The Adequacy Pension Income Conundrum

David Spiteri Gingell[1]

Abstract. In March 2004, the World Bank presented to government a report on the robustness of the pension system. The report was dire. The World Bank projected that the Average Pension Replacement Rate - that is, the average pension in proportion to the average wage - would fall from 54% in 2004 to 14.1% by 2050. As the adequacy of the Maltese pension system collapsed, the cost of the pension system, in terms of the pension deficit as a percentage of GDP, was estimated to increase from (1.8%) in 2004 to (3.3%) in 2050. The World Bank underlined that unless comprehensive reforms were carried out the pension system was neither adequate nor sustainable for future generations. Malta's pension system is a Pay-As-You-Go system - introduced in 1979 following a major reform of the social security landscape. The social security contributory pension, as it is known, was established as the pension an individual is entitled to - resulting in the closure of a private pension market which was, then, vibrant. This article traces the development of the pension system in Malta by charting the 2004 reforms and adequacy followed by the 2010 changes and 2015 restructurings, whilst also asking whether Maltese households are addressing the adequacy pension gap, and whether automatic enrolment is a solution for the adequacy pension income conundrum?

Keywords: pension, income security, retirement, active ageing.

Introduction

In March 2004, the World Bank (WB) presented to government a report on the robustness of the pension system (PS). The report was dire. The WB projected that the Average Pension Replacement Rate (APRR) - that is, the average pension in proportion to the average wage - would fall from 54% in 2004 to 14.1% by 2050. As the adequacy of the Malta PS collapsed, the cost of the PS, in terms of the pension deficit as a percentage of GDP, was estimated to increase from (1.8%) in 2004 to (3.3%) in 2050. The WB underlined that unless comprehensive reforms were carried out the PS was neither adequate nor sustainable for future generations.

[1] Independent management consultant (david.gingell-dsg@gmail.com)

Malta's PS is a Pay-As-You-Go (PAYG) system - introduced in 1979 following a major reform of the social security landscape. The social security contributory pension (SSCP), as it is known, was established as the pension an individual is entitled to – resulting in the closure of a private pension market which was, then, vibrant. Between 1979 and 2003, the year preceding the WB's report, successive administrations failed to give due attention to the long-term performance and robustness of the PS at a time when its fundamentals changed significantly - namely, (i) the fertility rate collapsed, falling from over 2.1 to 1.4, and (ii), longevity increased from 67 years and 74 years of age for males and females in 1979 to 79 years and 84 years in 2003 (respectively). The Maltese PS is, theoretically, a two-thirds salary based pension calculated on the basis of the best consecutive annual three salaries over the last 10 years of employment - subject to a capped ceiling - the Maximum Pension Income (MPI) (The 2004 reforms changed this pension calculation formula for persons born on and after 1962 to the best 10 years over a 40 year contributory period). When the SSCP was introduced in 1979, the MPI was pegged to the salary of the President of Malta (the highest state salary at the time): €13,980. By 2003, the MPI increased only to €15,145 - that is, €1,165 over a 24 years period (€48.5 annually). As salaries increased as Malta enjoyed economic and social growth over the said period, the pension income remained constant - thereby negating the originally 2/3 or 66% relationship with the highest salary paid by the state. Furthermore, the actual value of the pension income was eroded by inflation as the PS did not allow for the MPI to be adjusted to counter inflationary pressures. Pensioners who retired in 2003 were, therefore, 'poorer' than their peers who retired in 1980.

In June 2004, the Maltese government established a technical group to study the WB report, and presented recommendations on the adequacy and sustainability of the PS for future generations. This initiated a process of continuing reform that is still underway today.

The 2004 reforms and adequacy

A strategic goal of the 2004 reform, one retained by subsequent reforms, was to secure an adequacy footprint for future generations, equivalent to that enjoyed by pensioners who were to retire between 2004 and 2010 - an APRR of 54% (Pensions Working Group, 2005). The 54% adequacy rate was seen as a reasonable retirement income benchmark that provides dignity to persons in retirement. It was, however, recognised that a 54% APRR will not secure a quality of life in retirement similar to that enjoyed whilst in employment. Nevertheless, in designing the parametric and institutional aspects of reform to the PS, it was evident that a 54% APRR for future pensioners achieved solely through the SSCP was not achievable. This was not a matter of simply safeguarding the sustainability of the PS. Increases in the contributory rate do not, given Malta's PAYG system, translate to a higher individual pension. Indeed, Malta's PS does not have a ring fenced pension fund where contributory benefits are invested to accrue a higher return to contributors - as contributions paid by beneficiaries are treated as government revenue posted to the Consolidated Fund. Moreover, Malta's PAYG system is not a Notional Defined Contribution (NDC) PAYG where the PS mimics a private pension by allocating individual notional accounts which compound over time by means of an assigned interest rate.

The 2004 reform stipulated that the maximum level of APRR that could be attained by the SSCP in a sustainable manner following parametric and institutional reforms was 45%. Amongst the important parametric changes to the SSCP was the introduction of an automatic indexation mechanism that annually adjusts the MPI by a formula of 70% Wage Inflation +30% Retail Inflation. The objective of this specific measure was to ensure that the pension income of future generations retains a strong link with inflationary impacts on market wages. Be that as it may, the parametric reforms still resulted in a state of play where the APRR of future pensioners (2050) was 9 percentage points (p.p.) lower than that of persons retiring between 2004 - 2010. It was argued at the time that bridging the gap between the maximum sustainable APRR secured through the SSCP and the desired adequacy benchmark of 54% through a voluntary third pension would not achieve the desired result. Research showed that when people are left by themselves, to provide for retirement, most will not save enough for retirement. In Ireland, for example, whilst 41.3% of the individuals working in the private sector aged 20 to 69 were covered by a voluntary private pension plan 31% were covered by occupational private pension plans, while only 12% were covered by personal pension plans. Similar rates of coverage for occupational pension plans were reported in Canada and the United Kingdom (OECD, 2013). The coverage of voluntary pension plans was, at time, also very low (below 5%) in countries such as Greece, Luxembourg, Portugal, and Turkey.

The low take-up of voluntary private pensions (including occupational retirement pensions - where, for example, in the United Kingdom showed a marked decline between 1990 and 2005) is a direct result of the types of heuristics that influence behaviour for generational planning as is the case with regard to saving for retirement. It was, therefore posited, that the 9 p.p. gap between the maximum APRR resulting from a sustainable SSPC and the desired APRR adequacy goal would best be secured through the introduction of mandatory second pension. The selection of a mandatory second pension instrument was strategically chosen to counter the impact of behavioural heuristics which impede persons from thinking long term and preparing for their retirement. The recommendation presented was that an employee and an employer would each pay an additional contribution of 4% annually - incrementally phased over an 18-year period to give both employees and employers time to adjust. The reforms further underlined, that individuals should be provided with opportunity and choice to invest for their retirement in the event that they sought an APRR higher than the 54% benchmark provided by a combined SSPC and a second mandatory pension. Indeed, in 2004 the pension regulatory framework still prohibited an individual to have a second pension. The reforms also proposed the introduction of comprehensive framework for persons to prepare for retirement - from child pension accounts to home equity release; the latter seen to be of specific importance in Maltese society as home ownership is high - with over 76% owning a home, which according to the 2011 Census, over 80% are of a high quality. The reaction by both enterprise and unions to the introduction of a mandatory second pension was negative. Enterprise underlined that the targeted 4% new contribution would undermine competitiveness whilst unions argued that, in the here and now, disposable income will be reduced. The opposition also positioned itself against a mandatory second pension. The government too came out against this

recommendation - responding to the general societal negative response in the run up to a general election which had to take place by early 2008.

In many ways, the 2004 reforms resulted in cherry picking. The recommendations relating to key parametric reforms to the SSCP, which secured the 45% APRR, were introduced effective 1st January 2007. The complementary reforms to (i) ensure that future generations (which reforms defined to be persons born on or after 1962) retire at a pension level similar to persons retiring between 2004 and 2010; and (ii) providing persons with the right to invest for their retirement to secure an income higher than that provided by the SSCP were rejected. Other 2004 reform measures merit mention. First, a safety net was proposed to protect future pensioners from being at-risk-of-poverty (AROP). This was to be secured by means of a Guaranteed Minimum Pension - benchmarked to 60% of the median income. This recommendation was accepted. Second, to avoid a repetition of policy paralysis in the pension policy domain a trigger was proposed to be grafted onto the Social Security Act (SSA) for the carrying out every 5 years of a strategic review on the sustainability, adequacy, and solidarity of the PS. This recommendation, too, was accepted with first strategic review mandated to take place by the end of 2010.

The reforms also included flanking policies. Two such policies, which affected the adequacy of income levels in retirement of both current and future pensioners, were key. The first relates to the removal of a constraint at law that restricted persons from continuing to work whilst in retirement as they would otherwise forfeit their pension. At the time the number of retirees active in the labour market was negligible. The second relates to measures directed to increase female participation in the labour market. Due to local cultural and traditional norms, the majority of households benefited from only one pension income - primarily that of the male spouse who in the Maltese polity is the main bread winner.

The 2010 reforms and adequacy

The 2010 Strategic Review triggered by the newly introduced Article 64B of the SSA confirmed that the attainment of a 45% APRR by SSCP was on track (Pensions Working Group, 2010, 2012). Given that the review was carried out within the midst of the financial and economic crisis a critical question that it grappled with was whether a mandatory second pension remained a viable option. The 2010 review posited that the "question relating to the introduction of a second mandatory pension must be answered with regard to the knowledge and certainty that an APRR of 45% will not be adequate as against the uncertainty on the global economy and behaviour of the financial markets as well as its impact on the national economy".

The review concluded that a decision to postpone further a mandatory second pension would only exacerbate the issue relating to the adequacy of the APRR; requiring drastic measures in the near future. The review recommended that the government should seek to introduce a mandatory second pension at the earliest possible - and not later than 2018. The review, however, emphasised that the framework for a mandatory second pension should take on board lessons learnt from the economic and financial crisis - embracing mechanisms

such as a default fund based on a lifecycle investment strategy to provide protection to those persons who do not or are unable to decide how to invest and to manage that investment over their working period. Once again the recommendation to introduce a mandatory second pension was rejected by government, the Opposition, enterprise and the unions - the reactions similar to those presented in 2004. The 2010 review, again, underlined the importance of introducing a third pillar framework incorporating occupational and personal pensions, home equity release, etc. at the earliest possible so that individuals are provided with the opportunity and choice to provide for a quality of life in retirement that closer reflects that enjoyed whilst in employment. Once again, whilst accepting the recommendations no action was taken by government.

The 2015 reforms and adequacy

The 2015 strategic review was triggered by the incoming new administration within months from being elected in March 2013 (Pensions Strategy Group, 2015). The incoming government, whilst declaring the technical team to be independent, made it clear that it would reject recommendations that went contrary to pledges made in the electoral manifesto - mainly (i) the 65 years statutory retirement age will not be increased but rather that persons will, mainly, through supporting policies be encouraged to work beyond the statutory pension retirement age; and (ii) no mandatory second pension will be introduced. The main report targeted four aspects - namely, (i) changing needs and issues relating to society and the labour market; (ii) retaining a fair balance between contributions and benefits across generations; (iii) reforms to ensure that the pension income is not the only source of income; and (iv), addressing challenges faced by current pensioners. The 2015 reforms also assessed the possibility, with the assistance of the WB, to migrate the PAYG PS to a NDC PAYG system (recommended in the 2010 review for study). The review concluded that the benefits stemming from such a complex transition were too small to mitigate the risks associated with such an institutional framework overhaul. With regard to adequacy, the 2015 reforms presented five key trusts:

- First, in 2014 recommendations were presented for the introduction of a third pillar pension. The underlying fiscal incentive framework was designed to bridge the 9 p.p. between the 45% APRR SSCP footprint and the 54% APRR benchmark. The review also recommended that the government should work with the financial services industry and employers so that a Voluntary Occupational Retirement Pension scheme (VORPS) is introduced. Both recommendations were accepted. The first private pension products were placed on the market in late 2015; and in 2017 the government issued a tax incentive framework for VORPS.
- Second, with particular regard to future generations, a behaviour inducing scheme directed to incentivise people to work up to 65 years of age rather than opting for early retirement at 61 years of age was introduced - with an individual accruing an additional 23% on their pension income, if they retired at 65 years of age (during which period they do not draw down their pension). This recommendation too was accepted; though it is currently limited to employees in the private sector.

- Third, the primary focus of adequacy and pension income was directed towards current pensioners. Although the recommendations as presented in the review were not accepted by Government in the 2016, 2017, and 2018 budgets the government introduced a spate of measures directed to improve the pension adequacy of current pensioners – primarily with regard to those pensioners who are AROP.
- Fourth, the government took on board a recommendation that secured a female the full pension income of her spouse in the event of his death rather than 5/6ths survivor pension in the event that she qualifies for a pension in her own right.
- Finally, the 2015 review reaffirmed the recommendations presented in the 2010 review that a retirement and financial capability strategy is designed and implemented to inculcate, amongst others, a culture of retirement planning and action.

One other important reform relating to adequacy introduced by government in the 2017 and 2018 budgets was that of rendering pension income for single and married households to a maximum of €14,000 to be tax free.

Are Maltese households addressing the adequacy pension gap?

Research on the extent to which Maltese households are planning for their retirement to ensure that they have a retirement nest egg that provides them a level of adequacy beyond the 45% APRR provided by the SSCP is limited. Nevertheless, converging different empirical data leads one to conclude that, in the main, Maltese persons are not preparing for their retirement.

A study by Caruana and Pace (2013) estimated households' net wealth, which is defined as the sum of real and financial assets net of financial liabilities, at a median value of €215,932. The survey further showed that the main residence accounted for 51% of household wealth in the form of real assets. Furthermore, the share of the main residence in the net wealth of those households in the highest 20% net wealth percentile was lower, contributing about 30% to their total real assets. For the lowest 20% percentile in net wealth terms this was more than half. The survey further showed that a higher level of net wealth was reported when the reference person in the household was a university graduate or self-employed or was aged within the 55 - 64 age bracket. The median net wealth of households represented by reference persons with tertiary, secondary and below-secondary levels of education respectively was found to be €319,994, €226,126 and €129,469 respectively. The survey demonstrated that the median for net wealth, of all households, the median for households represented by a self-employed person was 2.5 times higher. The median net wealth of households whose reference persons were aged between 55 and 64 years was €272,625, and the overall median value of holdings of financial assets was estimated at €26,229. The median value of financial asset holdings was found to vary with the educational attainment and work status of the reference person representing the household. For example, households whose reference person was an employee accounted for 36% of all households and owned financial assets with a median value of €29,769, while households whose reference person was self-employed persons representing 8% of all households, held financial assets with a median value of €68,856. The median financial asset holdings for

retired persons (27% of all households) stood at €28,906. Households with a primary level of education (23% of all households) owned financial assets with a median value of €17,015; those with a secondary level (62% of all households) held financial assets with a median value of €25,407, while those holding a university degree (15% of all households) owned financial assets with a median value of €54,029. The study concluded that 76.3% of households in Malta do not save - with only 23.7% of households being net savers with a median annual savings of €3,000, and an average saving level of €4,400. Other research carried out by Galea (as cited in Ministry for the Family and Social Solidarity, 2017) on attitudes towards retirement found that 64.0% of persons in Malta do not give any thought to the level of savings they should have given their desired retirement age and life expectancy; although 70% of respondents state that the SSCP will only provide sufficient income to pay for bare necessities. Additionally, of those who do think about the level of income they seek in retirement, 52.4% state that they require the same level as pre-retirement income whilst 9.5% state that they do not know (ibid.). Moreover, most of the respondents in a survey on financial literacy state that they do not hold a specific savings plan for retirement - whilst those who do invest for their retirement invest approximately €1,161 annually - or €97 per month (Mangion, as cited in Ministry for the Family and Social Solidarity, 2016).

Is the third pension framework meeting its objective of nudging sufficient persons to bridge the 9 p.p. deficit by investing in it? Whilst it may be early to pronounce judgement the following should be noted. The take up of the personal private pension products is disappointing. In 2015, there were 344 pension members, which increased to 1,446 (increase of 1,106 on 2015) by 2016, and 2,255 (increase of 809 on 2016) by 2017. The response to the VORPS framework by employers has, so far, been cold. One of the big five consultancy firms withdrew from establishing VORPS as a service line for employers and concluded that the framework was not sufficient attractive to introduce a VORPS for its own staff. On the plus side, the following is to be taken into account. The 2004 reform directed to incentivise persons past their retirement age to be active in the labour market was successful. Today there are over 11,152 persons who are of retirement age and who continue to be productively engaged in the labour market. Female participation in the labour market increased from under 30% in 2004 to 53.8% in 2015 - with female participation in the 25-54 age bracket standing at 65.8%. This means that whilst today most retired households depend on one pension - the pension of the single spouse who was the main breadwinner- the majority of future retired households will benefit from a combined retirement income consisting of a pension received individually by both partners in a household. Despite that to date no formal home equity mechanisms are introduced, informal equity takes place - many elder households release their home to private operators of elderly care residences in exchange for placement in such residences. In the 2018 budget the government announced the formulation of a working group to present recommendations on an equity release framework for Malta - which can provide options that allow households to transform home assets into income whilst continuing to live in their homes. Be that as it may there are, however, strong indications that future generation are less likely to be home owners' than their parents' generation. The number of rentals by local persons is on the increase - in part

fuelled by ever increasing costs of residential property which is discouraging young persons from being their own property owners.

Maltese society has a strong culture of handing down wealth from one generation to the next. Many households today are likely, to some extent, to boost their retirement income from inheritance. Although there is no empirical evidence Malta is expected to follow the pattern of other European societies where the passing over of wealth from one generation to the next decreases as future Maltese households are likely to be relatively poorer than previous generations. On balance, it is concluded that future generations are likely to have a lower wealth profile than their parents and the evidence in hand, insubstantial as it is, suggests that young persons are not taking action to have a retirement nest egg that allows them to bridge the quality of life in retirement as close as possible to that enjoyed whilst in employment.

Automatic enrolment: A solution for the adequacy pension income conundrum?

The strategic review inherent in the *Strategy for an Adequate and Sustainable Maltese Pension System* (Pension Strategy Group, 2015) recommended:

> The Supporting Retirement Pension Scheme that is to be introduced in 2014 may be subject to heuristics which will influence behaviour with regard to long term planning and savings, particularly given that the scheme is completely voluntary. The Pensions Strategy Group recommends that during 2020 Strategic Review, the proposed pension commission (Recommendation 10) should carry out an in-depth review on the performance of the scheme. In the event that the Review shows that voluntary pensions would not have delivered as planned, it should strategically assess the introduction of Mandatory Opt-In Voluntary Opt Out framework, which would see the employer responsible for managing the administration aspects of the scheme… (Pension Strategy Group, 2015 : 100).

As discussed above, early evidence of the performance of the personal private pensions shows that, given the small number of schemes issued, up-take is impacted by behavioural heuristics. The financial incentive offered to employers to introduce VORPS in their workplaces has, so far, gained no traction. Automatic enrolment (AE) is a possible solution towards addressing the adequacy pension income conundrum - therefore, is a creative innovation. The principle of AE turns behavioural heuristics, in particular inertia, on their head, for under a purely voluntary scheme inertia affects a person in a way that it inhibits them from enrolling. Even if a person believes that becoming a member of a voluntary workplace pension is important to them, they may keep differing taking action as more immediate and pressing matters require their immediate attention. Under a voluntary workplace pension based on AE, inertia works on inhibiting the person from opting out of the PS once they are enrolled. The same inertia that propels a person to procrastinate enrolling in a voluntary pension scheme now restrains the person from opting out once enrolled. AE schemes, such as those introduced in New Zealand (Kiwi Saver) and the United Kingdom (NEST), show that these are successfully meeting their objectives of engaging, and retaining over time, individuals to save for their retirement.

Invariably, the question arises whether - given the controversy that has, since 2004, surrounded mandatory second pensions - a political and social climate exists in Malta for the introduction of AE as a vehicle to address the adequacy issue. The answer is, yes, if only, however, the AE PS is designed to carefully address the concerns raised by stakeholders when rejecting the introduction of a mandatory second pension. It is therefore argued that for an AE PS to work within Malta's social and political milieu it should be based on a number of critical design elements. These are discussed below.

Targeted audience

The AE scheme targets middle income earners. As mentioned earlier, to take account of retail and wage inflationary pressures, the MPI for future pensioners has an automatic indexation mechanism. This indexation came into effect in 2013. Since then, the MPI for those born on and after 1962 increased from €20,964 to €22,803 in 2017 (when compared to the MPI of current pensioners which increases on the basis of a cost of living adjustment which increased from €17,475 to €18,024 over the same period) - an average annual increase of €460. Persons born in 1962 retire at the age of 65 years in 2027. Extrapolating the annual €460 increase to 2027 sees the MPI rise to €27,403. The maximum pension that a person is eligible to on retirement is €18,268. A person earning €30,000 in 2027 will see their income in retirement fall at best by €11,732. An AE should target persons who are (i) 18 years of age or over; (ii) 55 years of age or under; (iii) earn a gross wage or salary that is €18,268; and (iv), joining the labour market as well as persons who are already employed within the age ranges indicated above.

Exempting vulnerable groups

Financial capability is a central social policy concern as lack of financial knowledge, ability, opportunity and assets contribute to poverty and inequality. Research shows that the priority with such persons is less that of making sure that they save for their retirement but rather of providing them with the knowledge and education for them to manage their budgets more efficiently and wisely with financial guidance on money management during unemployment, separation and divorce, debts, priorities and choices, home foreclosure, or when facing long-term financial instability, such as poverty, disability, chronic illness, etc. People in lower income do save - but they do so more to have a small financial cushion for a rainy day or for personal consumption - such as a family holiday. The referenced CBM study shows that people with a level of education below secondary have an annual savings or a surplus of €750 - lower than €3,000 and €4,088 held by persons who hold secondary and tertiary education respectively. Additionally, the median household debt burden for persons with a level of education below secondary education is non-mortgage debt - €6,515. This contrasts with persons holding secondary and university education respectively, who although holding a level of non-mortgage debt, the primary debt is mortgage debt. Persons whose wage is below the MPI enjoy a higher pension than persons whose wage is above the MPI as they obtain the full 2/3 entitlement. Persons who are on a relatively low income should, therefore, be excluded from mandatorily opting into an AE. Whilst they should be

afforded the choice to opt in they should be counselled on the impact that the monthly contribution payment will have on their monthly household budget. An AE scheme should exempt persons (i) whose wage is lower than €18,268; or (ii) are 55 years and over; or (iii) are in temporary or casual employment; or (iv), work less than 40 hours.

The right to opt-out

An employee who is automatically enrolled into an AE has the right to opt-out. The employee should be presented with a reasonable time period to exercise their judgement on whether they exercise the right to opt out - for example, between a period ranging from 60 to 90 days from when they are employed or enrolled.

Contributions paid by eligible employees

The AE scheme is based on the premise that an eligible employee will upon automatic enrolment invest in their pension fund. To render savings in their pension fund meaningful the minimum contribution level is set at 3% of their gross salary or wage. Employees should have the opportunity to increase their contribution rate to 8% of their gross salary or wage should they voluntary chose to do so.

No obligation placed on the employer to contribute to the employee's pension fund

The AE scheme is designed in a manner that places no obligation on the employer to contribute to an employee pension fund under the scheme. An employer should be nudged to play an active role in an AE scheme through (i) a well-designed fiscal incentive scheme; and (ii), collective bargaining.

Obligation placed on an employer with regard to an automatic enrolment pension scheme

The obligations of an employer under the AE scheme should be only limited to the administrative aspects of the PS. These include mainly:

- Automatically enrolling an eligible employee.
- Enrolling any employee who so requests.
- Affecting an opt-out notice.
- Deducting the contribution from an eligible employee's gross salary or wage and transferring that contribution to the administrator responsible for pension plan chosen by the employee.
- Refunding the employee the contributions deducted from their wages or salaries from the date of their enrolment and when the opt-out notice is affected.
- Providing employees with a choice of AE pension schemes - which can either be tailored designed specifically for the employer or generic ones provided by the financial services market.
- Providing information to employees prior on retirement planning.

Contribution deduction holidays and permissible withdrawal of accumulated funds

The AE pension scheme is based on the principle that once a person opts in they remain locked in. This is an important principle as it ensures that the individual truly accrues a reasonable retirement nest egg for their retirement. There are instances in an individual's or family's lifecycle, however, were circumstances do not permit them to save or leave them with little option but to dip into their savings. An AE PS, therefore, should be designed to take into account such circumstances. Thus, an AE PS should include (i) a contributions deduction holiday, for example of 12 months, due to arising circumstances such as financial hardship, ill health, study, etc.; (ii) withdrawal of 'n' months of contributions made including a percentage of accumulated profit for reasons such as purchasing a residential property; financial hardship; or serious illness; and (iii), opting out in the event of emigration.

Protecting retirement savings in an AE PS

The 2008 economic crisis clearly showed that many members of defined contributions' PS were incapable of choosing the appropriate investment strategies and that most members failed to manage the risk exposure of their pension investment the closer they got to their retirement age. Indeed, analysis of the financial crisis shows that those persons who had shifted their investment strategy from equities to bonds closer to their retirement suffered limited consequential losses whilst persons in similar age groups who failed to adjust their risk by shifting to bonds had their pension investment significantly negatively affected. An AE PS should automatically seek to protect members by mandating that any qualifying scheme should have (i) a default profile option; and (ii), employees on enrolment are automatically placed on the default investment profile of a pension

Conclusion

The reforms carried out since 2004 result in significant innovation and solutions addressing specific issues relating to the PS and its flanking environment - short to medium term sustainability, balancing the inherent gender discrimination of a PAYG PS, reducing early invalidity exit, increasing number of retired persons in the labour market, establishing a balance amongst current and future generations to mention a few. The reforms managed to break the adequacy pension income collapse forecasted by the WB - stabilising the APRR for future generations to 45%. This, however, as shown, is 9 p.p. below that enjoyed by persons retiring between 2004 and 2010. Recommendations to bridge this gap by means of a mandatory second pension resulted in societal and political negative reaction leading to its rejection. Early indications are that bridging this gap through voluntary private and occupational voluntary pensions are not resulting in a large population coverage. This means, that for many, the pension income through the SSCP will not act as a sufficient bridge to secure a quality of life in retirement as close to that enjoyed whilst in employment. This paper posits that the time has come for Malta to consider alternative means of how to address the adequacy pension income conundrum. An AE PS cleverly designed to address

societal and political issues raised with regard to a mandatory second pension is seen as a solution to break the deadlock in this regard.

References

Caruana, K., & Pace, C., (2013). *Household finance and consumption survey in Malta: Main results of 2010 exercise*. https://www.centralbankmalta.org/file.aspx?f=883. Accessed 8 March 2018.

Ministry for the Family and Social Solidarity. (2016). *Draft National Strategy for Retirement Income and Financial Literacy: 2016-2018*. https://family.gov.mt/financial-education/the-commission/Pages/The-Draft-National-Strategy.aspx. Accessed 8 March 2018.

Ministry for the Family and Social Solidarity. (2017). *National Strategy for Retirement and Financial Capability, 2017-2019*. http://family.gov.mt/financial-education/Documents/Document%20ENGLISH%2021.01.17.pdf. Accessed 8 March 2018.

Pensions Working Group. (2005). *Social impact assessment - White Paper "Pensions – Adequate and Sustainable"*. http://family.gov.mt/financial-education/publications/Documents/Social%20Impact%20Assessment.pdf. Accessed 13 March 2018.

Pensions Working Group. (2010). *Strategic review on the adequacy, sustainability and social solidarity of the pensions system*. http://family.gov.mt/financial-education/publications/Documents/Malta_Pensions_Strategic_Review_2010.pdf. Accessed 13 March 2018.

Pensions Working Group. (2012). *Final report: Strategic review - Outcome of the consultation process and proposed next steps*. http://family.gov.mt/financial-education/publications/Documents/Final%20Report%20Strategic%20Review%20-%20Outcome%20of%20the%20Consultation%20Process%20-%202011.pdf. Accessed 13 March 2018.

Pension Strategy Group. (2015). *A strategy for an adequate and sustainable Maltese pension System*. https://socialsecurity.gov.mt/en/Pensions-Reform/Documents/Pensions%20Report.pdf. Accessed 8 March 2018.

Organization for Economic Co-operation and Development. (OECD). (2013). *Pensions at a glance 2013: OECD and G20 Indicators*, OECD Publishing. http://dx.doi.org/10.1787/pension_glance-2013-en. Accessed 8 March 2018.