An idea for the revitalisation of Europe: consistent retirement funding

At the moment the economies of the world are controlled by retirement funding. This fact could have been well-known since the economist Lester Thurow stated as early as 1992 in *Head to Head, The Coming Economic Battle Among Japan, Europe and America*: '(…) pension and mutual funds owned only a small fraction of the total number of shares outstanding. But today they own 60 to 70 percent of the shares of most publicly listed companies.' Nowadays the seven countries with the largest investments for retirement together own together USD 37,773 billion. But someone who wants to start a grocery in small town in Eastern-European, in order to counter the necessity of transport and make Europe more sustainable, will find investments impossible to find.

Economic and social problems since 1989, and in particular after 2008, have been attributed to neoliberalism, the collapse of the Iron Curtain, austerity, not enough austerity, high and low taxes and a too large public sector. But the political management of the tax-deferred retirement investments is the real cause of European problems. It has become urgent to solve puzzles such as those surrounding the climate, the social changes after 1989, the questions of aging, the position of the middle class and the retirement of the owners of small companies. The issues demand investments as well as a different approach of capital-based retirement funding. The base has to be in order. Wouldn't it be a good idea to gradually creat a large European Retirement Investment Fund, with a capital of at least one trillion euro (a thousand billion euro) as goal, to start with? We, the Stichting Intergenerationeel Overleg, thinks so.

Our idea is:

- To create a large economical, ecological and social sustainable European Retirement Investment Fund, controlled by the European Commission.
- Make it possible for all Europeans and those organizations that wish so, to invest, tax deferred, in Eastern Europe, smaller companies, depopulating areas, green and sustainable technologies, natural farming, and sustainable production.
- If necessary, change the Treaty of Maastricht and limit the tax-deferred retirement investments to Europe and those that are in the interest of the European tax payers.

Investing in listed companies outside Europe, and that is what tax-deferred retirement investments mean in practice, will not solve Europe's problems. Moreover, in practice, tax deferment means an infringement of the idea of free markets. To make it consistent we should consider abolishing it for investments outside Europe and at the same time an extension is needed for private retirement investors in Europe, comparable with the American 401(k) systems.

From the political left, such as Sarah Wagenknecht in *Focus* July 14 2019, to the political right, such as Friedrich Merz in *die Zeit* on June 11 2019, in Germany one sees the necessity of investments. The future demands so. As does ageing, which is the reason why in the report of Jean-Michel Charpin *L'avenir de nos retraites* (1999) more capital based funding for the French retirements is put forward. In Germany this has become policy with the Riester-rente in 2002 and the Rürup-rente in 2005. These two systems are performing below expectations. The same holds for far more ideas that have been put into practice in Europe. Europe, and the individual Europe constituting states, have lost control. The system of retirement investing works contrary to the objectives. The need for capital is insoluble, in the contemporary circumstances, *because the capital-based retirement systems, as they have developed, invest in the creation of problems instead of solving problems by investing.*

The European need of a European Retirement Investment Fund
Crises in climate, food, soil and pollution are developing. With consequences for work, housing and lifestyles. Therefore, it is necessary to have a balanced, reciprocal, consistent, fact-based and behaviour-based policy for sustainable economic development and climate crisis. Without public support policies fail. It is necessary, in order to deal with the environmental crises, first to deal with problems as:

- Overpopulated cities and urbanized areas with unaffordable houses and (over time) overburdened workers contrast with youth unemployment and depopulated areas with villages where only the very old and the exceptionally young didn't leave. Having the unemployed, the younger generations or migrants, working for free, or as cheap as possible, will not solve the problems with care or overpopulated areas.
- The European middle-class is in need, with respect to available time as well as available income. The position of farmers, shop holders, and more in general the owners of small and smaller companies is alarming. The production of essential, but easy to fabricate products, has all but disappeared from Europe.

Europe needs a consistent system which connects social, economic and ecological efficient as much as possible with retirement investing to the benefit of society. And thus, matches the problems with solutions. Necessary are Thousands of smaller companies with sustainable production are needed, in particular in the European regions with problems. These will have further effects, directly or indirectly they will employ people, they will buy locally and serve local interests.

The era of climate crises and social unrest, of large divisions and extreme polarizations, of nationalism and the inclusion of the own identity first, demands small and flexible mid-term strategical thinking, and not retirement systems that have large, inflexible, short-term effects.

Consistent solutions for Europe demands investments, for research, for the implementation of technological renewal, and to call new sustainable producing companies into existence. Robotization and artificial intelligence demand investments. Soil-friendly environmental and biological responsible farming with scarce use of insecticides and pesticides and varied production that spares insects and human beings, does ask for investments as well. It is convenient that there is a large demand for investment possibilities at the same time. The system however keeps supply and demand apart.

Retirement funding rules
The advantages of capital funded retirement are great. Participation by way of the collective aspect makes it cheap, pension funds are known for their

inexpensive management of assets, the state can borrow from its own population if necessary, and one doesn't need to extract from the retirement funds in case of a financial disappointment.

The retirement investments of superannuation funds, pension funds, banks, insurers and other investors cannot be estimated. But to give an impression: according to the *Pension Assets Study 2018* (February 14, 2019) by Willis Towers Watson 22 pension markets in the world owned pension assets of USD 41,355 billion. More than half of World's assets is connected to retirement funding. Private investments, like savings on a bank account for retirement, should be added. This gigantic retirement capital started to grow in the eighties. January 1, 1980 started the American 401(k), a retirement system that makes it possible to invest tax deferred for retirement. Retirement investments are almost always tax deferred since the contributions are considered to be postponed wages that are to be taxed when they are received as a pension.

Massive saving and investing for retirement created cheap money and low interest. After the crash in September 2008 one could read everywhere that money had been cheap. The reason why was not mentioned: all over the world, the large generation of well-to-do baby boomers started saving and investing for their retirement in the eighties of last century, voluntary and mandatory, collectively and private. It made money cheap, created an enduring demand for stocks and bonds, and made states collect sovereign debts with a clear conscience. At the moment, collective sovereign debt in the Eurozone is over ten trillion euro.

Worldwide the demographic peak of the baby boom generation was in 1947. Succeeding generations became smaller and smaller. Which in Europe is causing a change in proportion from five working people to two working people against one retiree. It could be expected that in 2012, when of the demographic peak of the baby boom generation reached the age of 65 years, the retirement savings and investments would have been used as intended, thereby causing a critical economic and financial tipping point. In 2012 a change was therefore to be expected from buying to selling, of continuously offering retirement investments by a disappointing demand, since the younger generations are smaller and poorer. This would have caused an enormous financial crisis. But the monetary politics of the central banks prevented this to happen. They kept money cheap by keeping the interest rate low, and quantitative eased for some USD 14 trillion (USD 14.000 billion). The consequence has been that countries with a low proportion of capital funded retirement could continue borrowing from countries with a large proportion of capital funded retirement.

Disadvantages of the current system of retirement investing
The heritage of the massive, undesired and out of control, environmental hostile, collective farms in eastern Europe, makes clear that small is flexible. But small is considered economically more expensive. Still retirement investing, tax deferred, in European interest has to be stimulated in smaller companies, Eastern Europe, depopulating areas, green technology, biological responsible agriculture and sustainable production. Because it is social effective and necessary during a climate crisis. At the same time this counterbalances the disadvantages and undesired side effects of the current system of retirement investing:

1. *Quantitative easing and the low interest rate policy of central banks had very unpleasant consequences for those that saved for retirement in a traditional way*. The policy of the central banks shall not change in the foreseeable future. The meaning of 'financial risk' has changed due to the worldwide volume of retirement savings. Stocks used to have a risk-premium which, with the current levels of sovereign debt, should be placed on bonds. Higher interest rates will make the problems worse, since it will not improve the financial base of the retirement pyramid in the current system.
2. *In the eighties, retirement capital started searching for possibilities to invest, almost exclusively in large listed companies and cheap ways of producing. This made countries with low wages and wage costs attractive, costs that were low, amongst others, because there was no retirement system in these countries, which makes the statement defensible that the quest for returns on retirement investments created globalization*. A direct line seems to exist between the start of the 401(k) in the United States in 1980, a growing baby boom concern over pensions, massive saving and investing for retirement in the eighties on one side, and the problems with wages, labour costs, unemployment, outsourcing and offshoring in the nineties, on the other side. Traditional production in the USA and Europe disappeared in this period.
3. *Retirement saving and investing created asset inflation*. Prices of real estate and stocks have been higher than reasonably could be expected. One cause is that the investors in the worldwide retirement capital are trading which each other. A pension fund buys some stocks from another with a small profit for the other and sells some other stock with a small profit in return, and both stocks have become more valuable.
4. *A consequence of retirement investments is speculation*. In the current system the competition for returns creates hidden costs and unpleasant side effects. The annual returns are more important than the connections with tax payers, the companies one invests in, the contributors for retirement or society as a whole.
5. *Taxpayers are paying the tax-deferred part of the contribution for retirement in advance which is the reason why they are confronted with austerity*. This in particular puts the position of the middle classes under pressure in countries with a large proportion capital-based retirement funding, as they had to pay for disappointing tax incomes for the state.
6. *The future tax income from the tax-deferred retirement investments are not taken into account in the national budgets, but are charged as necessary austerity on the taxpayers.* The future tax income could be borrowed easily without side effects. If necessary from retirement investors. The latter may not make directly the hoped-for returns, which does not need to be a problem with a necessary fine-tuning of the interests of governance, taxpayers, and Europe.
7. *The pensions that are payed out are disappointing*. For example, *the Guardian* reported 'annuity returns have fallen' on September 14, 2019. In the Netherlands, another example, pensions haven't been indexed for over ten years and are threatened to be cut back. The total amount of organized retirement investing in the Netherlands was over €1300 billion in December 2018, this is approximately two times the Dutch GDP. According to the Global Pension Assets Study 2018 by Willis Towers Watson of February 2019 the Dutch retirement investments in terms of

GDP were 36 percent higher than those in Australia, the number two on the list of largest retirement investors. Mercer, an Australian company that invests as well, crowned the Dutch system 'the best in the World'.

8. *The more tax-deferred retirement contributions are paid the less tax income the state receives*. After the bursting of the dotcom bubble in 2000 retirement contributions had to be higher in order to keep enough investment value. The consequence was lower revenues for the national states. The subprime crisis and the sovereign debt crisis in 2008 made this situation worse. After 2008 the countries with higher proportions capital-based funding were the countries with more economical problems and higher levels of austerity.
9. *There are too little investments in smaller companies*. Large investors do not invest in small companies since it is too impractical, too expensive because of the required control and too complicated. And small investors don't invest in smaller companies because it is too inflexible and too risky. Investments mainly are done in large listed companies, whether with mandatory tax-deferred contributions or with private savings. The Swedish retirement funding, for example, are heavily invested in US and Chinese technology, amongst others in companies like Amazon and Facebook (Focus-online 26-07-2019). These are companies whose labour conditions drew attention in the media. On Augustus 8, 2019 the Guardian revealed: 'Hundreds of schoolchildren have been drafted in to make Amazon's Alexa devices in China'. On the other hand, natural farming on a smaller scale is more expensive but can't get investments, because investments prefer in 'large and cheap', with the consequence that taxpayers have to pay for the cost of pollution and other environmental problems.
10. *A system of capital export has been created, subsidized by the taxpayers who pays the taxes on the future pensions in advance*. In 2013 approximately 86% of the Dutch retirement capital was invested outside the national borders, and over 50% outside the European borders, according to De Nederlandsche Bank, the controlling authority for the Dutch retirement system.
11. *The creation of more return on investments by investing the tax-deferred retirement investments outside Europe is very expensive*. Investments in companies outside Europe do not pay for the taxes, contributions or social security in Europe. Employees in Europe who take part in capital-based retirement funding, mandatory or voluntary, have to pay their contributions, which in case of mandatory capital-based retirement funding are part of their labour conditions. Which puts pressure on their own labour conditions when they invest in their competitors outside Europe and creates the risk that European production and services are too expensive in the international competition. Cheap production and services outside Europe, in the current system, cause unemployment in Europe and social costs worldwide. Something the European taxpayers ultimately have to pay for.
12. *Last, and certainly not least: the current system of retirement investing sustains a non-level playing field*. Smaller Dutch companies, for example, could hardly get a loan after the crisis of 2008. Capital in the world was too scarce and their wage costs were too high. The latter was caused by the retirement contributions for their employees which form a very large part of the wage costs. The companies weren't competitive enough, which makes sense, since part of their wage costs were retirement investments,

invested outside the Netherlands in more competitive companies. An internationally active Dutch entrepreneur told us that he found out that the retirement contributions paid by him were invested outside Europe in a competitor. This is systematic. When an European entrepreneur wants to sell her/his company which was meant to pay for retirement, the professional investors will have no interest. When he/she wants to invest additionally in the company, it will be not tax deferred. The same holds when someone else wants to invest in this company, outside the system. To make matters worse, returns of private investments are sometimes heavily taxed, even when they are made with retirement in mind. The owners of most small and smaller companies have in mind to sell it for retirement one day. But if someone wants to acquire such a company with their own retirement in mind there is no tax deferment, but taxes on the profits. And there are banks, advisors, and assorted middlemen who want to become rich through someone else's efforts. Which makes the existence of non-listed companies difficult, more so while consumers with retirement investments do not act as shareholders, they are buying their products as cheap as possible, without looking at their own retirement investments.

Towards consistency
The uniform Maastricht Treaty was not made with the differences in retirement systems in Europe in mind, which has been a severe flaw in the era of aging. A change of rules that takes the effects of taxes and tax deferment into account and uses the time horizon of retirement investing could be the answer. Since it cannot have been the intention of the Treaty of Maastricht to punish countries with a high proportion of capital retirement funding by imposing on their savings and investments the same regime as on countries that are lending to spend. The hidden side effects of retirement funding and generational needs in Europe, have to be combined in a sustainable, just and consistent way:

- If necessary, change the Treaty of Maastricht in order to leave the tax-deferred part of retirement investments in Europe out of the calculations of sovereign debt.
- It might be considered to prescribe taking the future tax income from the tax-deferred retirement investments into account in the national budgets.
- A deduction of the tax-deferred part of retirement investments in Europe in the national European contribution could be an answer.
- Recalculations of the actual state of financial affairs can be necessary by taking asset-inflation, a side effect of capital funded retirement, into account.

Taxes and tax deferment can be used as a steering mechanism for the combination of retirement funding with societal needs. The time lapse between saving and investing for retirement and the paying out of the pensions can be used. A combination with regional stimulation and development programs is evident. Controlling the taxes, instead of tax-deferred investing, has another advantage: unintended benefits can be taxed.

With the well-meant and in principle sound idea of capital-based retirement funding an inconsistent system has been made that forces taxpayers to act contrary to their interest. Indirectly they have to invest in polluting and unethical production and services and are compelled to act against their own, their local, their national and their European interest.

In Europe there is enough work, money in abundance and sufficient demand, but our own failing in the international competition is organised by the system of tax-deferred retirement saving and investing, systematic focussing on returns and keeping the inconsistencies, side effects and hidden costs out of sight. When a system is created that prevents hidden costs and undesired side effects, more retirement investing in Europe could be what society asks for in the future. Anticipating future developments is as essential as restoring agriculture and to enable the younger generations, the financial base of the retirement pyramid, to provide care for the older generations and finance their pensions. Control should be taken back in Europe, by restoring sustainable connections between investing, future needs, capital and society and restoring the economic cycle by making the financial base larger. Hence our idea.

Sander Boelens, on behalf of the Stichting 'het Intergenerationeel Overleg'
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The Stichting 'het Intergenerationeel Overleg' is an international, not-for-profit, nonpartisan, independent foundation based in the Netherlands.