Forced Savings and Annuitisation with Cross-Subsidies: A Mutation of the Beast

We adopt a two-tiered economic approach to classify national retirement savings schemes. We extend the plain vanilla system of forced savings by allowing for annuitisation and cross-subsidies. The first tier of our model is controlled by government, which mandates contribution rates, interest rates, and conversion into benefits. In contrast, agents make voluntary contributions in the second tier, which earn interest at a rate broadly reflecting market conditions and any cross-subsidy between both tiers. Cross-subsidies within the mandated tier and between both tiers allow for social redistribution as well as the creation of a liquid market of privately provided annuities. We conclude with a discussion of the Swiss and Australian systems of retirement savings as seen through the lens of our model.

This is joint work with Dr Benjamin Avanzi (UNSW).

Working paper can be obtained from http://ssrn.com/abstract=1466386