

***Comments on 'The role of
Government in Life-Cycle Saving
and Investing'***

Lans Bovenberg

Netspar, Tilburg University

October 27, 2006



Life cycle saving and investing

- Broad life-course perspective
- Human capital and labor markets
- Owner-occupied housing
- Health care

Outline

- A European (Dutch?) perspective
 - A third way (between individual DC and corporate DB plans)
- Role government: public-private partnership
- Financial and institutional innovation
- Labor markets and human capital

Demise corporate pension plans

- Firm-sponsored plans with firms as residual risk bearers belong to the past.....and rightly so
 - DB guarantees have become so expensive that they dominate core business
 - Ineffective with rapid turnover of firms
 - Participants bear credit risk of company
 - Use capital markets do diversify
 - Conflicts of interest
 - Employers may exploit put option provided by participants (and in US: government)

A third way: collective, stand-alone plans

- Fight selection in annuity markets
 - Homogenous groups in terms of human capital
- Limit transaction costs
 - Administrative and marketing expenses
- Protect imperfect individuals against themselves
 - Lack foresight, discipline and skill
- Exploit capital markets to shed risk externally
- Participants can share risks internally
 - Risk sharing between young and old
 - 'hard' (DB) and 'soft' (DC) claims
- Non profit insurance company with workers as shareholders

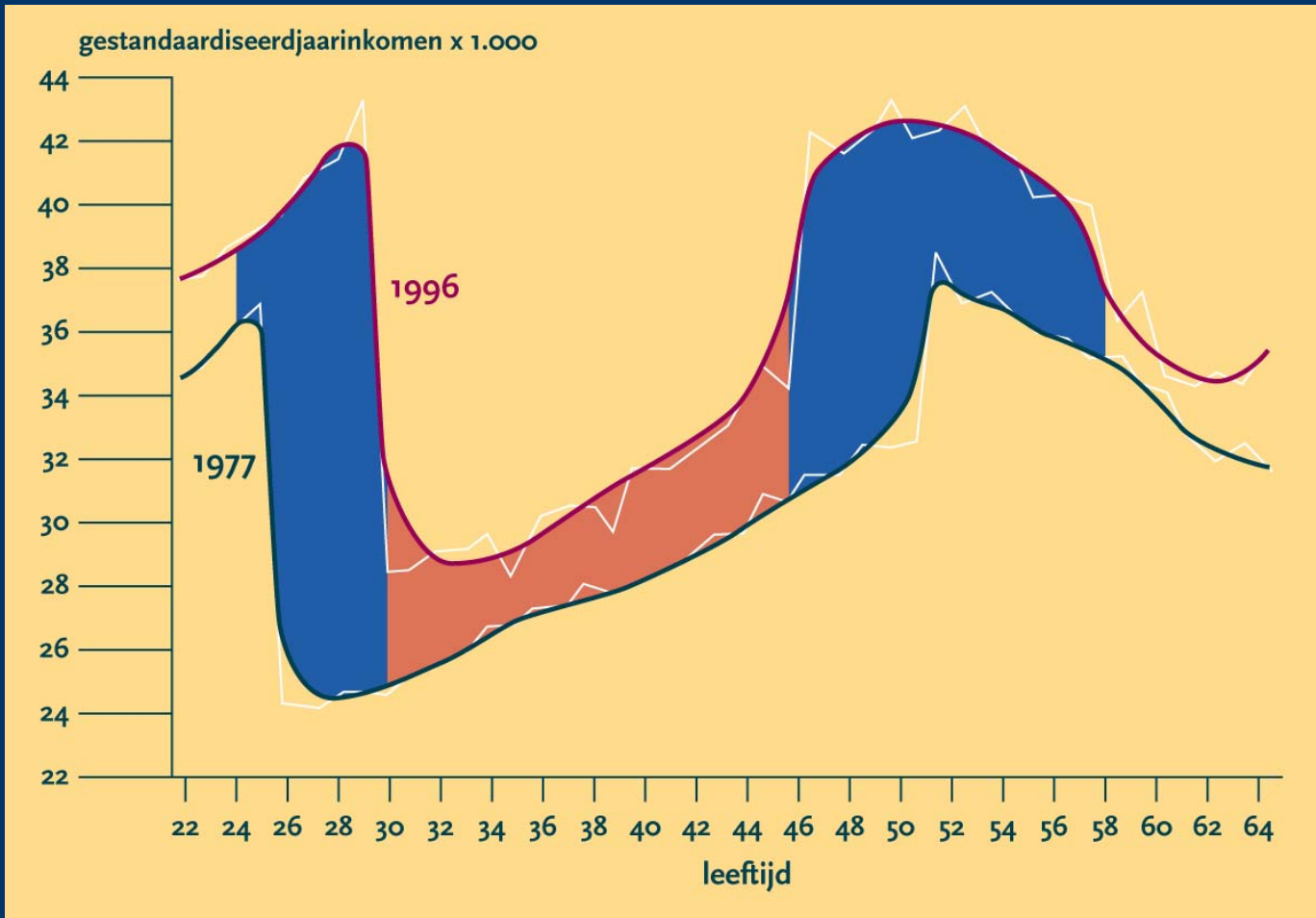
public policy

- Issue longevity bonds
 - Link retirement age to longevity
- Issue inflation indexed bonds with long maturities
 - Intergenerational risk sharing
- Limit tax advantages to annuities and worker's mortgages that are amortized
 - What is benchmark for tax expenditures?
 - Reverse mortgages hedge interest-rate risk annuities
- Compulsion (or defaults)
 - Amount of saving
 - Create pools by sorting on type of human capital
- Stable first PAYG pillar
 - prevent old-age poverty through flat (or means-tested) benefits
 - earnings-related benefits a private responsibility

Financial and Institutional innovation

- Integrated financial planning over the life cycle
 - Decumulation phase: annuities, health insurance, housing
 - Accumulation phase: insure human capital
 - Combine precautionary saving and insurance
 - Other types of leave: feminization of work
 - Labor markets: New roles employers and unions
 - Build insurance pools
 - Select providers
 - Educate workers
 - Set defaults
 - Help works maintain human capital and absorb risks through flexible labor markets

Life-course perspective



Labor market; accumulate, maintain and use human capital

- Invest more in human capital: walk on two legs
 - Expensive health care and increased longevity
 - Worse risk-return trade off
 - Knowledge economy and scarce human capital
 - Low real interest rates
- Raise effective retirement age (and link to longevity)
 - Avoid vicious circle decline with maintenance human capital
 - Fight concentration work in child-bearing years
- Flexible, gradual retirement as risk absorber to prevent risk shedding
- Tie worker less to single employer
 - Replace job security by employment security
 - Reduce back loading: Stimulate entrepreneurship elderly

Contact Information

Lans Bovenberg

Prof.dr.

Tilburg University / Netspar

+31 13 466 2703

+31 13 466 3066

a.l.bovenberg@uvt.nl

www.netspar.nl