

The Ambachtsheer Letter

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RETHINKING PENSIONS IN AMERICA:

ADEQUACY, RISK BEARING, AND INSTITUTIONAL STRUCTURE

“The Global Pension Index compares the adequacy, sustainability, and integrity of retirement income systems in 11 countries around the globe...”

Melbourne Centre for Financial Studies

Ranking America’s Retirement Income System

Last week in Miami we received the 2010 Lilly-white Award for “lifetime contributions to Americans’ economic security” from the Employee Benefits Research Institute (EBRI). The only thing that gave us some pause in accepting this honor was the word ‘lifetime’. Was there a subtle implication in that word that it is over now? No more *Letters* to write? In our view, not so! As evidence, we offer some fresh reflections on the state of America’s retirement income system in this *Letter*, focusing especially on opportunities where the system could be improved.

We noted in Miami that this was the first time the Award has gone to a person who the United States Immigration classifies an “alien”. We commended EBRI for recognizing the power of the internationalization of pensions, and understanding that much can be learned by comparing the strengths and weaknesses of retirement income systems (RIS), even if only on this planet. Indeed, a recent research project led by Australia’s David Knox through the Melbourne Centre for Financial Studies has produced the world’s first Global Pension Index (GPI), which attempts to capture the quality of a country’s RIS in a single metric. Eleven countries were evaluated in this first attempt, including the United States.

The overall findings (which Knox cautions are preliminary) are summarized in Table 1. Note that the United States receives a middling GPI ranking

of ‘C’, on a par with the United Kingdom, Chile, and Singapore. The report observes that the American GPI ranking could be increased by taking the following four measures:

- raising the minimum pension for low income earners,
- adjusting the level of mandatory contributions to increase the net replacement for median income earners,
- introducing a minimum access age so that it is clear that benefits are preserved for retirement purposes, and
- introducing a requirement that part of the benefit must be taken as an income stream.

Note that these measures focus on ensuring retirement income adequacy. Other areas for RIS improvement identified in the study were in the ‘system integrity’ area for the United States, specifically, regulation, governance, risk protection, and communications.

Table 1: Melbourne Mercer Global Pension Index: Overall Results

| <u>Grade</u> | <u>Countries</u> |
|--------------|--|
| A (>80) | |
| B (65-80) | Netherlands (76.1); Australia (74.0); Sweden (73.5); Canada (73.2) |
| C (50-65) | UK (63.9); USA (59.8); Chile (59.6); Singapore (57.0) |
| D (35-50) | Germany (48.2); China (48.0); Japan (41.5) |

Source: Melbourne Mercer Global Pension Index October 2009