on number of participants and assets under management as of December 2021*

The overall coverage of Pillar II, measured as a ratio between the number of participants and the economically active population, was almost entire working population in 2019, while Pillar III covered only 6% of the economically active population. Thus, we can expect than future pension income stream will be influenced mostly by Pillar II pensions, while Pillar III will generate an insignificant part of individuals income during retirement.

**Summary Return Table**

| | Pillar II | | Pillar III | |
|---|---|---|---|---|
| **Holding Period** | Nominal | Real | Nominal | Real |
| 1 year | 4.12% | -2.58% | 3.63% | -3.07% |
| 3 years | 5.84% | 1.64% | 4.80% | 0.6% |
| 7 years | 3.73% | 1.23% | 2.71% | 0.22% |
| 10 years | 5.28% | 2.83% | 4.35% | 1.90% |
| Since inception | 5.38% | 1.91% | 2.63% | -1.00% |

Source: BETTER FINANCE own composition, 2022

# Pension Savings: The Real Return

## 2022 Edition

## *Country Case: Slovakia*


### Zhrnutie

Slovenský dôchodkový systém je typickým modelom Svetovej banky založenom na viac-pilierovom (troj-pilierovom) systéme s individuálnymi (osobnými) účtami sporiteľov. V roku 2019 došlo výrazným zmenám v I. pilieri, ktoré boli motivované politickým populizmom pred voľbami. Do dôchodkového systému bol ústavným zákonom zapracovaný dvojpilierový systém a zároveň strop dôchodkového veku. V roku 2021 boli očakávané výrazné reformné zmeny v I. pilieri, ktoré by mali zvýšiť finančnú stabilitu I. piliera a vyriešiť problémy v nastavení súkromných dôchodkových schém. V roku 2021 tak boli v kontexte reformných snáh ohlásené zmeny v II. pilieri cielené za zavedenie predvolenej investičnej stratégie a reformné snahy o zvýšenie konkurencie v schémach dobrovoľného doplnkového dôchodkového sporenia, ktoré však zastali a zaviedol sa výlučne zákon o celoeurópskom osobnom dôchodkovom produkte.

### Summary

The Slovak pension system is a typical World Bank model based on a multi-pillar (three-pillar) system with individual (personal) accounts of savers. In 2019, there were significant changes in Pillar I, which were motivated by political populism before the elections. The two-pillar system was incorporated into the pension system by a constitutional law, as well as a ceiling on the retirement age. Significant reform changes to Pillar I were expected in 2021, which should increase the financial stability of Pillar I and resolve problems in the set-up of private pension schemes. Thus, in 2021, in the context of reform efforts, changes in Pillar II were announced targeting the introduction of a default investment strategy and reform efforts to increase competition in voluntary supplementary pension saving schemes, but these stalled and only a law on a pan-European personal pension product was introduced.


### Introduction

The Slovak old-age pension system is based on the multi-pillar approach, which consists of three main pillars:

- Pillar I – State pension organized as a mandatory Pay-As-You-Go (PAYG) scheme;
- Pillar II – Funded pension organized as voluntary funded DC based scheme; and

- Pillar III – Supplementary pension organized as a voluntary individual pension DC based scheme.

The Slovakian pension reform started in 1996 with the introduction of Pillar III, which at that time (and until 2009) was organized as voluntary pension pillar offering life insurance contracts and as an occupational pillar as well. Since July 2009, the system was changed to funded saving schemes and voluntary Pillar III pension funds are offered to the savers (members). The organization of Pillar III started to become more personal with the financial support of employers.

The World Bank's approach has been fully implemented by introducing Pillar II at the beginning of 2005, and, from a terminological point of view, it should be called the "1bis pillar", as individual retirement accounts are funded via partial redirection of social security contributions on individual pension savings accounts.

For a person who works a full career (42 years) and retires in 2021, the main income stream derives from the PAYG (Pillar I) pension scheme. On average, the individual replacement ratio of such a person could reach 50% of his gross salary. If the person would have participated since 1996 in Pillar III and contributed on average 3% of his salary into a Pillar III pension scheme, having also entered Pillar II (1bis pillar) in 2005, his income stream during retirement would have been slightly different and his replacement ratio would have been a little higher than 50%. However, still more than 90% of the retirement income stream is provided via the PAYG scheme (Pillar I), around 5% from Pillar II (1bis pillar) and 5% from Pillar III.

| Introductory Table - SK Pension System Overview | | |
|---|---|---|
| **Pillar I** | **Pillar II** | **Pillar III** |
| State pension (almost 100% coverage) - Mandatory (PAYG) | Occupational pensions - Mandatory DC (funded schemes) - coverage 68% | Individual pensions - Voluntary fully funded DC - coverage 28% |
| Managed by the Social Insurance Company | Managed by Pension Asset Management Companies | |
| Contribution rate: 14.00% (employer) and 4% (employee); Gross replacement rate: 41.8%; Average pension: € 506 | Contribution rate: 4.25%; 17 pension funds offered | 19 funds offered |
| **Quick facts** | | |
| Retirement age – 62 years and 10 months | | |
| A relatively high old-age dependency ratio of 24.95% in 2021 | | |
| Aggregate replacement ratio for pensions (excl. social benefits) in 2021 of 49.3% | | |

Sources: Social Insurance Company, 2022 (https://www.socpoist.sk/646/1614s); Eurostat, 2022 (online data code: tespn070)

# Pension Savings: The Real Return

## 2022 Edition

## *Country Case: Spain*

## Resumen

Los trabajadores españoles no ahorran para su pensión. Más del 70% de sus activos totales son “ladrillos y cemento”, que de ninguna manera puede considerarse un “activo previsional”. Cuando las pensiones de Seguridad Social sustituyen más del 80% del salario previo a la jubilación, ¿por qué los trabajadores deberían ahorrar para ello? Como resultado de estos y otros factores, la “industria de las pensiones” (Pilares II y III) en España es pequeña y menos eficiente que si fuese tan grande como las de Holanda, Dinamarca o el Reino Unido. Los activos previsionales de los Planes de Pensiones a 31 de diciembre de 2021 llegaban al 10,55% del PIB de ese año, y las reservas técnicas de una amplia gama de productos asegurados para la jubilación (o similares) alcanzaban otro 15,82% del PIB, en total un 26,37% del PIB. Por estas razones, la gestión de estos activos no es barata, aunque puede llegar a serlo, y mucho, en los esquemas del Pilar II. La Fiscalidad de los activos y rentas de ambos pilares en España responde al régimen EET, común en la mayor parte de los países de la OCDE, si bien en los últimos dos años se ha deteriorado considerablemente para los vehículos del Pilar III. El rendimiento acumulativo medio general de los esquemas del sistema de Planes de Pensiones, una vez descontada la inflación, y antes de impuestos (marginal del IRPF, en este caso) ha sido del 0,58% por año en el periodo 2000-2021. Todos los datos utilizados en este capítulo provienen de fuentes oficiales fácilmente accesibles en internet (INVERCO, DGSFP, INE y Banco de España).

## Summary

Spanish workers don't save for their retirement. “Bricks & Mortar” make more than 70% of a typical Spanish household’s portfolio. And there is no way to think of this asset as retirement savings. As Social Security old-age benefits replace more than 80% of lost labour income at retirement, why Spanish employees should save with this purpose? As a result, Spanish Pensions Industry (Pillars II and III) is small and less efficient as that of Denmark, Netherlands or the UK. Pension Funds’ assets at end 2021 reached 10.55 percentage points of GDP that year, and if insured retirement or retirement-like vehicles’ mathematical reserves were added to this, an extra 15.82 percentage points could be found, adding to a grand total of 26.37% of GDP. These and other reasons imply that asset management in this low-scale industry cannot be cheap. To be sure, Pillar II assets are as cheap to manage as in advanced countries or more, but this is not the case with Pillar III assets. Taxation of retirement assets and income in Spain

responds to the EET regime, as in most OECD countries, although the last two years have witnessed a deterioration of fiscal terms grants to Pillar III schemes. Average cumulative net real return since 2000 through 2021, in the standard Pension Plans system, once inflation adjusted, and before taxes (the marginal Personal Income Tax in this case), has been just 0.58% annually. All data used in this chapter can be found on readily available official sources' web sites (INVERCO, DGSFP, INE and Bank of Spain).

## Introduction

The Spanish pension system is composed of three pillars:

- Pillar I – Public, with a pay-as-you-go major branch of compulsory, earnings related pensions (old-age, invalidity and survivors' benefits) and a minor, means-tested assistance branch for over 65 years old individuals (old-age and invalidity).

- Pillar II – Voluntary, defined benefit and defined contribution occupational, employer-sponsored pension plans (restricted de facto to large companies) and other qualified pension vehicles (insured and non-insured).

- Pillar III – Voluntary, individual defined contribution pension plans and a variety of other qualified retirement savings vehicles (insured and non-insured).

A more detailed structure of these three pillars is presented in the following table.

Security, as a matter of fact, has returned every euro paid in contributions around 12 years after retirement when the average retiree has yet another 10 years of remaining life.

This implicit return is difficult to beat by marketed retirement products, even if these are by default sustainable when they are of the DC variety.

This said, the summary table below tells a story that bears a sharp contrast with the above description of Social Security internal rate of return. Long term (since 2000) net (of fees), real (after inflation) and before taxes, returns of the standard retirement plans (Pillars II and III) in Spain has been 0.68% in annual cumulative terms (0.50% for Pillar III schemes and 0.96% for Pillar II schemes) and this thanks to the good performance of stock markets in 2019 and 2021 (overall 8.8% in 2019 and 8.5% in 2021).

| Aggregate summary return table | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | 1 year | | 3 years | | 7 years | | 10 years | | Since 2000 | |
| | 2021 | 2020 | 2019-2021 | 2018-2020 | 2015-2021 | 2014-2020 | 2012-2021 | 2011-2020 | 2000-2021 | 2000-2020 |
| PILLAR II | | | | | | | | | | |
| Nominal return | 8.09% | 1.53% | 4.93% | 3.32% | 4.38% | 4.33% | 4.62% | 4.02% | 3.18% | 2.94% |
| Real return | 1.52% | 2.10% | 2.25% | 2.40% | 3.02% | 3.86% | 2.56% | 2.86% | 0.89% | 0.86% |
| PILLAR III | | | | | | | | | | |
| Nominal return | 8.67% | 0.29% | 4.24% | 2.25% | 3.55% | 3.55% | 3.78% | 2.77% | 2.71% | 2.42% |
| Real return | 2.10% | 0.86% | 1.58% | 1.33% | 2.20% | 3.08% | 2.26% | 1.60% | 0.43% | 0.35% |
| Both Pillars | | | | | | | | | | |
| Nominal return | 8.50% | 0.67% | 1.80% | 0.79% | 3.83% | 3.81% | 4.07% | 3.22% | 2.89% | 2.62% |
| Real return | 1.93% | 1.24% | 1.80% | -0.5% | 2.48% | 3.34% | 2.56% | 2.05% | 0.61% | 0.54% |

Source: own composition based on INVERCO data

## Pillar I

The National Institute for Social Security (INSS, Spanish acronym) is the national agency for pensions run by the central government. The Spanish Social Security covers all workers against old-age, invalidity, and survivorship (widowhood and orphanhood). It has two separate branches: an insurance, contributory and earnings-related branch and a non-contributory, assistance, flat means-tested benefits branch, sharply differentiated not only by law but also by its size, nature, and functions.

The insurance branch of Social Security is, by far, the dominant scheme in the Spanish pension's arena (all public and private vehicles considered). It is contributory, compulsive for all workers, either employees or self-employed workers, and firms and is financed through social contributions that, within each current year, are used to pay for current pensions. The financial method of the system is thus of the Pay-As-You-Go variety. The pension formula is of

# Pension Savings: The Real Return

## 2022 Edition

## *Country Case: Sweden*

## Swedish summary

Det svenska pensionssytemet består till stor del av avgiftsbestämda/fonderade pensioner. Totalt förvaltas över 7300 miljarder SEK (€726 miljarder) i pensionskapital. I det allmänna pensionssystemet sätts 2.5% av lönen av till den så kallade premiepensionen. I premiepensionen har förvalsalternativet, AP7 Såfa, haft en genomsnittlig realavkastning på 7.78% sedan 2001, jämfört med 4.95% för alla andra valbara fonder. Tjänstepensionssystemet domineras av fyra stora avtal som täcker över 90% av alla arbetstagare. Tjänstepensionerna har till största del gått från att vara PAYG till fonderade pensionssystem.

## Summary

The Swedish pension system contains a great variety of different retirement savings products with over SEK 7,300 trillion (€726 billion) in assets under management (AuM). There are funded components in each of the three pillars. In the public pension system, 2.5% of earnings are allocated to the *premium pension*, whereas the default fund, AP7 Såfa, has had an average real rate of return of 7.78% compared to the 4.95% of all other funds over the last 19 years. The second pillar is dominated by four large agreement-based pension plans, covering more than 90% of the workforce. These have largely transitioned from a pay-as-you-go (PAYG) system to a funded system.

## Introduction

The Swedish pension system is divided into three pillars:

- Pillar 1 - The national pension
- Pillar 2 - Occupational pension plans
- Pillar 3 - Private pension

The Swedish pension system is a combination of mandatory and voluntary components. Table 1 shows how the pension capital is distributed between the different types of providers in the pension system. In 2020, the total pension capital was estimated at SEK 7,300 billion (€726 billion), which corresponds to fourteen times the size of outgoing pension payments. A share of 50% of the capital is accounted for by the occupational pension system. The fully funded component in the public pension system, the *premium pension*, accounts for 49% of the pension capital in the first pillar. The remaining 51% is managed by the buffer funds (see next section).

| Introductory table: Pension system in Sweden | | |
|---|---|---|
| **Pillar I** | **Pillar II** | **Pillar III** |
| Mandatory | Mandatory* | Voluntary |
| PAYG/funded | Funded | Funded |
| DC/NDC | DC/DB** | DC |
| Flexible retirement age 62-68 | ERA of 55 or 62, usually paid out at 65 or 67 | Tax rebate abolished in 2016*** |
| No earnings test | Normally a restriction on working hours | |
| Mandatory | Mandatory* | Voluntary |
| **Quick facts** | | |
| Number of old-age pensioners: 2,3 million | Coverage: >90% | Share contributing (2015): 24,2% |
| Coverage (active population): Universal | Pension plans: 4 major (agreement-based) | Funds: >30 |
| Average monthly pension: 1793 EUR | Average monthly pension: 488 EUR | Average monthly pension: 90 EUR |
| Average monthly salary (gross, age 60-64): 3,100 EUR | AuM: 364 billion EUR (see Table SE 1) | AuM: 34 billion EUR (see Table SE 1) |

Average replacement rate: 58%****

** Occupational pension coverage is organized by the employer*
*** The defined benefit components are being phased out*
**** Self-employed and employees without occupational pension still eligible*
***** OECD estimate 54%*

| Summary returns table. Sweden nominal returns in 1st and 2nd pillar | | | | | | |
|---|---|---|---|---|---|---|
| | Public pension | | Occupational pension* | | | |
| | AP7 Såfa | Other funds | ITP1 | SAF-LO | PA-16 | AKAP-KL |
| 2021 | 31,5 | 27,1 | 24,57 | 28,93 | 31,3889 | 27,47 |
| 2020 | 4,4 | 8 | 7,28 | 7,833 | 7,62222 | 7,729 |
| 2019 | 32,2 | 27,6 | 23,99 | 26,64 | 27,3667 | 26,98 |

* For each occupational pension plan, the return is an unweighted average among the available funds.
Source: Tables SE11 and SE14

# Pension Savings: The Real Return

## 2022 Edition

## *Country Case: The Netherlands*

## Samenvating

In veel opzichten bevinden de Nederlanders zich in een benijdenswaardige positie wat hun pensioenen betreft. Het Nederlandse pensioenstelsel staat, naast het Deense en het IJslandse, voor het vierde jaar op rij bovenaan in de Mercer CFA Institute Global Pensions Index als een A-klasse stelsel, wat betekent "*een eersteklas en robuust pensioeninkomensstelsel dat goede uitkeringen biedt, duurzaam is en een hoog niveau van integriteit heeft*". De tweede en derde grootste pensioenfondsen (naar beheerd vermogen) in "*Europe's top 1000 pension funds*" zijn het ABP en PFZW, alleen het Pensioenfonds van de Noorse regering staat op de tweede plaats. De Nederlandse bedrijfspensioenfondsen komen in ons rapport ook op de tweede plaats wat betreft reële nettorendementen, na het Zweedse premiepensioenstelsel. Maar terwijl het particuliere pensioenstelsel in Nederland beter presteert met zijn fondsen, blijven de verzekeringen achter: de sector is bijna tien keer kleiner in termen van activa (24% van het bbp tegen 239%) en de vergelijking van het reële nettorendement over 22 jaar tussen bedrijfspensioenfondsen en levensverzekeringen van pijler III spreekt voor zich: 2,80% tegen 0,02%. Het vertrouwen van Nederlandse werknemers in de toereikendheid van hun pensioen is de afgelopen 10 jaar echter gedaald van 75% (het vertrouwen dat hun pensioen voldoende zal zijn om hun levensstijl bij pensionering voort te zetten) naar 66%. Het Nederlandse stelsel maakt een belangrijk moment door, aangezien de wet inzake de overgang van toegezegd-pensioenregelingen (DB) naar collectieve toegezegde-bijdrageregelingen (CDC) momenteel in behandeling is.

De lage rente (tot juli 2022) maakte het voor pensioenfondsen moeilijk om hun dekkingsgraad boven de vereiste quota te houden, een situatie die veranderde door de verschuiving in het monetaire beleid in de eurozone.

In dit rapport geven we een schets van het Nederlandse pensioenstelsel, kijken we naar de jaarlijkse beleggingsrendementen van pensioenfondsen en berekenen we het reële rendement, waarbij we het nominale rendement corrigeren voor diverse lasten, belastingen en inflatie. Daarnaast heeft het onderzoeksteam de openbaarmaking van duurzaamheidsinformatie van de vijf grootste bedrijfspensioenfondsen in Nederland geanalyseerd. In de eerste paragraaf wordt dit laatste onderwerp behandeld, waarna de traditionele Nederlandse landencasus wordt gepresenteerd.

## Summary

In many ways, the Dutch are in an enviable position as far as their pensions are concerned. The Dutch pension system, next to the Danish and Icelandic ones, ranked for the fourth year in a row highest in the Mercer CFA Institute Global Pensions Index[268] as an A-grade system, meaning "*a first class and robust retirement income system that delivers good benefits, is sustainable and has a high level of integrity*". The second and third largest pension funds (by assets under management) in "Europe's top 1000 pension funds" are the ABP and PFZW, only outranked by the Norwegian Government's Pension Fund.[269] Dutch occupational pension funds also rank second best in our report in terms of real net returns, after the Swedish premium pension system. Nevertheless, while the private retirement system in the Netherlands outperforms with its funds, insurances lag behind: the sector is almost 10 times smaller in terms of assets (24% of GDP compared to 239%) and the 22-year real net return comparison between occupational pension funds and pillar III life insurances speaks for itself: 2.80% vs 0.02%. However, Dutch workers' trust in the adequacy of their pensions has been decreasing from 75% (trusting that their pension will be sufficient to continue their lifestyle at retirement) to 66% in the last 10 years.[270] The Dutch system is passing through a key moment as the law on the transition from defined-benefit (DB) to collective defined-contribution (CDC) plans is currently work in progress.

Low interest rates (until July 2022) made it difficult for pension funds to maintain their funding ratios above the required quota, situation which changed with the shift in monetary policy in the Eurozone.

In this report we will provide an outline of the Dutch pension system, take a look at the annual returns on investment of pension funds and calculate the real return, adjusting the nominal return for various charges, taxes and inflation. In addition, the research team also analysed the sustainability information disclosure from the top five occupational pension funds in the Netherlands. The first section addresses the latter topic and afterwards the traditional Dutch country case is presented.

[268] Mercer CFA Global Pensions Index, 2021, available on p.5 at: https://www.mercer.com/content/dam/mercer/attachments/private/gl-2021-global-pension-index-mercer.pdf
[269] Investment & Pensions Europe, *2022 European Pensions Guide* (Supplement to the September 2022 issue of Investment & Pensions Europe magazine), p. 11.
[270] Frank van Alphen, 'Dutch Workers Expect Lower Pensions in DC System' (IPE.com, 29 June 2021), accessed 7 October 2021, available at: https://www.ipe.com/news/dutch-workers-expect-lower-pensions-in-dc-system/10053757.article.

associations that cover more than half of the sector have agreed a specific sector-wide scheme with relevant labour unions, which by law then become mandatory for the entire sector at hand. In practice this means that most sectors of the economy are covered by these (sector-specific) mandatory schemes;

- Pillar III – composed of pre- and post-retirement fully funded and completely defined-benefit (DB) pension saving products, for which participation is voluntary.

**Table NL1. The Dutch pension system**

| Pillar | Characteristics | Coverage | Replacement ratio |
|---|---|---|---|
| Pillar I | PAYG, DB, social insurance, taxed as income on pay out | 100% | According to Eurostat, 50% (2021)[276] |
| Pillar II | Funded by the employer and employee, (mostly) DB, investment plan, contributions tax exempted, return on investment tax exempted, pay-out taxed at progressive income tax rates, formed of: occupational pension funds (278, €2 trillion AuM,[277] % of total managed) and the premium pension institutions (€22 bln AuM,[278] 1.09% of total managed) | Approx. 75% coverage[279] | |
| Pillar III | Funded by individual, DC, contributions subject to a limit, contributions tax exempted, pay-out taxed at progressive income tax rates | n.a. | |

*Source: BETTER FINANCE own composition; OECD data*

**Summary Return Table - Pensions in the Netherlands**

| | 1 year | 3 years | 7 years | 10 years | whole reporting period |
|---|---|---|---|---|---|
| | 2021 | 2019-2021 | 2015-2021 | 2012-2021 | 2000-2021 |
| Pension funds | 0.85% | 6.58% | 3.94% | 5.00% | 2.80% |
| Life insurances | -2.29% | -0.04% | 1.19% | 0.33% | 0.02% |

*Source: own computations based on Table NL15*

## Pillar I

Pillar I is a social insurance scheme and consists of the Dutch state pension, called AOW (*Algemene Ouderdomswet* or General Old-Age Law). It provides a lifelong state pension for all

[276] Eurostat Aggregate Income Replacement Rate, Total, Netherlands, 2021.
[277] DNB Statistieken, Balans van Pensioenfondsen (Kwartaal; breukvrij), 2021Q4.
[278] DNB Statistieken, Balans Premiepensioeninstellingen, 2021Q4.
[279] Based on the data published by the Dutch Central Bank on the number of participants in Dutch pension funds (5,957,899, 2021) and in the premium pension institutions (1,189,929, 2021Q4), divided by the occupied force labour (World Bank Data, 2021, 9,897,689, minus 408,000 –unemployment rate).

# Imprint

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