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The Italian Public Pension System: Current Prospects and Reform Options

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Abstract

Public pension expenditure in Italy has been growing rapidly in the last three decades and is now among the highest in industrialized countries. Despite recent reforms, benefits remain generous by international standards and, unless additional measures are taken, the financial situation of the system will deteriorate in the long term. The paper reviews the current system, its history, and its prospects, and examines through simulations the long-run effects of alternative pension reform options.

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Summary

Public pension expenditure in Italy grew from about 5 percent of GDP in the early 1960s to over 15 percent in the early 1990s, outpacing all other categories of primary government expenditure and making Italy one of the biggest spenders on pensions among industrialized countries. In the future, the adverse demographic dynamics are expected to increase the pressures on the pension system. Against this background, a reform of the pension system was undertaken in 1992, aimed at stabilizing the share of pension spending in GDP and at reducing the distortions and inequities of the system. This reform was insufficient to restore the system to equilibrium, and further reforms are currently being prepared on the basis of an agreement reached between the Italian government and the trade unions in November 1994.

The paper reviews the current state of, and outlook for, the Italian public pension system, focusing primarily on its financial aspects. A pension system has, of course, other important implications, notably for the labor market, savings, and income distribution; these, however, lie outside the scope of this study. In view of the impending pension reform in Italy and the current public debate on this topic, the paper also simulates the quantitative effects of four possible reform options: lowering the accrual rate; raising the retirement age for women; introducing an early retirement penalty; and reducing survivors' benefits. These options do not exhaust the menu of possible reforms, but any package intended to restore the long-term equilibrium of the system would have to include at least some of them.

One thing that the simulations underscore is that there is no quick fix: in all cases, the effects of the measures on pension spending would be relatively limited in the next three to five years, and in some cases it would be negligible. However, some of the measures would generate substantial savings in the long term. The paper therefore suggests that the ideal package would contain a mix of some measures with immediate impact and some with a growing effect over time.