ILLUSTRATION: BINAY SINHA

Fresh urgency on pension reforms

The Union government needs to step in and lead the next round of pension reforms, which are now in danger of unravelling

Recent data releases show significant movement on the Indian demographic transition. The share of the youth (aged 15-29) has dropped to 26.7 per cent in 2021 and is projected to go down to 22.6 per cent by 2036. A striking feature of India's population is that projections of the demographic transition have routinely proved to be on the lower side; the transition has always materialised at a higher pace than was anticipated. The pandemic may well induce a further deceleration in births.

"Demographics is destiny" in many dimensions of thinking about India's future. On the problem of old age income and social security, the simple logic involves counting the working young present for each elderly person. Civil service pension reform in India is one of the silent successes of recent decades. However, there are some recent, worrying signs of state governments undoing the reform achieved in the past two decades. Such decisions, driven partly by populist considerations and partly to allay immediate fiscal pressures, will only result in transferring liabilities on to the future generations.

AARTHIKAM CHINTANAM

K P KRISHNAN

Looking back is useful for looking forward. An eight-member inter-ministerial expert committee led by Surendra Dave, named project Old Age Social and Income Security (OASIS) initiated by the then Ministry of Welfare in 1998, was the genesis of ideas around building a pension system for the *uncovered population*. Until then, the Indian pension system covered three categories of people. Government employees who received them under the traditional pay-as-you-go defined benefit (DB) system, destitute persons who were eligible under the National Old Age Pension Scheme, and the organised sector workers covered under the Employees' Provident Fund Organisation's pension scheme. Project OASIS helped create and socialise new knowledge on the failure of DB systems worldwide as well as the difficulties of the newer defined contribution (DC) systems that had been rolled out in many countries by then.

Though the OASIS report emphasised all the three components of pensions, policymakers chose to start with one: Pensions of government servants. There were compelling fiscal reasons for this. As a percentage of gross domestic product (GDP), the pension bill of the Union government increased from 0.24 per cent of GDP in 1980-81 to 0.73 per cent of GDP in 1999-2000 —a nominal annual growth rate of 22 per cent. When the reforms were launched, the pension bill constituted 5.7 per cent of the total revenue expenditure of the Union budget, reflecting a quantum jump from the 1980-81 level of 2.4 per cent. The pension bill of the Government of India consumed 8 per cent of the revenue receipts in the year 1999-2000 as against 2.9 per cent in 1980-81.

In February 2002, the National Democratic Alliance government announced the creation of a DC pension system. More significantly, new recruits to the civil services and the uncovered segment of the population were then merged into a single system — the National Pension System (NPS)— and a new agency, the Pension Fund Regulatory and Development Authority of India (PFRDA), was created to regulate the NPS.

State governments, beginning with Himachal Pradesh, in 2003, started joining the NPS. The successive United Progressive Alliance regimes stayed on course despite serious opposition from the left parties and managed to strengthen the new pensions regulator through an Act of Parliament. A critical cost in every pension system is the overhead of operational costs that is placed upon each participant. The NPS rapidly achieved scale. It lived up to its promise about driving down costs, and has become the cheapest fund management system in India.

Pension reforms like the NPS, where all old promises are fully upheld, imposes a double cost for one generation, which is termed "the transition generation". Governments have to pay individuals under the old DB scheme (those recruited up until 2003) full pension and contribute its share of the NPS to the new DC recruits (starting from 2004). There is thus no short-term gain in fiscal conditions through the NPS reform. It is only with time, where the persons receiving the DB pension fade away, that the fiscal gains are obtained. And yet, the NPS reform inexorably lays the foundation for a sound structure in the future, where governments evolve from the double payment to only paying contributions, and the young are de-risked from fiscal concerns.

The progress of this pension reform is the result of the sagacity of a spectrum of political leadership and administrations. Their patience and foresight, regime after regime, was necessary, since economic reform of such a nature typically takes decades to pay off. Despite the benefits being years away, the policy legitimacy of NPS came from the intellectual and evidence-based consensus around it, public debate and discussion, and good usage of external domain expertise. Today, the NPS is open to all citizens, and has separate schemes for corporations and low-income unorganised sector workers, apart from central and state government employees. Notwithstanding the various state governments moving in the opposite direction, the present Union government has been absolutely steadfast in its support for the NPS.

If the best demographic projections available in 1999-2002 were considered, the balance of logic in favour of the DC pension was stronger. Given what we now know about the acceleration of the demographic transition in the following 20 years, the case for the NPS reform is even stronger. Our best hope lies in everybody getting a pension account that is personal wealth, in having high economic growth so that individuals are able to salt away significant resources into this pension account, and in wise financial management through which good asset returns are obtained, commensurate with the level of risk taken.

All of this is not to say that everything is right with the design and implementation of the NPS and the grievances of government servants are not genuine. There are both process and substance issues but these concerns with the NPS could be allayed in less-damaging ways. Long-term economic reform in pensions is at risk of coming undone in the wake of populist and short-term views taken by state governments. The Union government must continue to lead this to build broad-based intellectual and political consensus to bring about more comprehensive reforms of all pension systems. .

The writer is an honorary professor at CPR, member of a few for-profit and not-for-profit boards, and a former civil servant