The Economic and Labour Relations Review Vol. 20 No. 1, pp. 129–138

Book Reviews

Hazel Bateman (ed.) (2007) ***Retirement Provision in Scary Markets***, Elgar, vii + 224 pp., Hardback, RRP $104.70

'… private pensions are getting meaner, riskier and less predictable, and money saved for retirement is threatened by financial crises, what is the man on the street to do to make ends meet?' (The Economist 2009a). This timely and wide-ranging volume, a collection of ten papers (plus a comprehensive introductory chapter by the editor), is neatly bound together by the theme of retirement provision in volatile financial markets, and goes some way to answering this question.

And it is no longer only private sector workers who have to worry about how to squirrel away their savings. Public sector workers, often protected by defined benefit superannuation schemes backed by government, are now feeling the heat as cost concerns are raised about such retirement arrangements (The Economist 2009b).

The widespread switch away from occupational defined benefit superannuation to defined contribution plans has meant employees now bear the investment risk of their retirement savings. How should they invest for retirement? Should they avoid risky equity markets? Chapter 2 points out that investors avoid the equity market at their peril. The authors find that, when analysed over the long term, Australian equity markets have not become more volatile. They also note that including equities in a portfolio results in the lowest chance of individuals outliving their savings.

Chapter 3 turns the focus to bond markets. The author points out that fixed interest markets have become riskier, as governments have tended to reduce their debt issuance and lead to a higher concentration of corporate debt.[1] He argues, however, that bond portfolios are not necessarily more risky, as long as risks are properly understood. The chapter also treats the impact on asset markets of the perceived switch from equity markets to bond markets by baby boomers as they age. Chapter 4 also treats the question of how to invest, looking at passively managed (and thus cheaper) index funds as an alternative to actively managed investment funds. The emergence of index funds is explained, as well as the particular issues that surround their use.

In the vein of financial engineering, chapter 7 looks at questions about one's portfolio structure — the optimal mix between risky and safe assets — and annuitisation. Here, the authors innovate by modelling consumers who have a consumption floor. They find such a change leads to more conservative investment strategies, and a shortening of the delay to purchase longevity insurance (annuitisation). Chapter 8 tackles the question of smoothing investment returns to protect individuals from the vagaries of fluctuating asset returns. It describes strategies used by insurers and pension funds to smooth investment returns and advances a novel approach for defined contribution members to smooth their asset returns.

Not only financial volatility, but labour market volatility will impact on retirement savings. Chapter 5 reports on an analysis of the US Health and Retirement Study. This comprehensive data set throws up some very interesting findings, including lower earnings variability by those with higher lifetime earnings, and that married individuals enjoy retirement wealth that is less sensitive to earnings variability than those who are not married. Chapter 6 considers employee reaction to the UK financial downturn in 1992–2002. The authors surveyed a large number of people close to retirement, partially retired or retired. They found individuals near to retirement expect to push out their retirement date into the future. Indeed, working longer is a clear response to suddenly diminished retirement savings, making the issue of opportunities for older employees a significant one.

Private sector defined benefit superannuation as not necessarily a panacea to employees. Chapter 9 is a case study of the bankruptcy of the airline Ansett in Australia. Employees were left with less than their full entitlements, and the author details the shortcomings of the regulatory environment.

How should an economy in recession and with a rapidly ageing population reform its pensions? Chapter 10 presents the approach Japan has undertaken in meeting these challenges. Key changes include conversion of defined benefit plans to defined contribution plans, more sophisticated asset management by pension funds, as well as reform of government regulations to permit such changes. The last chapter considers the case of Brazil, where reformers are moving the retirement system towards one similar to that seen in the US, UK or Australia. Asset markets are extremely volatile, however, and the author gives the details of the approach taken. One troubling point that emerges in the Brazilian developments is the rapid growth in regulatory complexity concomitant with reform — regulatory change which, the author points out, is just as scary as the fluctuating asset markets.

The book includes a detailed index. It is an excellent addition to the pension literature, and of interest to researchers, practitioners and policy makers interested in pensions, pension policy, financial economics and public sector economics.

Notes

1. The current global financial crisis has reversed this trend.

References

The Economist (2009a) 'A special report on ageing populations: Scrimp and save', 27 June, pp. S9–S11.

The Economist (2009b) 'Briefing: Public-sector pensions. Unsatisfactory state', 11 July, pp. 64–66.

reviewed by **Sachi Purcal**
The University of New South Wales