

# FINANCIAL CRISIS AND THE PENSION SYSTEM

Prof. Gheorghe Matei Ph. D  
University of Craiova  
Faculty of Economics and Business Administration  
Craiova, Romania  
Daniela Pîrvu Ph. D Student  
University of Pitești  
Faculty of Economics  
Pitești, Romania

**Abstract:** Currently, public pension systems PAY-AS-YOU-GO (PAYG) from more countries in the world based solely on solidarity between generations are facing increasingly difficult problems to solve. Causes due to evolution. And demographic trends of aging while reducing the birth rate, increasing the average lifetime, inflation, growing costs in the period following the early post active retirement. Last but not least, reducing the dependency ratio, meaning the decrease number of taxpayers while increasing number of retirees.

**JEL classification:** E60, H55, I38

**Key words:** financial crisis, pension crisis, pension systems, pension system reform, demographic evolution

## 1. INTRODUCTION

All the problems of the pension systems were accentuated by the global financial crisis has become an important economic dimension and the influence of increasingly large social terms. in this context more and more organizations hospitalized! National and regional experts are concerned about its many social effects of global financial and economic crisis, especially over pensions. It is estimated that despite the severity of the financial crisis, its effects are minor compared to the effects caused by aging and population reduction; within the European Union, the demographic crisis could have an impact 10 times worse, as noted in The World Bank report "Pension Crisis" (Pensions in Crisis: Europe and Central Asia Regional Policy Note), published in the December 2009 and The European Union Report "The public pension system in Romania, threatened by the demographic evolution" (published in March 2009).

## 2. PENSION SYSTEM CRISIS

In the average rate conditions of dependency (ratio of population over 65 years with the population aged 15-64 years) in Europe will double by the year 2060 (Table no. 1) pressure on public pension systems will become unbearable.

**Table no. 1** Evolution of the number of pensioners in some European countries

Country	Number of pensionaries	Percent of the population	How the wealth will rise until 2040	Life expectancy (in years)
Germany	16,4 thousand	20,0%	Up to 33,0%	77 men / 82,2 women
France	12 thousand	21,0%	Up to 40,0%	77,5 men / 84,4 women
Italy	15,3 thousand	25,0%	Up to 32,6%	79 men / 84 women
Spain	8.6 thousand	18,4%	Up to 36,0%	79 men / 83 women
Great Britain	10 thousand	16,0%	Up to 25,0%	77,2 men / 81,5 women
Hungary	2,5 thousand	23,0%	Up to 30,0%	69,2 men / 77,4 women

*Source: The European Union Report "The public pension system in Romania, threatened by the demographic evolution", March 2009*

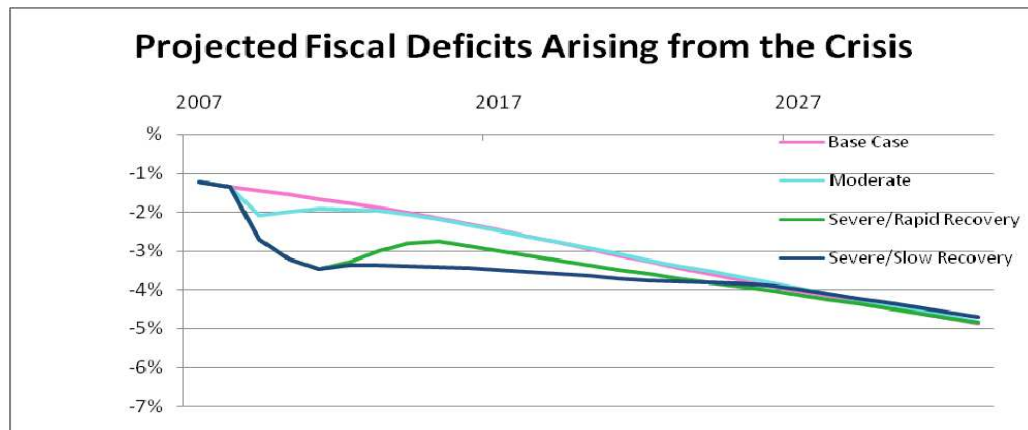
In Romania, the great advantage recorded after 1990 due to aggressive demographic policy promoted by the old regime, there was a large number of taxpayers who support public pension system. This is only temporary advantage against a negative natural increase of population, work in conjunction with migrations forged in different countries, especially Western, and even early retirement age onwards the age of 50 years a large number of people active economic restructuring and institutionalization fund or medical reasons. If in 1990 more than three employees sustained a pensioner, when there were 2.6 millions retired in 2001 included the number of pensioners that reached 4.5 million in 2009 and has 5.5 million, of which about 900 000 are retired on medical grounds. It is estimated that approximately 25% of pensioners in medical cases are incorrectly classified in a degree of disability. Relationship between employees and pensioners has today reached a nearly one (0.98 employees / 1 retired). If current conditions persist retirement in 2050 half of Romania's active population will be retired. Aggressive population policy in the late 60s of the twentieth century only delayed the aging process and saved temporary pension. After 2030, when those born at the time they reach retirement age, the pension system will collapse because of low labor input together with massive inflows of pensioners, which will contribute to the degradation rate of dependence.

Public pension systems in countries of the world are very diverse in terms of shape and size. However, no pension, was structured as well, not proved immune to the economic and financial crisis. In this context, some governments have tended to operate some changes in the policy area in response to growing deficits higher pension budgets, while other reforms have stalled, delayed or postponed them, preferring to borrow to maintain existing public pension systems.

As shown Anita Schwarz, author of World Bank Report "financial crisis affects every part of the pension system differently, and although the magnitude and distribution in time may be different, each component is adversely affected. Sudden decreases in the efficiency and reduce the overall tax base have reduced the public funds available for pension and unemployment at the same time, growing, low pensions and the depreciation

of financial assets are adversely affected systems and funded by contributions from employers to employees.

It was found that in countries where fiscal balances were affected by the pension schemes were taken to change social policies aimed at promoting, on the one hand, increasing resources and, secondly, to reduce costs. If they concern only short term benefits in the future is likely to generate additional costs because according to World Bank simulations, even her most. scenario yields severe financial crisis "before the crisis in view of demographic aging. deficits of pension schemes in the future on three levels to show what is currently registered and is estimated to remain at this level for another 20 years, before improving slightly (see Figure no. 1).



Source: The World Bank report "Pension Crisis" (*Pensions in Crisis: Europe and Central Asia Regional Policy Note*), December 2009, page 6

**Figure no. 1 Projected fiscal deficits of public pension systems due to global crisis**

In Romania in 2009 the public pension system has a deficit of 1.5 million Euros, ie 20% of its revenue, while the average pension increased by 5% but not to an improving standard of living for pensioners but is merely an anti-inflation measure. Even if the public pension system operates well above its real possibilities, it fails to provide decent pensions for most of the pensioners who have worked and contributed to achieving and exceeding the complete contribution.

Policymakers should seize the current crisis to address long-term problems that could lead to bankruptcy of pension systems while the number of pension recipients is steadily increasing.

### 3. PENSION REFORM

Public pension reform is not possible after a single prescription in all states, but must take into account the specificities of each country taking into account a combination of long-term. Many of the recommendations made by experts of international institutions for long-term pension reform can be taken into account in Romania in this respect we consider:

a) public pension system:

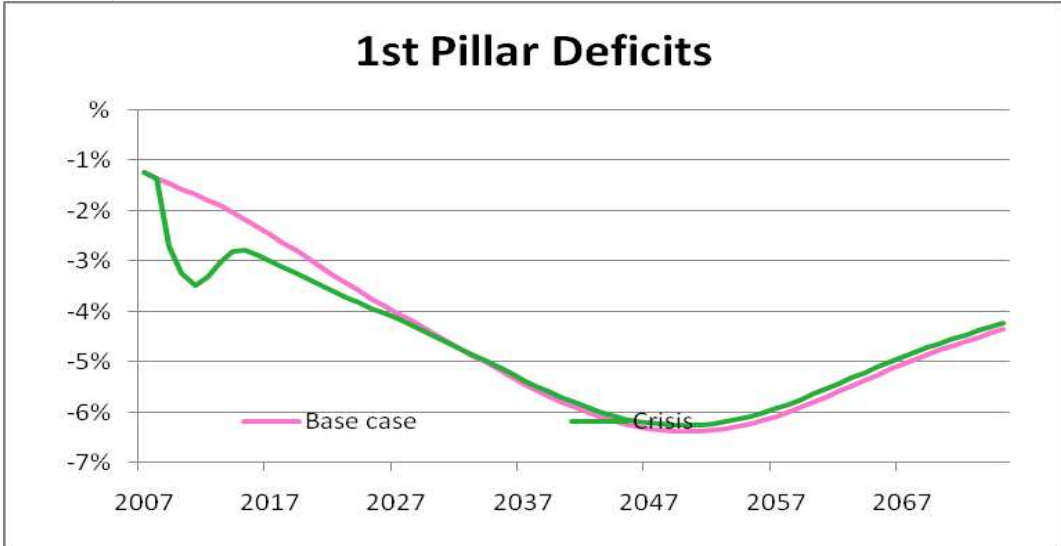
- Raising the retirement age and its equalizing men and women. Reform since 2000 gradually increased the retirement age to 57 for women and for men 62 to 60 years for women and 65 men. In some Western European countries the retirement age exceeded

65 years: Iceland and Norway, the standard retirement age is 67 years and above who receive a supplementary pension bonus up to 70 years in Denmark, Netherlands and Germany the retirement age is 67 for men and 65 women (Germany aimed at retirement age to 70 years for men and 67 women) in Britain has passed the age of retirement at 68 years, until 2045, by increasing your retirement age men and women each year in Italy was provided equalize retirement ages for men and women by the year 2018 by increasing the retirement age of women working in welfare payments public from 60 to 65 years;

However, there is an opinion that the life expectancy statistics and other physical and mental ability of a man 70 years or a woman of 67 years. The question arises whether a person reached the age may work quantity and quality as a person takes 55-60 years. With age, obsolescence increases and decreases an individual's ability to work in line with a younger person will have problems of efficiency could influence the activity of an entire company. In the same time, even if the old staff has the advantage of experience, there is no guarantee that can quickly accumulate information and technologies, market, as a younger person. Raising the retirement age might give me a lower quality of life in general, and increased social spending, take account of actual demand for labor, health condition or older if they are motivated to work.

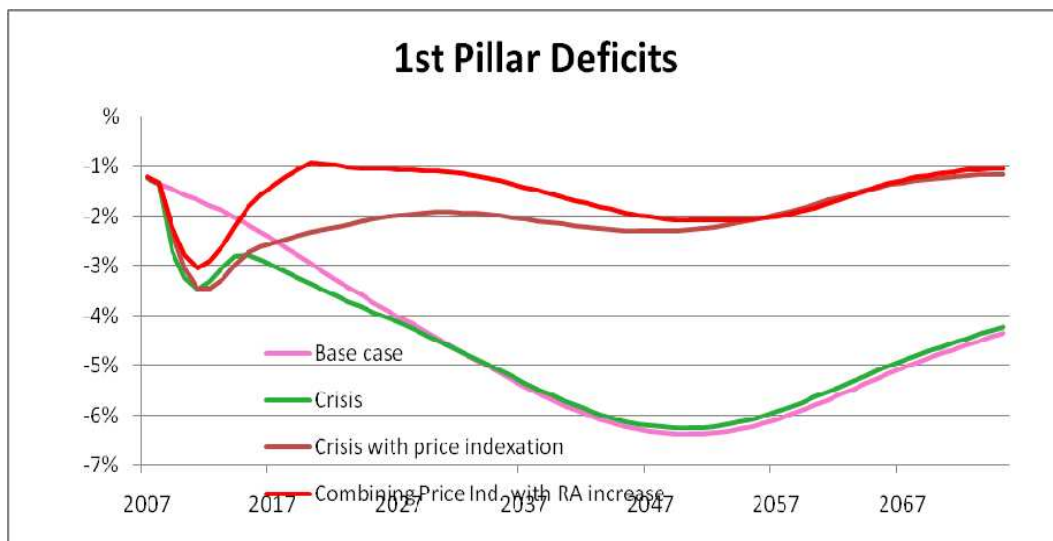
- Early retirement penalty. Many European countries, including Romania, have at one time based employment policy on the idea that early retirement would create preconditions youth labor market entry. In fact, early retirement and more secured pension systems and countries like Finland and Britain have realized that such a policy leads to increased taxation of labor and creates distortions in the economy. In Slovenia, early retirement pension is reduced with 0.5% reduction determined by every month of anticipation. In Romania, for its word partial early retirement is reduced compared with the period of contribution made and the number of months that has reduced the retirement age;

- Only switch to inflation indexation of pensions in payment and giving up other more generous indexation, wage developments related to the economy. According to The World Bank estimations, the public pension system deficits are to evolve (see figure no. 2 and no.3 ):



Source: The World Bank report "Pension Crisis" (Pensions in Crisis: Europe and Central Asia Regional Policy Note), December 2009, page 13

Figure no.2 Development of pension deficits in the next 60 years



Source: The World Bank report "Pension Crisis" (*Pensions in Crisis: Europe and Central Asia Regional Policy Note*), December 2009, page 15

**Figure no. 3 Deficits estimated in terms of indexation of pensions by inflation and increasing age of retirement**

- Awareness through information campaigns among the public that pension payments are to be less generous than in the past, if you want one of their sustainability.

b) Private pension systems:

- Adoption of means to mitigate financial market volatility on pension funds by adopting multifond model type or providing security for the entire period of accumulation efficiency (existing safeguards for those enrolled in the mandatory private pension funds in Romania);

- Accelerate the legislative and supervisory reforms to allow private pension funds to achieve returns as high for participants.

If the public pension contributions are not active savings to invest, but are spent immediately to pay pensions in the current period in Pillar II (privately managed public pensions) and third pillar (private pensions in full) system has proven viability and product performance for participants. Average yield of private pension funds, mandatory and optional in Romania in 2009 by 15-16%. However, in countries such as Romania, Estonia, Latvia and Lithuania, the authorities have reduced contributions to pension pillar (where Romania has been delayed already scheduled to increase 0.5% annually). This temporary measure has a short term, increase government revenue, but long-term policyholders will collect less money in their private pension accounts and therefore will have lower pensions. Since they have contributed more to the public system during this period, it should compensate the reduction rate of contribution. The impact of this compromise on short and long term depends on many factors, and overall it is impossible to favor both the government and policyholders;

- Proactive development of financial markets by the authorities by issuing variable-yield bonds in inflation.

#### 4. CONCLUSIONS

In the current economic and financial crisis, public pension systems around the world have been more affected than private schemes. As a result, global, state pensions shown much less sustainable than systems based on capitalization and private management, the conclusion should stay from now on the public policies of social insurance.

In Western Europe and the rest of the developed countries, private saving is stimulated by significant tax deductions that the long term, win both the individual (higher income) as State Hi (reducing pressure on public pension budget)

Regarding Romania, goals to be achieved should not cover only public pension reform but also increase viral contributions Pillar take it, with more attractive tax incentives for participation in voluntary third pillar private pensions.

Basically, private pensions, which complement the public system of pensions for cation participant must mean a diversification of income, but also a risk reduction for a decent financial inefficiency.

#### REFERENCES

1. EFRP: Global Economic Crisis - no reason to give back from the way of private pensions (May 2009)

---

2. EFRP: Directions for the European pensions reform and a report on the 11 private pension systems in Central and Eastern Europe (October 2009)

---

3. EU report: Public Pension system in Romania, threatened by demographic change (March 2009)

---

4. EU: Romania, among the countries with the largest long-term risks of the public pension systems (October 2009)

---

5. OECD: Economic crisis makes private pensions more necessary than ever (April 2009)

---

6. OECD: Securing yields of private pension funds should be avoided (June 2009)

---

7. OECD: What guarantees and restrictions are there in world of private pensions (July 2009)

---

8. \* \* \* Romania with the Pillar II Pension Fund returns compulsory private contributions to the initial schedule (June 2009)

---

9. \* \* \* Romania's agreement with the EU with IMF makes conditions double: speeding Pillar II and reform the public pension system (June 2009)

---

10. \* \* \* World Bank on the introduction of private pensions in Romania: reform can be difficult but successful (July 2009)

---

11. \* \* \* World Economic Forum: What should the states do to increase pension level (September 2009)