

# ON THE POLITICAL FEASIBILITY OF INCREASING THE LEGAL RETIREMENT AGE

Benjamin Bittschi and Berthold U. Wigger

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# MOTIVATION

- ▶ Population aging due to an increase in life expectancy is a trend in virtually all developed economies
- ▶ Trend as such hardly alarming
- ▶ However, pressure on old-age security

OECD average: Expected years in retirement, by sex

Time	1970	1980	1990	2000	2010	2016
Men	10,6	12,6	14,8	16,9	18,2	18,1
Women	14,6	17,4	20,0	22,6	22,8	22,5

Source: OECD

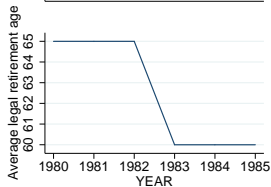
# MOTIVATION

Basically, three strategies have been pursued to stabilize the financing of public pensions:

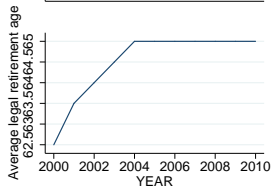
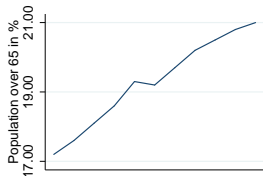
1. Increasing revenue by raising contribution rates, taxes or debt
  2. Cutting benefits
  3. Postponing retirement
- ▶ First strategy, widely used but given the current economic environment not sustainable anymore
  - ▶ Second strategy, becomes the more unpopular the older the population grows
  - ▶ ... third strategy remains

## MOTIVATION

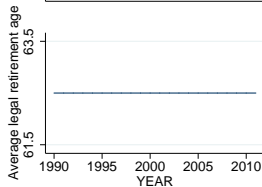
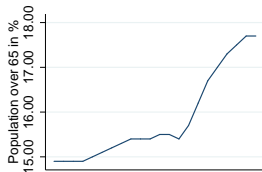
France



Germany



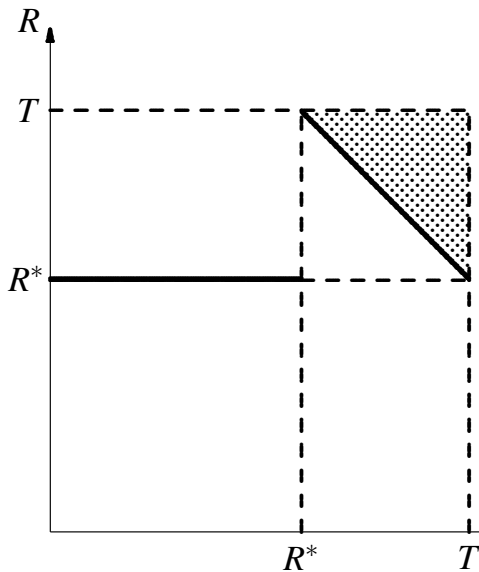
Austria



# CONTRIBUTION

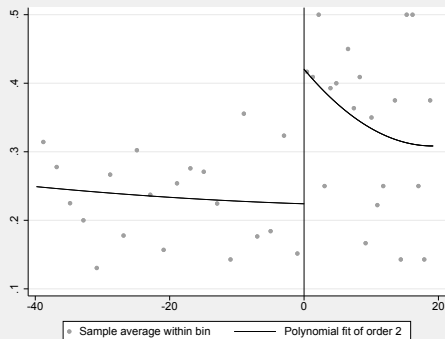
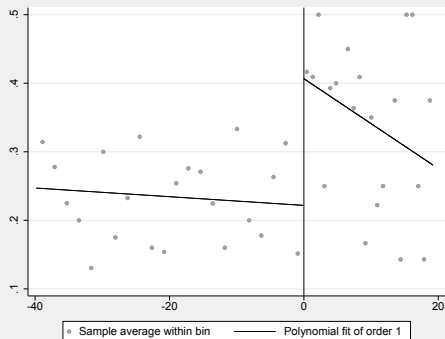
- ▶ Simple politico-economic model with legal retirement age as outcome of majority voting demonstrates that
  - ▶ retirees prefer a higher legal retirement age compared to workers
  - ▶ Retirees who have just retired prefer the highest legal retirement age
  - ▶ increase in life expectancy leads to higher legal retirement age
  - ▶ increase in replacement rate leads to lower legal retirement age
- ▶ Empirical validation of the theoretical predictions
  - ▶ Individual reform preferences using German micro data
  - ▶ Comparatively using OECD data

## RESULTS



## RESULTS – FRD

Discontinuity effect of pension



## RESULTS – FIXED EFFECTS REGRESSION

	(1) Legal ret. age Average	(2) Legal ret. age Average	(3) Legal ret. age Women	(4) Legal ret. age Women	(5) Legal ret. age Men	(6) Legal ret. age Men
Replacement rate	-0.073*** (0.025)	-0.050** (0.020)	-0.083*** (0.026)	-0.065** (0.023)	-0.063** (0.025)	-0.035* (0.020)
Population over 65	0.352*** (0.092)	0.364** (0.130)	0.511*** (0.092)	0.543*** (0.121)	0.194* (0.112)	0.185 (0.157)
Life expectancy at age 65		0.243 (0.507)		0.152 (0.677)		0.334 (0.444)
GDP per capita		-3.594 (2.084)		-3.205 (2.174)		-3.983* (2.072)
GDP growth		0.017 (0.038)		-0.005 (0.045)		0.038 (0.039)
Government support		-0.007 (0.013)		-0.003 (0.013)		-0.011 (0.013)
Country FE	YES	YES	YES	YES	YES	YES
Time FE	NO	YES	NO	YES	NO	YES
Observations	713	700	713	700	713	700
Countries	20	20	20	20	20	20
Adj. R <sup>2</sup>	0.247	0.305	0.335	0.359	0.122	0.217

Standard errors (clustered at the country level) in parentheses; \*  $p < 0.10$ , \*\*  $p < 0.05$ , \*\*\*  $p < 0.01$





# CONCLUSION

- ▶ Retirees compared to workers have a higher probability to vote for an increase in legal retirement age (micro data for Germany)
- ▶ 1 percentage point increase in share of the elderly increases legal retirement age by 0.3 to 0.5 years (cross country data)
- ▶ 10 percentage point increase in replacement rate reduces legal retirement age by 0.5 to 3 years (cross country data)
- ▶ Policy Conclusion (i): If policy manages to limit generosity of pension system, increase in legal retirement age as response to aging can be expected to find political support
- ▶ Policy Conclusion (ii): The just retired support an increasing retirement age most → implications for pension reform timing, as the expected retirement of the baby boomer generation will be favorable to increase the retirement age.