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Press Release, Zurich, 19 June 2023

Pension at Risk: Is Our Pension System Under Threat? Future Scenarios for the Swiss 2nd Pillar

The Swiss 2nd pillar—a key component of the Swiss social system and of utmost relevance to almost all Swiss workers and retirees—is currently experiencing a major stress test. In addition to ongoing increases in life expectancy, the recent surge in interest rates represents a considerable challenge for Swiss pension funds.

In a new SFI Public Discussion Note, Swiss Finance Institute Professor Olivier Scaillet from the University of Geneva, along with Marc Fournier and Stéphane Riesen, both from Pittet Associés Ltd, analyze the effects of interest rates in the current context and then test the robustness of the Swiss 2nd pillar's financial capacity in light of several different economic scenarios.

The level of detail in the data they use makes it possible to study the stability of the 2nd pillar system in a granular way using complete and individual data for all of the country's pension funds, to develop a precise model of the future evolution of each pension fund, and to map out the risk borne by each institution.

Despite the proven strength of the Swiss 2nd pillar, the authors recommend the following options to improve the financial stability of this system:

- Ensure structurally adequate financing of benefits. The results of the sensitivity analyses clearly show that performance requirements are the cornerstone of the 2nd pillar's long-term stability. These performance requirements depend on the regulatory conversion rates. The constraint of a conversion rate of 6.8% or even 6.0% puts financial pressure on the Swiss occupational pension system as a whole, and should be alleviated by additional funding. Actuarially, this financing should be covered by contributions, rather than by performance, so that, on the one hand, it is structurally secure, and, on the other, performance requirements are reduced.
- Investigate solutions to limit the dilution of the coverage ratio when new affiliates join a fund. The analyses show that the concentration of pension funds, and the resulting dilution of coverage ratios, affects the stability of the 2nd pillar. When new employers join collective or joint foundations, the technical provisions and value fluctuation reserves are generally not financed, partly because of a lack of funds and partly because of the rules governing liquidation and partial liquidation. Introducing measures to limit the dilution of the coverage ratio, however, would probably reduce the possibilities for companies that wish to change their pension funds.
- Strengthen the supervisory framework by standardizing investment control processes. While the actuarial parameters and accounting values, such as the financial situation and annual statements, of a pension fund are periodically controlled by an independent body, investment of the fund's assets is

the sole responsibility of the Foundation Board, without any defined body tasked with exercising independent control and assuming civil and criminal liability. A uniform framework for the investment control process, both in actuarial and accounting terms, would strengthen the monitoring of risk management at the asset allocation level.

The findings of the SFI Public Discussion Note, as well as possible solutions, will be presented on Wednesday, 21 June 2023, at 6:00 p.m., at the Zurich Zunfthaus zur Saffran. Details on the event and the SFI Public Discussion Note on the Swiss 2nd Pillar can be found at www.sfi.ch/event2ndpillar.

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