Pension Reform for the 21st Century

From Universal Entitlement to Protection Against Poverty

Core Idea

A pension should not be an automatic lifetime entitlement.
It should function as **protection against poverty in old age**.

Most citizens secure their living standard in retirement through their own capital accumulation.
The state guarantees only a **dignified minimum** to those who genuinely need it.

---

1) The Structural Problem

Demographic Shift

- In the 1960s, the ratio of workers to retirees was roughly **5 : 1**.
- Today it is about **2.5 : 1**.
- By 2050, people aged 65+ may represent **30–35% of the population** in many developed countries.

Fiscal Pressure

In many European systems:

- Public pension expenditures equal approximately **9–12% of GDP**.
- This share has been increasing and will continue to rise under current demographic trends.

The problem is structural:
an ageing population increases expenditures while the contributor base shrinks.

---

2) Conceptual Shift

The reform is based on one fundamental principle:

A public pension is not a reward for past work.
It is insurance against poverty in old age.

This is analogous to health insurance:

- Everyone contributes.
- Only those who need care receive benefits.

---

3) Structural Design of the Reform

Pillar I – Means-Tested Public Pension

The public pension is granted only to seniors in genuine economic need.

Eligibility criteria may include:

- Income below a defined threshold.
- Financial and real assets below a specified limit.
- No substantial income from productive or investment assets.

No confiscation of property.
No forced liquidation of assets.
If a retiree is financially secure, they simply do not receive public benefits.

Estimated outcome:

- Instead of nearly **100% of retirees receiving pensions**,
  only about **80–85%** (those in real need) would qualify.

Public expenditure would decrease from roughly **10–12% of GDP** to approximately **7–8% of GDP**.

Pillar II – Mandatory Individual Capital Accounts

A portion of current payroll contributions would be redirected into:

- Individually owned investment accounts,
- Fully inheritable,
- Legally protected private property.

Indicative structure of payroll allocation:

- **12–15% of gross wages** → individual capital accounts
- **10–12%** → public poverty protection reserve
- **7–8%** → administration and transition costs

This does not increase overall contribution burden — it reallocates it.

Effects:

- Higher domestic capital formation
- Increased long-term investment
- Greater intergenerational capital transfer
- Reduced dependence on public redistribution

Pillar III – Cost-Efficient Senior Infrastructure

Encouraging community-based senior living and shared services reduces:

- Housing costs,
- Social isolation,
- Healthcare system pressure.

Lower living costs mean lower required public minimum support.

Pillar IV – Flexible Retirement Age and Protection Against Late-Life Unemployability

In response to demographic developments, the **statutory retirement age shall be set at 67 years**. This threshold reflects increasing life expectancy and the need to ensure long-term fiscal sustainability of the pension system.

At the same time, a **protective mechanism shall be introduced for individuals aged 63 and above** who:

- are demonstrably unable to secure long-term employment despite active efforts, or
- experience significant health limitations that reduce their work capacity without meeting the criteria for full disability status.

In such cases, entitlement shall arise to:

- **early retirement without punitive benefit reductions**, or
- a **partial pension combined with part-time employment**, where partial work capacity remains.

The objective of this measure is to prevent the emergence of a social gap between unemployment and statutory retirement and to ensure that individuals over 63 are not left without income in situations where their employability is objectively constrained.

This pillar complements fiscal responsibility with social stability and helps prevent structural poverty in later life.

4) Macroeconomic Comparison

Current System

Indicator	Current Model
Public pension spending	~10–12% of GDP
Share of retirees receiving pensions	~100%
Demographic dependency	High
Implicit public pension debt	Rising

The system is highly sensitive to population ageing.

Reformed Model

Indicator	Reformed Model
Public pension spending	~7–8% of GDP
Share of retirees receiving public pension	~80–85%
Capital-based retirement share	High
Demographic dependency	Low
Fiscal sustainability	Structurally stable

Public obligations become limited and predictable.

5) Fiscal Sustainability

Under this model:

- Pension expenditure no longer scales linearly with ageing.
- Public liabilities are capped by poverty levels, not by total retiree count.
- The implicit pension debt declines significantly.

Even with zero population growth, the system remains viable.

6) Capital Accumulation and Growth

The reform increases:

- Household savings rates,
- Investment capital availability,
- Domestic capital ownership.

Higher capital intensity improves:

- Productivity,
- Wage growth,
- Tax revenues.

Economic stability becomes tied to productivity, not demographic expansion.

7) Intergenerational Effects

If middle-class retirees transfer assets earlier:

- Younger generations receive capital sooner,
- Investment cycles accelerate,
- Tax bases strengthen.

Capital is not destroyed — it is activated earlier.

8) Civilizational Context

Modern societies:

- Have low fertility,
- Live longer,
- Are highly individualised,
- Cannot rely on exponential population growth.

A sustainable pension model must function under demographic stagnation.

9) Strategic Conclusion

A 21st-century pension system should be:

- **Poverty protection**, not universal entitlement
- **Capital-based**, not fully pay-as-you-go
- **Demographically neutral**
- **Fiscally predictable**

The state guarantees dignity in old age.
Individual responsibility determines comfort.

This framework aligns economic sustainability with long-term demographic reality.

10) Quantitative Implication of Distributional Exclusion

A key fiscal mechanism of the reform derives from the non-uniform distribution of pension benefits across income groups.

If approximately the top 15% of the wealth distribution are excluded from eligibility for the public poverty-protection pension, the reduction in expenditure is not proportional to the population share. Pension benefits in the current system are positively correlated with lifetime earnings, and upper-income retirees receive significantly higher-than-average payments — in some cases approaching twice the minimum pension level.

Let the lower 85% of retirees receive an average normalized benefit of 1, and the upper 15% receive an average benefit multiplier of *k* (where *k* is plausibly in the range of 1.5–2.0). Total expenditure can then be expressed as:

$0.85 \times 1 + 0.15 \times k$.

Under these parameters, the upper 15% account for approximately 21–26% of total pension expenditure. Their exclusion would therefore generate a fiscal reduction in that range, materially exceeding their demographic share.

Depending on the precise benefit distribution, total public pension spending could decline by up to roughly 25–30%, representing a substantial structural adjustment rather than a marginal parametric reform.

11) Social Incentive Structure and Reputational Effects

Concerns about large-scale abuse of a means-tested pension system often overestimate purely financial motivation. In advanced societies, social status and reputation function as powerful non-monetary regulators of behaviour. For affluent individuals, applying for a poverty-based public pension would signal a visible loss of economic standing. The reputational cost — both socially and psychologically — would significantly outweigh the financial benefit of a modest minimum pension. Empirical evidence from welfare economics suggests that means-tested benefits typically exhibit lower participation rates among higher socio-economic groups not only due to income thresholds but also due to status considerations and perceived stigma. Therefore, beyond administrative safeguards, the system benefits from a built-in sociological stabiliser:
those who are economically secure have little incentive - financial or social - to claim a poverty-based pension.

12) Final Assessment

If expenditure is effectively stabilized at around **8–10% of GDP**,
if automatic disproportionate indexation is avoided,
and if productivity continues to grow at a moderate rate (e.g., 1–2% annually),

then the system remains **macroeconomically sustainable even with a 2:1 worker-to-retiree ratio**.

Without reform, a trajectory toward **20% of GDP** in pension spending would likely become structurally destabilizing — either through excessive labor taxation, chronic public deficits, or crowding out of other essential state functions.

This reform should be understood as a **structural response to long-term demographic and societal transformation**, not as a temporary fiscal adjustment.

Historically, only a relatively small share of the population reached advanced old age due to wars, lower life expectancy, and limited medical care. Pension systems were designed in that demographic context.

During the communist period, income differentiation was compressed. There was effectively one broad socioeconomic class, pension levels were relatively uniform, and multigenerational households were common. The pension system functioned within a socially homogeneous structure.

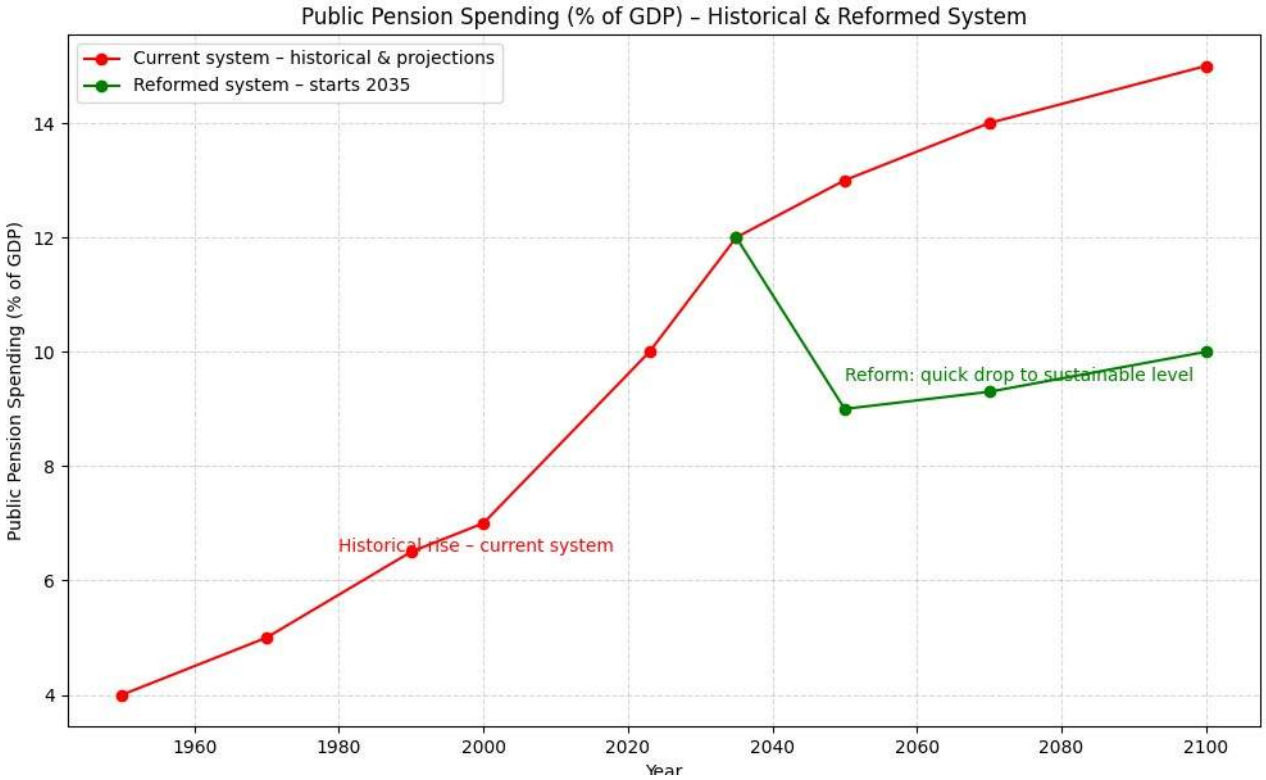
Today, the situation is fundamentally different:

- Longevity has increased significantly due to advanced medical care.
- Income inequality between high- and low-income groups has widened.
- Single-person households are far more common.
- Wealth accumulation at the top of the distribution has created structural divergence in retirement security.
- Longevity medicine further extends the duration of benefit collection.

In this new environment, maintaining a universal pension architecture designed for a shorter-lived, economically compressed society may lead to exponential fiscal pressure.

The proposed reform is therefore not merely a cost-cutting measure.
It represents an adaptation of the pension system to the **new structural reality of aging, inequality, and individualized living patterns**.

Economically, such a reform can be coherent and sustainable.
Politically and socially, it is inevitably contentious.


Public Pension Spending (% of GDP) – Historical & Reformed System
Current system – historical & projections
Reformed system – starts 2035
Public Pension Spending (% of GDP)
Year
Historical rise – current system
Reform: quick drop to sustainable level
4
6
8
10
12
14
1960
1980
2000
2020
2040
2060
2080
2100