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Tel. +41 44 234 85 00

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News Release

UBS International Pension Gap Index: Voluntary savings matter

UBS's latest International Pension Gap Index compares retirement systems across 25 markets based on the voluntary savings efforts required from its participants. It finds that private savings are crucial to maintain an accustomed lifestyle in retirement in many systems. Furthermore, it showcases the importance of retirement planning and stresses that investments can often help close pension gaps.

Zurich, 16 October 2024 – The International Pension Gap Index, published by UBS Global Wealth Management's Chief Investment Office, analyzes the mandatory part of 25 retirement systems, focusing on the benefits a worker can expect and the additional savings required to maintain an accustomed standard of living in retirement. Specifically, the study benchmarks retirement systems based on the savings effort required by a fictional character, measured by the share of current after-tax income that a female employee must save every year from age 50 until retirement, assuming she has no prior savings.

The results differ widely from city to city. For instance, private savings are not required in Amsterdam whereas they amount to an impossible 93% of wages in Tokyo. That's mainly because the Japanese system doesn't aim to replace a high share of labor income, whereas the Dutch one does – which is also reflected in its comparatively high retirement contribution rates. Also, the Japanese spend 50% more time in retirement than their Dutch peers as they retire earlier and live longer lives.

Unlike in the Netherlands, private savings are necessary to secure a given post-retirement standard of living in most cities around the world. How much depends on the design of the respective retirement system. While some require a low personal engagement from their participants, others put a greater emphasis on personal responsibility – i.e., they don't aim to maintain an accustomed standard of living.

Retirement benefits are rarely certain

Even when expected retirement benefits are high, they can be uncertain when they rely on the performance of financial markets or when the promised benefits are based on outdated demographic and financial parameters. That's especially true for some defined benefits schemes, which may not be able to deliver on their promises as they become more misaligned with actuarial reality. In particular, as the large cohort of baby boomers retires, existing unaddressed imbalances are set to widen in ailing pay-as-you-go financed schemes. To keep these schemes financially afloat without curtailing the pensions of current retirees, today's workers may be required to foot most of the bill. As a result, the authors argue that precautionary savings are recommended to ward off the inherent uncertainty of policy change.

There is such a thing as sustainable pension schemes

Yet, some countries have successfully taken measures to address the financial woes of basic pension schemes relying on a pay-as-you-go mechanism. For instance, Sweden's Income Pension features a sustainability backstop that conditions the indexation of pensions to the scheme's financial equilibrium." Looking at what has been implemented in some countries shows us that increasing the resilience of retirement systems without compromising on adequacy is possible," argues UBS economist Elisabeth Beusch.

The importance of retirement planning

In some cities, the estimated required savings rate exceeds a median income earner's savings potential by far. When confronted with that reality, one possibility is to reduce one's lifestyle to be able to afford it into retirement. Retiring later or relocating to a cheaper location upon retirement are also possibilities. However, these uncomfortable decisions can usually be avoided when one starts saving from an earlier age.

While saving is a necessity, investing can help a great deal even if it comes with risks. For instance, the authors argue that in Switzerland, investing savings in a diversified portfolio of bonds and equities will lead to better financial outcomes than cash nine times out of 10. Furthermore, relying solely on cash in Switzerland would increase the required savings rate by a third." Far from being reckless, investing savings in view of retirement can help workers maintain their accustomed lifestyle in old age," explains UBS economist James Mazeau.

Should women plan differently?

Retirement systems are usually gender agnostic – save for when women can retire earlier than men with the same level of benefits. Nevertheless, women tend to pause their careers and work part-time more often than men to take care of children, for instance. As a result, they often experience lower wage growth, accumulate fewer retirement benefits, and save less across their working lives. Furthermore, they tend to live longer lives than men. As a result, women usually have fewer retirement resources to finance longer retirement periods. This means that women's required savings efforts are usually higher than those of men.

Links

UBS International Pension Gap Index

About UBS

UBS Switzerland AG

Media contact

Switzerland:	+41-44-234 85 00
UK:	+44-207-567 47 14
Americas:	+1-212-882 58 58
APAC:	+852-297-1 82 00

www.ubs.com/media