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The 14th Economic International Conference: Strategies and Development Policies of Territories: International, Country, Region, City, Location Challenges | May 10-11, 2018 | Stefan cel Mare University of Suceava, Romania

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The 14th Economic International Conference: *Strategies and Development Policies of Territories: International, Country, Region, City, Location Challenges* | May 10-11, 2018 | Stefan cel Mare University of Suceava, Romania

## The Demographic Trends on Pension Systems in Romania

Tudor COLOMEISCHI<sup>1\*</sup>, Eugenia IANCU<sup>2</sup>

### *Abstract*

*Within national pension systems, the role of private pensions tends to become increasingly important. In support of this idea, we recall the conclusion that has been made by research that has taken place over time that the value of private pension fund assets has risen on average by 11.5% annually. The impressive value of assets becomes extremely tempting for investors who see extremely good long-term investment opportunities if we consider the amounts traded.*

*The Romanian pension system has entered a continuous process of change, not always with positive consequences on the level of pensions. The truly significant reforms have only emerged since 2000, being favored by the country's accession to the European Union. Unlike other states, in Romanian the 2008 crisis affected the pension system especially in its public component.*

*Private funds have resisted fairly well the problems that have arisen, partly because of the extremely prudent investment policy. The paper attempts to capture the pressures on pension systems, also making a series of forecasts on future developments in different hypotheses of the economic and social context.*

### **Keywords:**

*Pension system, demographic trend, pension strategies, risk of longevity.*

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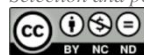
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## 1. Introduction

A defined benefit (DB) pension system implies that each active generation should economically support the generation that preceded it. The active population is subject to continued pressure from the retired population to increase the benefits of the public pension system without any direct link with their previous contributions to the system. Thus, the active population fears that when they retire, the public system will not be able to give them the same support they currently grant to the current generation of pensioners.

The current generation of contributors to the public pension system also faces the economic and financial pressures generated by the globalization process that affects most of the world's countries as well as other economic pressures and tensions and is not willing to allocate larger parts of personal income to support the previous generation, preferring to invest in the current standard of living or in the education of the next generation.

The solution adopted by most states, including Romania, to prevent these effects was the implementation of a privately managed defined contributions (DC) pension scheme that would provide the public with a decent pension. The private pension system is complementary to the public system and should together ensure a reasonable rate of return on income.

## 2. Sustainability of the pension system

A fair but at the same time very simple assessment of the sustainability of the public pension system in the economic and financial context in Romania can be done by analyzing the expenditures on pensions and the earnings from the contributions of employees and employers. For the future, if the value of the ratio between income and expenditure is positive, we can see that sustainability is ensured in the medium and long term; but if the value of the report is predicted to be negative, so with a revenue shortfall and an increase in spending, there is a need to find financing solutions for the system.

The main factors influencing the sustainability of the pension system are the following [1]:

- The demographic component, including the number of taxpayers and beneficiaries, as well as the forecasts related to their evolution over time;
- Medium salary;
- Rate of contributions to pension funds;

- Economic growth and GDP respectively.

Regarding the demographic component and its forecasts, the following can be made:

- The elderly population (over 65) has continuously increased, both numerically and in percentage terms. At the same time as the number of pensioners increased, there was a decrease in the number of the employed population. In this context there has been an increase in demographic dependence.

- The design of the population of Romania in the hypothesis of maintaining the current conjectural index of fertility (1.3) predict an inevitable demographic skew, which will be installed after 2025-2030, with the ages of 20-40 years by the reduced number of generations , born after 1989.

- The number of women of childbearing age will decrease continuously until 2025. Numerical growth started in the 1980s, due to the entry into fertile age of women of many generations born after 1966, diminished year after year.

At present, the number of contributors and pension beneficiaries is dependent on demographic change and economic growth, as they are the basic components that can influence the financial projections and the future of the public pension system.

### **3. Demographic Trends**

Age of retirement (or retirement) is the most visible parameter of the pension system. The increase in retirement age has proven to be among the most controversial measures of pension reform. It is defined as the age at which people can start to fully cash their benefits and is generally clearly stated in the country's legislation. However, in some cases early retirement is possible without an "actuarial" reduction in the pension, but additional conditions are set for contributions. There are also states that instead of a retirement age set a timeframe for people to start collecting the pension. In other countries, such as Italy or Turkey, retirement is based on the number of contribution years or the age of entry into employment, which is considered to be 20 years of age. Also, in Sweden and Finland there are no standard retirement ages, but only 65 years of age from which benefits can be accessed under resource-based retirement schemes.

Estimates made in the past about the increase in life expectancy (especially at retirement age) have often been found to be wrong, being

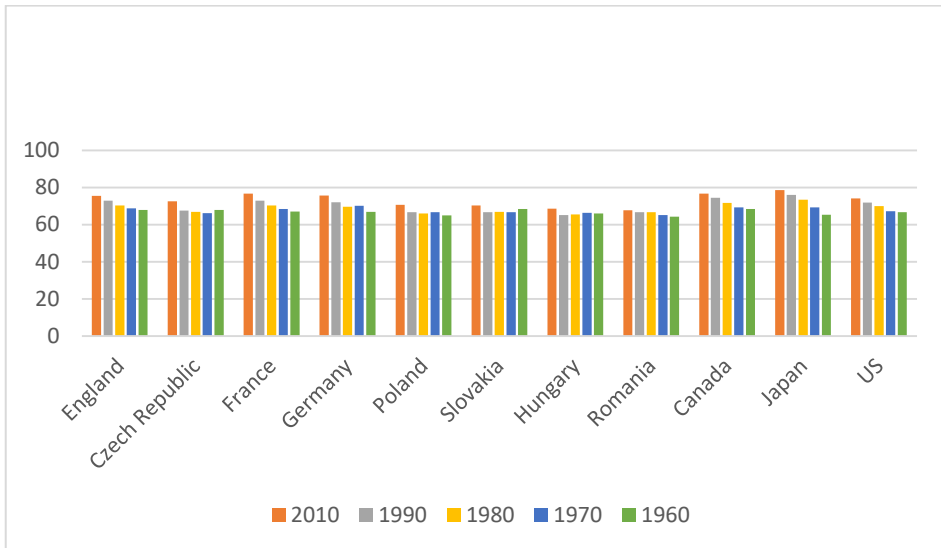
largely underestimated. Changes in parameters and computing rules have been successful only in the short term, requiring repeated reform measures.

It is quite surprising that some states have formally adopted the most obvious form of the link between retirement and life expectancy: increasing the retirement age as people live longer. In Denmark, the retirement age will increase from 65 to 67 years by 2027. Instead, Italy and Greece will do so by 2015 and 2020, while allowing retirement at any age of those with 40 years of contributions.

The UK's Pensions Commission has proposed a 2020 increase in the age of eligible retirement pensions that will keep life expectancy at retirement. The previous government had instead proposed a pre-announced program of staggered retirement ages, from 65 to 66 from 2024, then from 67 years from 2034 and from 68 years from 2044. Nor did it we have an "automatic" link with life expectancy.

France has established a link between the numbers of years of contribution needed to retire and changes in life expectancy, with a gradual increase from 40 contributing years (between 2003 - 2008) to 41.5 years in 2013. The link is not as strong as in other cases, the aim being to maintain a constant relationship between the length of the retirement period and the length of the career. In this way, additional years of life expectancy will increase the period of activity.

**Figure 1** Evolution of life expectancy at birth for men (years)

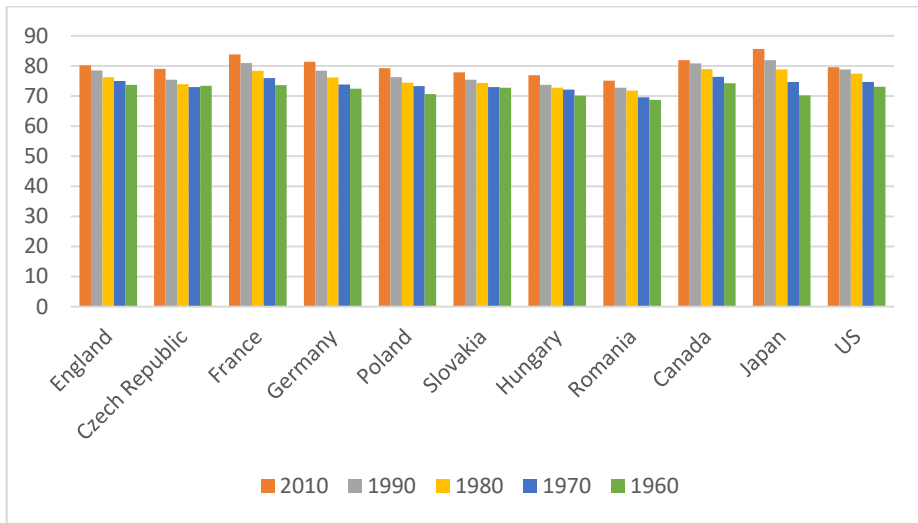


Source: [www.oecd.org](http://www.oecd.org)

In Europe, in the year 1990 there were 500 million people over 65, while their number will reach 1.4 billion in 2030. Life expectancy will also increase by nearly 5 years by 2050, year 2000. Thus, starting from a current life expectancy of 65 years of age for 15.5 years for men and 19.5 years for women, the 5-year increase will bring about an increase in 25- 30%.

Taking into account the fact that many generations born after the Second World War are going to retreat, the phenomenon of aging populations is giving rise to a growing concern among European states.

**Figure 2** Evolution of life expectancy at birth for women (years)



Source: [www.oecd.org](http://www.oecd.org)

In the following two figures we presented the evolution of life expectancy at birth (for men and women respectively) in several countries in Europe, North America and Asia.

It can be noticed that the growth rate of life expectancy may be different, even between developed countries, as shown by comparing US and Japanese data.

The increase in life expectancy was driven by improved living and education levels and medical discoveries. They are obviously a social benefit, but they also require additional effort from governments and active people to support their pensions for longer [2].

The phenomenon of reducing the mortality rate that cannot be anticipated is called the risk of longevity [4]. The risk of longevity has a major influence on the state, employers, employees and life insurance

companies that "must ensure that a longer life represents a benefit to society and does not turn into a financial burden," said Christian Mumenthaler, expert SwissRe Reinsurance Company.

In addition to increasing life expectancy, another cause of the aging population was the downward trend in fertility rates in recent years [3]. Thus, it can be said that they have fallen from an average of 2.26 in OECD countries to 1.65. However, as predicted by the OECD, a slight increase is expected in the next period, reaching 20 in the 2045-2050 at a level of 1.8.

#### 4. Conclusions

Given that birth rates decrease dramatically and people's average lifespan increases, aging populations is a major risk factor for the whole of Europe. Romania not only makes no exception, but it has one of the most pessimistic perspectives in this respect, partly due to the large number of emigrants leaving the country. Consequently, as the public pension system is designed, an employee will have to support more and more retirees on a monthly basis. If the ratio is currently 1 employee to 1.3 retired, in 2050 an employee will have to financially support more than two retirees. A possible identified solution is to empower people by saving and personal accounts, as well as financial planning to withdraw from work so as to ensure decent old age. These objectives are only possible through strong support for the expansion and development of the private pension system.

Older people make up a disadvantaged population in many respects, namely economic and financial resources, social inclusion, and the opportunities to carry out their dignity and autonomy. These, as well as young and mature taxpayers, depend to a large extent on the presence, permanence and stability of a consolidated pension system that can provide them - now or after a certain amount of time - with a living standard better.

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