Nonfinancial Defined Contribution Pension Schemes in a Changing Pension World

Volume 1: Progress, Lessons, and Implementation
Volume 2: Gender, Politics, and Financial Stability

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Nonfinancial Defined Contribution (NDC) schemes are now in their teens. The new pension concept was born in the early 1990s, implemented from the mid-1990s in Italy, Latvia, Poland and Sweden, legislated most recently in Norway and Egypt and serves as inspiration and benchmark for other reform countries in the OECD and non-OECD area. This innovative unfunded individual account scheme created high hopes at a time when the world seemed to have been locked into a stalemate between piecemeal reforms of ailing traditional defined benefit schemes and introducing pre-funded financial account schemes. Simply put, the scheme pays an individual out as pension when retired only what contributions have been paid in when active (plus notional interests every year). Financial stability is achieved by paying such a notional interest rate the unfunded, i.e. pay-as-you-go scheme can afford, and by making pension levels dependent on the life expectancy at retirement.

The experiences and conceptual issues of NDC in its childhood were reviewed in a prior anthology (Holzmann and Palmer, 2006). This new anthology serves to review its adolescence and with the aim of contributing to a successful adulthood. Volume 1, Lessons, Issues, and Implementation, reviews and draws policy lessons from experience with NDC schemes in the original pilot countries and in subsequent adopters and examines the potential of NDCs in other countries, including Chile, Greece, and China. Volume 2, Gender, Politics, and Financial Stability, contains new and deeper analyses of issues that received little or no attention in an earlier (2006) publication. such as the of the “NDC story”, making transparent the legacy costs, financial accounting, balancing, creation of a reserve fund, gender, and longevity. The book also contains analyses of the pros and cons of NDC contra FDC and a typical paygo DB scheme in two Latin American countries. The 24 chapters in the two volumes offer new insights and strong guidance for pension reformers around the world, independent of the reform model envisaged. The NDC approach pinpoints the pension issues that any main public scheme must confront, making it well suited to serve as a benchmark for discussion of reforms.

The key policy conclusions include: (i) NDC schemes work well (as documented by the experience of Italy, Latvia, Poland and Sweden during the recent and ongoing crisis) but there is room to make them work even better; (ii) Go for an immediate transition to the new scheme to avoid future problems; (iii) Identify the legacy costs and their explicit financing during the transition as they will hit you otherwise soon; (iv) Adopt an explicit stabilizing mechanism to guarantee solvency; (v) Establish a reserve fund to guarantee liquidity; (vi) Elaborate an explicit mechanism to share the systemic longevity risk; and, last but not least; (vii) Address the gender implications of NDC with deeper analysis and open political discourse.