



The pensions time bomb

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HADAS PARUSH / FLASH90

ACCORDING TO the National Insurance Institute, one in every five persons over 65 (185,000 people) is poor. This ranks Israel 24th out of 34 OECD countries, with an incidence of elderly poverty 11 times higher than the Netherlands. Many of the poor are Holocaust survivors, which makes their penury doubly sinful.

True, there has been progress – in 1997 one senior in every four was poor. But a major crisis looms. Demography, economics and politics are conspiring to deplete the National

Insurance Institute’s actuarial reserve fund, managed by the Bank of Israel, from which old-age benefits are paid. In less than a decade, payments from the fund will exceed income, and by 2042 or earlier, the whole fund will be gone.

In a nation where the long run is defined as tomorrow, it is nearly impossible to draw attention to a crisis that will occur in more than two decades. The problem is if we do not fix the slowly ticking pension time bomb now, it will be nearly impossi-

Retirees warm up during dance practice at a community center in Jerusalem’s Pisgat Ze’ev neighborhood

ble to defuse when it explodes.

Israel is not alone in facing this dilemma. Nearly the entire world faces a crisis in supporting its elderly. According to the Washington think tank Heritage Foundation, America’s Social Security fund will be insolvent by 2033, and probably much sooner.

MARKETPLACE

There are three main reasons.

First, fiscal: After overspending for decades, governments are slashing spending and deficits and, with them, elderly benefits. Moreover, by battling the 2008 global economic crisis by lowering interest rates, governments have forced pension funds to earn far lower returns on their investments.

Second, demographics: People are simply living longer, the baby boomers are retiring and the baby-bust generation is too few in numbers to support them. When the Prussian diplomat Otto von Bismarck invented old age pensions in 1889, he set the retirement age at 65 because few people lived that long. Today, in Israel, those aged 65 can expect to live for at least 20 more years. As a result there are five persons of working age for each person over 65. By 2050, there will be only three.

Third, psychology: Young people in the West do not save enough and, even in high-saving Asia, saving rates are falling. It's easy to understand why. Young people are raising families and enjoying life. Retirement seems far off. By the time people are able to save, after raising their families, it is simply too late to accumulate enough resources to retire comfortably.

In the US, the baby boomers thought their houses saved for them, as the property bubble inflated housing prices. When the bubble burst in 2008, many of them could no longer afford to retire.

WE'RE WAGING A WAR AGAINST OUR OWN CHILDREN. IT'S A WAR OF FUNDING SHORTFALLS AND EVER-INCREASING CONSUMPTION BY OLDER PEOPLE

The arithmetic of the pension crisis is very simple. Suppose you work for 40 years, from age 25 to 65. Suppose you save 20 percent of your net income, including your employers' pension contributions – a benchmark very few people attain. That means you have saved eight years' income (1/5 times 40). That sum has to pay for 20 years of retirement. Even if it earns interest, it will not be enough.

This is not just a governmental problem.



For years, universities paid “defined benefit” pensions directly out of their coffers with no contributions from employees or faculty. As a result, the Hebrew University of Jerusalem now has a total pension obligation amounting to 12.6 billion shekels (\$3.2 billion). Annual unfunded pension benefit outlays are over 600 million shekels (about \$150 million). This is a crippling burden on an annual budget of 2.5 billion shekels (\$600 million), half of which comes from the Treasury. Spending on research and equipment will suffer as a result.

Boston University Prof. Laurence Kotlikoff has studied the problem for years. Like many academics, his findings are usually understated and qualified. But here is what he told Credit Suisse's magazine, *The Financialist*, last November.

“We're waging a war against our own children. It's a war of funding shortfalls and ever-increasing consumption by older people at the expense of coming generations. We've turned retirement into a well-paid long-term occupation. It's extremely unfair to our children, grandchildren and great-grandchildren. We're burdening them with massive government debt in order to pay for that generosity. Those unfunded bills will stretch into eternity and our children won't be able to pay for them.”

In other words, if governments maintain retirement benefits at current levels, the burden on the younger generation will be intolerable. If they slash retirement benefits, they cause the elderly to sink into poverty. Both

outcomes are unacceptable.

Israel has been tackling the pension crisis piecemeal for years. Legislation in 1995 made it compulsory for all workers to contribute to a pension plan. In 2003 old-line pension funds mismanaged by unions (Histadrut, Israel Electric Co. and Israel Aircraft Industries) were bailed out and taken over by the government. Benjamin Netanyahu, then finance minister, enabled pension funds to invest in high-yield corporate bonds – a decision that later caused huge losses. In 2003, the retirement age was raised. Between 2005 and 2008 workers were enabled to shift their pensions among competing funds. But none of these measures even began to solve the underlying problem.

What in the world can be done now to defuse the time bomb? To find out, I spoke with Dr. Moshe Gerstenhaber, a Swiss-Jewish entrepreneur and Israel supporter who founded Kall Kwik, Europe's largest copy and printing chain, in 1978. He has been researching the pension crisis for nearly two decades, long before the world became aware of it. Gerstenhaber's 2009 book “Have You Ever Seen a Retired Tiger in the Jungle? Eradicating Pensioner Poverty” is lively, clear and full of common sense.

The Jerusalem Report: *Your book outlines a practical solution to what seems to be a nearly intractable problem. Can you explain your proposal briefly?*

Gerstenhaber: “In nature, tigers have no retirement prospects, but mankind does. This is a great achievement. But how much lon-



Moshe Gerstenhaber: Have you ever seen a retired tiger?

the economy, producing real jobs, real products, real prosperity. The cost? For Israel, just over 0.5 percent of Gross Domestic Product. ... I have suggested to Hebrew University Prof. Eitan Sheshinski that the state could launch the process [I propose] with some of the windfall money from the gas reserves.

“The power of this growing wealth fund is substantial; it can quickly generate additional GDP growth to more than offset the 0.5 percent cost.

“To pay for the Grant at Birth, we need a Special Levy, a tax collected one-third from households (excluding the poor) and two-thirds from employers.

“We want citizens to understand we are embarking on a new process of reinvention. And we want the nations’ politicians to think, for once, about the long-term well-being of the individual, society and nation. This is the real stumbling block. They do not stop to think how less than 5 percent [return on pension funds] over 20-30 years is not going to be enough to produce a living wage for the retired population. “The population of retirees is growing. They will vote to protect themselves and their pensions. The young will demonstrate and storm parliaments proclaiming that the old are stealing their dreams. Action is desperately needed.”

French economist Thomas Piketty [The Report, July 14, 2014] observed that the rich earn 8 percent a year, doubling their wealth each decade, while the middle class save little and earn very little. How can we level the playing field?

“MaxiLife – a one-stop Internet gateway software designed to become each individual’s ‘secret garden.’ Free to all, it will help each person maximize his or her own life potential and help generate enough income to assure continuing development. It will accumulate data to help each individual navigate more successfully the challenges and opportunities of life, including pension saving.”

We know today that ostriches do not, as the legend says, bury their heads in the sand in the face of looming danger. But societies do. How in the world can we get the democratic system to address the pension time bomb?

“Politicians tell us stories to keep us voting for them. No one really grabs the bull by the horns. The only way to ‘lance the boil’ is to get the public to demand it. We need the media to buy the story. Today, the Inter-

net is the biggest medium of contact among people. Going viral on Facebook is a good beginning.”

Underlying your thinking is a different paradigm of capitalism. What is it?

“The current [economic] environment is poisonous to the future of mankind. The actions of speculators created a virtual economy 200 times bigger than the real global economy [my estimate].

SOCIETIES NEED TO SET ASIDE MANY MORE RESOURCES TO FUND RETIREMENT

“My book introduces a new model I call Qumulism, from the words Community and Accumulation. Qumulism merges the vast wealth-creating potential of an ambitious community working together. It is an intelligent, affordable market-based solution to two of our most pressing economic challenges: funding pensions for all and developing a more robust, sustainable economy. The level of state participation in the economy will shrink substantially and welfare costs will fall once the job creation process picks up speed. The state will not try to manage the economy beyond reforming the tax system and controlling abuse by the speculators.”

I deeply regret that, at the urging of economists, governments in Europe, the US and to some degree even in Israel have embraced austerity – spending cuts to slash deficits. The result has been stagnating economies with deficient demand. In a flagging economy, Israel’s 2014 budget deficit was even less than the targeted three percent of GDP.

Gerstenhaber argues, persuasively, that societies need to set aside many more resources to fund retirement. Will this added saving not worsen the deficient-demand stagnation?

The answer is no. If the added saved resources of the Super Trusts are invested wisely in the real economy, to grow businesses, the resulting capital formation and new jobs will both fund retirement and spur growth.

It sounds logical. But, is anybody listening? ■

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ger can it last in the present circumstances? The pension accumulation process has to be lifelong if we are to achieve a real transformation. Time is of the essence. I propose to create a Super Trust Fund invested at 5 percent, which doubles every 14 years. From birth, that makes nearly five doublings by retirement at 65. And management fees will be 1/10 of 1 percent, not 1-1.5 percent.”

You dedicated your book to Warren Buffett, one of the world’s richest persons. Why?

“Buffett has been acquiring companies for the past 50 years and growing them – not dissimilar to the proposed Super Trusts. He achieved 22 percent return. That rate doubles wealth every 3.5 years. I am only asking for 5 percent compounded growth of shareholder funds.”

Israel privatized pensions some time ago. Why has this become part of the problem rather than the solution?

“Insurance companies take pension contributions and charge a whole range of fees that enrich the top managers but cut into the final pension substantially. It is said that pensions would be 40 percent higher without the fees. With the insurance industry, the pensioner has no way of knowing whether the company will still be around when retirement time arrives.”

If a 40-year working life is not sufficient to fund retirement, what should we do?

“We need to offer a ‘Grant at Birth’ – each child gets a pension account at birth. For 70 years, the person will not have access to the money – it will be used intensively to rebuild