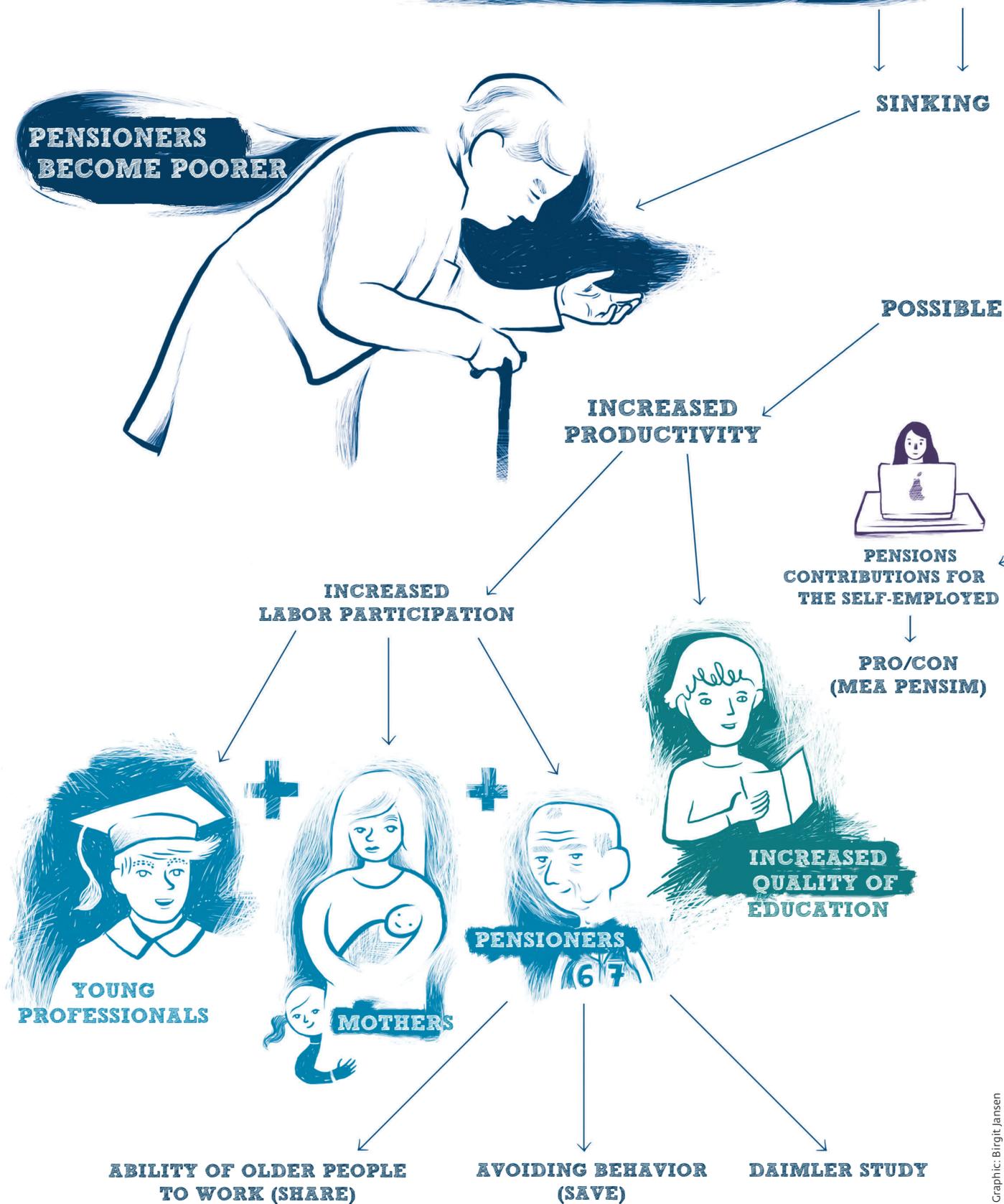


DEMOGRAPHIC CHANGE &

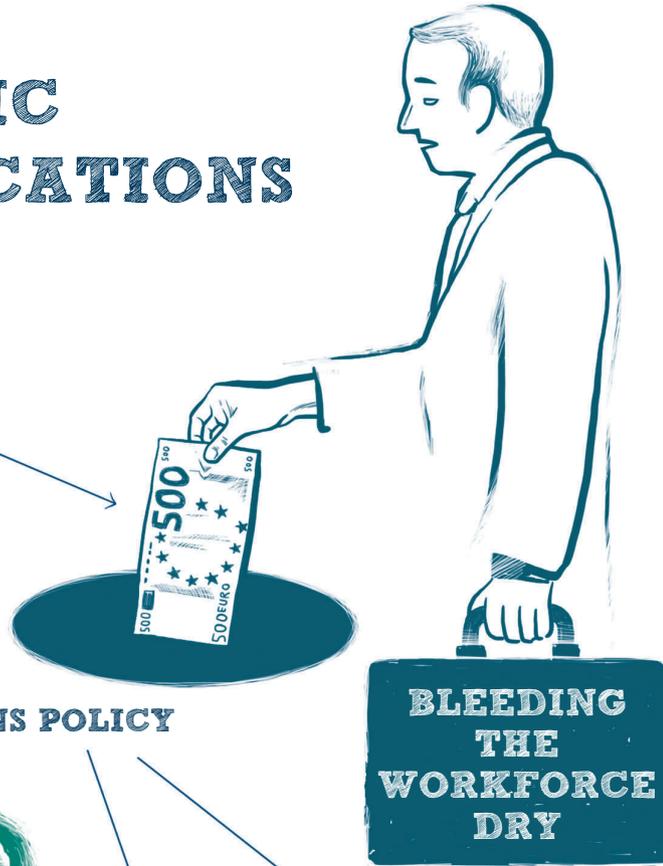


Graphic: Birgit Jansen

MACROECONOMIC IMPLICATIONS

↓ ↓ ↓
PRODUCTIVITY

SOLUTIONS



PENSIONS POLICY

**INCREASE IN
PENSION REDUCTIONS**



**PENSION
SUBSIDIES**

PRO/CON

**MONITOR +
READJUST**

**SIMPLIFICATION
OF THE RIESTER PENSION**



A Hard Piece of Work

Everyone who has worked for a long time wants to enjoy a sufficient pension. But is this still realistic given the scale of demographic change? How could the social insurance system be reformed to take the pressure off contributors and still prevent poverty in old age?

Axel Börsch-Supan conducts research in the politically charged field of pension financing, extended life expectancy and the threat of declining solidarity at the **Munich Center for the Economics of Aging (MEA)**, part of the **Max Planck Institute for Social Law and Social Policy**. He says the most important area to improve upon is labor force participation.

You study the macro-economic consequences of an aging society. What is the most pressing problem in this respect?

AXEL BÖRSCH-SUPAN: Our main challenge is how the productive capacity of the economy will develop in the future. In the decades ahead, there will continue to be a lot of people in Germany who want to consume goods and services. On the other hand, there will be fewer gainfully employed people available to produce the required output for the economy. This impacts the financing of pensions, among other things. An even greater problem could be financing health care, because this is an area in which costs are rising even faster than in pensions. Our ability to absorb this development depends primarily on economic growth. Without more labor force participation, the demographic shift toward a higher proportion of older people will see Germany slipping down the ranks of the world's strongest economies.

What concrete consequences can be expected?

If we don't succeed in helping more older people, women and young people to participate more in the labor market, our economic standard of living will fall by around a sixth by 2050. And that's not all. This isn't a one-time wave that we can just duck under in order to outlive the problem. If we follow the projected development into the future, the downward trend does slow somewhat, but the standard of living will

remain at a low level. A sudden return to the current level can't be expected.

How will the anticipated decline in the standard of living impact the different income groups?

We have only a macro forecast, which allows us to make statements about average people. It's difficult to estimate how the effects will be distributed among the different income groups. Over the past few years, the gap between rich and poor has grown ever larger. At the moment, the relationship seems to be constant. Future development is completely open and could go in any direction. The only thing we can say with any certainty is that the situation of migrants and single parents hasn't improved.

How do you produce forecasts like this? Are there also forecasts that reach a different conclusion?

We use mathematical models. The findings are relatively robust: none of the forecasts predict that things would get better or stay the same if conditions don't change. Essentially, it's a very simple formula. The models are based on an economy that comprises about as many people as today. After all, we don't expect a substantially shrinking population for the next 25 years. Quite the opposite – the German population even grew again in the past year. But year for year, the number of children starting school is decreasing.

These are the future gainfully employed workforce. This makes calculations simple: What does an individual gainfully employed person currently contribute? How much less do we get if the number of gainfully employed people declines?

Where do policymakers have to get involved to cushion the economic effects of demographic change?

The most important area to work on is labor force participation. In Germany, there are, for instance, still relatively few people who are gainfully employed by the age of 24. Germany also has a low participation of women in the workforce, as many work part-time. That's why we have lower productive capacity in the economy compared with the Scandinavian countries or Switzerland. Another area to be looked at is reforming college conditions so that people can start earning a living sooner. Likewise, we need a sufficient supply of childcare places to allow people to better reconcile work and family. These are all measures that increase the quantity of available productive capacity. Other approaches relate to quality – we have to improve the level of education. We know from the PISA and TIMSS studies that we in Germany have a relatively poor school education. We are systematically creating a real emergency situation in education, particularly among people with a migration background. Unemployment is concentrated within this group, as is poverty. We have to address this.

SIMULATIONS: MEA-PENSIM

MEA-PENSIM is a simulation system developed at the institute that can be used to investigate how economic and demographic factors change under mutual dependence.

One question that researchers are addressing is: What would the long-term consequences be if self-employed people were integrated into the national system of pension insurance? It is under discussion as a suggested reform, as it is suspected that a large proportion of non-socially insured self-employed people currently generate only low levels of income and don't have sufficient pension plans in place. When they are old, this group will be reliant on government aid. The results of the simulation studies show that the inclusion of self-employed people leads to a reduction in

pension insurance contributions in the short to medium term because the new group of people pay contributions, but initially claim hardly anything back. This takes the pressure off the middle generations from the 1960s to 1980s, whose perspectives have been particularly impacted by the reforms of the early 2000s, which agreed a reduction in the pension level. So in the end, this measure leads to greater equality between generations. However, in the long term (by 2060), contributions would reach the same level without self-employed people in all of the scenarios investigated. If one were to assume that self-employed people have a higher life expectancy because of their social background, the contributions would even be slightly higher.



"Pension policy is secondary" says Axel Börsch-Supan and warns: "If we don't succeed in helping more older people, women and young people to participate more in the labor market, our economic standard of living will fall by around a sixth by 2050."

How can research help to implement these strategies?

We can do two things: First, we have to analyze the status quo in the areas of education, poverty and health. We still have far too many prejudices here. One example is the much-cited fear of rising poverty, particularly in old age. In fact, however, it is children in single-parent households who are most impacted by poverty! Another example is the view that retirement as late as age 67 is practically impossible because most employees are either worn out or sick by 65. Wrong! Most people in the 60-70 age range are doing fine. We also know that 70-year-olds enjoy a substantially better level of health than they did 20 years ago.

Why is that?

The improvement has nothing to do with the fact that typical age-related illnesses are occurring later in life. After all, human biology changes very slowly. The disabling effects of typical age-related illnesses, however, are occurring later because modern medicine and technology are making it substantially easier to live with these illnesses. One example: disabilities stem-

ming from cardiovascular diseases are considerably less common than they used to be. This is due primarily to the fact that, today, anyone who has a problem with their heartbeat gets a pacemaker. Pacemaker batteries are even replaced for 85-year-olds, if need be. In the past, no one would have dared to do this.

How do you come to make reliable statements on the health of older workers?

You can't just ask people how healthy they think they are. Some people like to complain, while others brag. It has to be measured. You take blood and look for stress hormones, analyze blood sugar and check how many people have diabetes. You ask the study participants to walk a bit and then you look at their physical performance.

Do you only measure them? You don't ask any questions?

Of course we also ask questions – for instance about money. We do it all here at the institute: a huge data collection project called SHARE – Survey of Health, Ageing and Retirement in Europe. This allows us to ask also very different questions

than those relating to the health of the over-50-year-olds. We also investigate how people react to political measures. How rapid and how strong are the reactions? Do some things cause people to react in a completely different way than policymakers actually intended? Here we also attempt to identify causality. This is difficult because many things happen at the same time, so several causes for the observed phenomenon always have to be considered. We have to look carefully at the statistics and see what has changed in which situation and how. The SHARE data enables this because it is collected in 20 countries in parallel, making international comparisons possible.

How can you use the survey results to make statements relating not only to health, but also to the performance of older people in their work?

There are a whole host of studies that focus on cognitive ability alone. Most people need glasses or a hearing aid at some point. Reactions also slow down. On the other hand, older people perform better than young people when it comes to experience, soft skills and dealing with excep-

INDIVIDUAL BEHAVIOR: SAVE

As part of the SAVE study, academics and scientists from the MEA are examining how people in Germany save and make provision for the future. SAVE is designed as a longitudinal study, surveying the same households every year. The data provides information on how people react to political measures. One important topic is the government funding for Riester pension insurance contracts. The investigations show that people with lower incomes and a lower level of education take out these contracts less often than better-educated people even though the funding is more generous for the former group.

At the same time, the study also found that purely financial incentives are often not enough to encourage people to act. “We asked people: Are you entitled to Riester funding? And: Are you employed in a profession that requires social insurance? Is your partner? Many answered: I am employed in a profession that requires social insurance. But at the same time, they stated: I’m not entitled to funding. That’s a clear contradiction,” explains Michela Coppola, a department head at the MEA. Another question was then why they hadn’t concluded a Riester contract. The majority answered: I don’t have any money left over. However, the analysis showed that the frequency of this answer was relatively independent of the actual income situation. Coppola explains:

“This indicates that people don’t see pension planning as a motive for saving.”

We also wanted to know whether the study participants believe they will receive a basic pension when they are old – which could mean that a private pension would be unnecessary, because this would be taken into account for the amount of the basic pension, which is comparable to Hartz IV unemployment benefits. The results of the survey indicate that the probability of being entitled to the basic pension in old age is often overestimated, especially by those in the lower income classes.

Furthermore, the survey results from SAVE also make it possible to more precisely assess the successes of the Riester policy to date. General statistics provide only information about the number of newly concluded insurance contracts. However, it is only by examining the individual levels that we can see to what extent non-government-funded life insurance has been replaced by the subsidized Riester contracts. These figures actually give cause for skepticism. Especially in a particularly savings-oriented country such as Germany, researchers use the SAVE data to show that the additional incentives to make private pension provisions via Riester funding are incredibly low. Taxpayers’ money would therefore presumably be better invested elsewhere.

tional situations. We carried out a very interesting study together with Daimler: for four years, we monitored working groups of 12 to 16 people working on the production lines in a truck assembly plant. Work at some stations is heavily standardized: the conveyor belt always runs at the same speed. Now and again, though, errors occur. This allows productivity to be measured. We observed that older people make more small mistakes, while the younger people make the catastrophic errors. Catastrophic errors cost the factory more!

Which clearly shows that employing older people also has its advantages.

It’s all about the mix. Working groups that consist exclusively of older people are less productive overall than mixed teams! And this isn’t restricted to truck manufacturing. We are currently also carrying out a study with a large insurance company, and are seeing very similar results. Another example: Younger employees produce more patents. But turning the patents into saleable products – that’s something the older employees are more likely to do. You earn money by combining the two.

Now let’s talk about the topic of pension policy. Last year, together with other MEA researchers, you published a comprehensive statement on the federal government’s pension reform plans ...

Could I stop you here? I’ve been researching pensions for 20 years. My name is always associated with this topic – in fact, to an extent that I can no longer bear. When it comes to an “aging society,” everyone immediately thinks of old people, and then talks about pensions and pension policy. That’s the wrong approach! Even in 2050, there will still be more people under 50 than over 50. In this context, pension policy is secondary. Much more important than talking about minimum pensions are better education policies. You can already see, in people around the age of 20, who will be receiving the basic pension later. That’s something that depresses me and that I can get really upset about. We have to do more about this! We’re sending young people with no school diploma out into the world and then wondering why they’re long-term unemployed, why they can’t get enough points together for a pension, and why some might even turn to a life of crime.

Nevertheless, you also get involved in the discussion about pension reform. In particular, you criticized the plans for a “Lebensleistungsrente” – a pension based on how much a person worked in their life. Why?

The draft law about this is designed in such a way that the benefits for those affected by poverty in old age aren’t even achievable. At the moment, the debate is about an eligibility requirement that is based on 40 years of pension contributions in order to be a recipient of a pension subsidy. This is a qualification that those people who most desperately need the pension subsidy won’t be able to achieve. Another criticism: the pension subsidy is a redistribution from young to old, burdening young pension contributors. But those are exactly the ones who will suffer the most under the weight of demographic change.

How much of an influence do you think academics have when they advise policymakers?

You can get lucky and have a huge influence, or you can talk until you’re blue in the face and nothing happens. Everyone knows, for instance, that all the experts

are against an unlimited pension guarantee. However, this idea can no longer be shifted out of the political process. Or the pension at 67: Initially, this proposal failed in the Rürup Commission. But Mr. Müntefering saw that there was no other way. He used his power as a minister to get the pension at 67 adopted. Another example: The “sustainability factor” in the pension adjustment formula, which I suggested several years ago, was adopted one-to-one.

What is the sustainability factor?

The basic idea behind it is that if there are fewer contributors in the entire system, then on the one hand, pensions have to be reduced, and on the other hand, contributions to social insurance need to rise – both to an extent that the younger and older generations are impacted in exactly equal proportions. That is what the sustainability factor stands for.

What criteria should be used to evaluate political measures that respond to demographic change? Does fairness play a role, for example?

It is difficult for an economist to use such an emotionally charged term as fair distribution. It can be seen as unfair if someone works a lot and receives the same amount as someone who works a little. But you

can also see it as unfair that one person earns a lot and another little. Yet between these there is a contradiction: it's impossible to rid the world of both forms of unfairness in one fell swoop. In this situation, an economist, as a scientist, can't say anything.



“You can get lucky and have a huge influence, or you can talk until you’re blue in the face and nothing happens.” Max Planck Director Axel Börsch-Supan is in demand among policymakers and the media alike.

INTERNATIONAL COMPARISON: SURVEY OF HEALTH, AGEING AND RETIREMENT IN EUROPE (SHARE)

How do people living in the European Union countries age? Answering this question, with a view to using the opportunities of demographic change systematically, is the aim of the international survey project SHARE, which is being coordinated by the MEA.

The first representative survey of the financial, health and social situation of the population in the 50+ age group was carried out in 11 countries in 2004. Now, roughly 90,000 study participants from 20 countries are surveyed every two years, reporting their life stories. This allows researchers to examine how they deal with important events that occur in their lives, such as reaching pension age or becoming widowed, or how changes in the institutional framework (such as reforms in the healthcare or pension system) impact the quality of life of older Europeans. In addition, people’s grip strength, lung volume and walking pace are measured, for example, allowing health indicators to be compared across a number of countries.

The data is now used around the world by over 3,000 researchers from different disciplines. Numerous articles in scientific journals document the extensive analysis of the data that provides a scientific basis to support decision-making processes in national and European policy.

Last question: What has changed for the MEA now that the institute has been integrated into the Max Planck Society?

In contrast to what is otherwise the case with the Max Planck institutions, we haven’t set up a new institute. I founded the MEA in Mannheim in 2001 before we moved the entire operation to Munich in 2011. It goes without saying that we’re delighted to have gained a long-term basis for our research work with our integration into the Max Planck Institute for Social Law and Social Policy. Above all, however, we have since also gained a broad interdisciplinary peer group of Max Planck directors and young researchers with whom we can discuss issues on an academic basis. We work closely with the Max Planck Institutes for Demographic Research, for Human Development and for the Study of Societies. That is a massive gain for us.