

PATTERNS OF PENSION FINANCIALIZATION IN FOUR EUROPEAN WELFARE STATES

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ABSTRACT

This paper explores the financialization of pensions in four European welfare states: the United Kingdom, Germany, the Netherlands and Sweden. In these welfare states, financial markets and financial actors have become increasingly important for pension provisions. Pension financialization is a variegated phenomenon, involving changes in funding mechanism, plan design, financial management and the centrality of funded pension schemes in the political economy. Nationally-specific configurations of these dimensions have created distinct patterns of pension financialization in the four cases. I argue that each pattern is the outcome of specific sticking points for policy reform that have emerged out of the institutional context of the national pension system. Locating these institutional sticking points helps identify common mechanisms of pension financialization across cases that are characterized by empirical variegation.

KEYWORDS

Europe; Financialization; Pensions; Welfare state.

MODELOS DE FINANCIARIZACIÓN DE LAS PENSIONES EN CUATRO ESTADOS DE BIENESTAR EUROPEOS

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RESUMEN

Este artículo analiza la financiarización de las pensiones en cuatro estados de bienestar europeos: el Reino Unido, Alemania, los Países Bajos y Suecia. En estos estados de bienestar, los mercados y actores financieros se han vuelto cada vez más importantes en la provisión de las pensiones. La financiarización de las pensiones es un fenómeno variado, que implica cambios en el mecanismo de financiación, el diseño del plan, la gestión financiera y la centralidad de las pensiones de capitalización en la economía política. Las configuraciones nacionales específicas de estas dimensiones han creado patrones distintos de financiarización en los cuatro casos. Sostengo que cada patrón es el resultado de puntos de conflicto específicos para la reforma de dichas políticas, que han surgido del contexto institucional del sistema nacional de pensiones. La localización de estos elementos de referencia institucionales ayuda a identificar mecanismos comunes de financiarización en todos los casos, que se caracterizan por una variedad empírica.

PALABRAS CLAVE

Europa; Financiarización; Pensiones; Estado de bienestar.

INTRODUCTION

Research on financialization has grown exponentially since the Great Financial Crisis of 2008. The initial focus of the financialization scholarship on the non-financial corporation emerged out of the specific context of the United States with its highly developed financial markets (Krippner 2005). Since then, scholars of financialization have identified many other areas where the growing role of financial markets and actors has manifested itself in contemporary societies, including the household, the state and the natural world (see Mader et al. 2020 and other articles in this special issue). The growth of financialization studies has also been met with a widening geographical scope of the literature with a growing number of studies on financialization in traditionally bank-based economies (Hardie and Howarth 2009), state capitalist economies (Wang 2020) and emerging markets (Bonizzi et al. 2020). Scholars' forays into additional sites and locations of financialization have resulted in new understandings of the distinctive and often uneven manifestations of financialization across different types of capitalist economies (Karwoski and Stockhammer 2017).

Yet, the contemporary focus on variegation also complicates scholarly understandings of financialization. Financialization remains an elusive term, as scholars employ a host of definitions and conceptualizations to describe related, but not identical phenomena. Among the most well-known of these is Gerald Epstein's definition of financialization as "the increasing role of financial motives, financial markets, financial actors, and financial institutions in the operation of the domestic and international economies" (2005:3). However, as has already been noted by several contributors to this debate (Engelen 2008, Christophers 2015), such fairly broad understandings of financialization run the risk of conceptual stretching. When conceptualizations of financialization become so broad that they encompass almost 'everything finance', the concept may lose its analytical prowess (Van der Zwan 2014: 101). For this reason, Mader et al. (2020:8) have proposed that scholars develop conceptualizations of financialization that are 1) limiting, 2) mechanism-oriented, and 3) contextual.

Studies of pension financialization in Europe have largely mirrored the developments in the broader field of scholarship. Pension financialization refers to the growing role of financial markets and financial actors in the provision of old-age pensions. Starting with an initial focus on the United Kingdom (Waine 2001; Langley 2004), research on pension financialization now includes case studies of the Nordic countries (Anderson 2019; Belfrage 2008), continental Europe (Bonizzi and Churchill 2017; Natali 2018), Iceland (Macheda 2012), Portugal (Rodrigues et al. 2018) and Turkey (Saritas 2020). These studies have identified changes to existing pension systems along

several dimensions (i.e. Wiss 2019), four of which I will consider here. The first is *capital-funding* as a method of financing, which involves the investment of pension savings in financial markets with the goal of generating returns to cover future liabilities. A second dimension of pension financialization relates to the introduction of *pension contracts* that make benefit levels conditional upon financial market performance, as is the case with Defined Contribution contracts. Third, pension financialization involves particular changes to *financial management*, specifically the growing exposure to investment risk as a result of changing asset allocations. Lastly, pension financialization may refer to the *centrality of funded pension schemes* in the (global) political economy.

The goal of this paper is to provide an interpretive lens through which to analyse empirically distinct manifestations of pension financialization. To this end, I will identify patterns of pension financialization in the United Kingdom, Germany, the Netherlands, and Sweden. The cases represent different welfare state regimes (Esping-Andersen 1990): a liberal welfare state (United Kingdom), a social-democratic welfare state (Sweden) and two conservative welfare states (Germany and the Netherlands). The two conservative welfare states show internal variation: the Netherlands has a mature three-pillar pension system that dates back to the early 20th century, whereas Germany has begun to expand its second and third pillars since the turn of the 21st century. Institutional differences notwithstanding, policy reforms have expanded the role of finance in all four cases, albeit in different ways. As the paper will show, the cases are characterized by important variations along each of the dimensions of pension financialization identified above: the scope of capital-funding, plan design, financial management, and pension fund capitalism.

In line with Mader et al. (2020), I carry out a contextualized comparison of the four patterns of pension financialization. Contextualized comparison moves institutional analysis beyond explanations of cross-national variation that centre on path dependencies created by pre-existing welfare institutions. Rather, a contextualized approach considers how common pressures may set in motion different policy reforms in different national contexts. The approach revolves around the identification of institutional 'sticking points' which emerge from the flexibilities and rigidities of the existing institutional framework (Thelen and Locke 1995: 342). These sticking points shape the salience of the policy reform to the actors involved and create the fault lines along which political conflict plays out. To recast Thelen and Locke's approach for present purposes: to understand which dimension(s) of pension financialization has (have) become relevant in the four cases requires identifying the institutional sticking points around which policy challenges have emerged.

Drawing on existing case studies of pension financialization, I will show how concerns regarding the long-term sustainability of the pension system resulted in similar patterns of pension financialization in the otherwise institutionally different cases of the UK and Germany. In both cases, policy reforms responded to the perceived need to expand coverage in the second and third pillars of the pension system. In the Netherlands and Sweden, expanding coverage was not politically salient due to the already quasi-mandatory nature of workplace pensions. Instead, concerns over the costliness of DB workplace pensions led to renegotiation of these contracts by employers and unions. In Sweden, such renegotiation already took place in the 1990s and coincided with a radical overhaul of the state pension in the first pillar. In the Netherlands, a continued reliance on DB pensions in a system with high capitalization and coverage throughout the financial crises of 2001 and 2008 created large-scale underfunding of pension liabilities. Here, both plan design and investment practices became sticking points for pension reform.

The outline of this paper is as follows. First, I will conceptualize pension financialization, focusing on four dimensions that are associated with the growing role of financial markets and financial actors in pension provision. The second section of the paper applies this conceptualization of pension financialization to the four cases. Here I show how the four dimensions identified earlier form building blocks that create nationally distinct patterns of pension financialization. The third section of the paper contextualizes these findings by comparing the cases of the United Kingdom, Germany, the Netherlands and Sweden. In the final section of the paper, I take these findings as a starting point to further reflect on the mechanisms underlying processes of pension financialization.

WHAT IS PENSION FINANCIALIZATION?

While pension financialization broadly conceived can be defined as the growing role of financial markets and financial actors in the provision of old-age pensions, scholars within the field have categorized various empirical phenomena under this rubric. Following Mader et al. (2020), I propose a limited understanding of pension financialization by outlining four dimensions associated with this concept. Based on a review of the literature, I identify: 1) the expansion of capital-funding; 2) changes to pension scheme design; 3) changes to the financial management of pension plans, including the investment of assets; and 4) the centrality of funded pension schemes in the (global) political economy.

Expansion of funded pension schemes

Pension financialization starts with the introduction of capital-funding as a method of financing. Capital-funding implies that pensions are to be

(partially) financed from investment returns rather than current contributions or book reserves, thus creating a dependency on global financial markets. It is often juxtaposed with Pay-As-You-Go (PAYGO) financing, whereby current contributions pay for current benefits. Since the 1990s, capital-funding has become an attractive policy alternative to PAYGO financing in light of growing financial pressures on public pension systems due to demographic ageing. As pension systems need to accommodate a growing group of retirees, who will spend more years in retirement than previous generations, the ability of the active working population to contribute to this system has become severely limited. For this reason, international organizations such as the World Bank, the OECD and the European Union produced influential policy reports that promoted the so-called multi-pillar pension system, in which retirement income is provided by a combination of state (first pillar), occupational (second pillar) and personal (third pillar) pensions (for an overview, see Rodrigues et al. 2018).

The growing importance of capital-funding within national pension systems has coincided with the expansion of private occupational and personal pensions (pension privatization) and a growing role for market-based pension providers (marketization) (Ebbinghaus 2015). Since the 1990s, many states have sought to reduce pension expenditures by reducing citizens' reliance on public pensions and instead increase the importance of private provisions for future retirement income. Orenstein (2013) shows how more than 30 countries across the world adopted this new policy paradigm between 1981 and 2004. Still, the expansion of capital-funding is by no means universal. Several European welfare states (e.g. Belgium, Austria) have so far maintained first pillar PAYGO pensions without substantially expanding the second or third pillars of the pension system. In a number of European countries, moreover, the initial introduction of funded pensions in the second pillar has been partially reversed, as high transition costs were exacerbated with mounting fiscal pressures following the Great Financial Crisis of 2008. This has happened, for instance, in several Central and Eastern European countries (Naczyk and Domonkos 2016) and in Portugal (Rodrigues et al. 2018).¹

Since the Great Financial Crisis, the expansion of capital-funding through pension privatization has slowed. In addition to fiscal constraints, Orenstein (2013) argues that an ideational shift caused by failed reforms and growing criticism within the World Bank and IMF contributed to the declining appeal of the privatization paradigm. Since the 1990s, a growing number of countries have introduced the so-called Notion Defined Contribution (NDC) pensions to improve the financial sustainability of the first pillar.

NDC pensions combine individual pension accounts with pay-as-you-go financing: citizens pay fixed contributions, while retirement age and benefit levels are adjusted for demographic and macroeconomic changes. While non-funded, such pensions allow for flexible adjustment to changing circumstances, while avoiding the transition costs associated with pension privatization (Guardiancich et al. 2019). NDC pensions therefore pose an influential policy alternative to capital-funding.

Pension financialization through plan design

Plan design shapes the extent to which investment returns affect pension benefits. Defined Benefit (DB) pension plans promise a guaranteed pension benefit upon retirement, for instance 70% of a beneficiary's average salary. In Defined Contribution (DC) plans, contributions are fixed but benefits are conditional upon investment return. Following this logic, low investment returns directly affect retirement benefits in DC and indirectly in DB plans, as underfunding may undercut the pension promises made. Underfunding will therefore require higher contributions or repair payments from sponsors. In DC plans, investment risk is carried entirely by the beneficiary. The presence of institutional buffers, however, may mitigate participants' financial market exposure. Such institutional buffers include, for instance, minimum investment returns and caps on investment fees for DC plans (Naczyk and Hassel 2019) or the presence of pension protection schemes for DB plans (Stewart 2007).

DB schemes are increasingly considered less sustainable than DC pensions (OECD 2019a).² Demographic ageing poses longevity risk, while low interest rates and market volatility further threaten DB schemes' funding status. Additionally, DB pensions are argued to be less suitable to respond to changing labour market conditions, such as increased job mobility and non-traditional work (ibid.). While DB schemes were widely adopted in the second half of the twentieth century, they have lost in popularity since the 1990s (OECD 2019a). This is not only the result of pension privatization, described above, but also of employers withdrawing from DB workplace pensions. Employers may not only be motivated by cost considerations. Dixon and Monk (2009), for instance, argue that international accounting standards have incentivized employers to switch from DB to DC pensions to avoid being penalized by shareholders for pension liabilities on their balance sheets. Short of a complete transition to DC pensions, however, employers may also change the conditions of their DB plans, for example by introducing a contributions cap or removing the responsibility to make repair payments (Bridgen and Meyer 2009).

Pension financialization by financial management

Scholars have also associated pension financialization with changing practices of managing capital-funded pension plans, including the investment of pension assets. This is not only the case in political economies that have witnessed a rise in individual DC pensions, but also in the case of collective DB pensions. Each type of plan requires a host of financial services, provided by professional groups (asset managers, pension lawyers, actuaries, proxy advisors) that therefore stand to benefit from the worldwide growth in pension assets. The result is a large network of financial intermediaries, that stand between the plan members and the financial markets in which their savings are invested. Such intermediation comes at a cost, as each actor within the network charges fees for their services (Arjaliès et al. 2017). Here, developments in the welfare state connect to the broader process of financialization, which involves the growing share of profits for the financial sector in the economy (Krippner 2005).

The growth of capital-funded pensions has not only impacted which actors are involved in pension management, but also the ways in which pension assets are invested. In particular, scholars have observed a shift in pension asset allocations since the 1980s from fixed-income assets (government or corporate bonds) towards corporate shares (McCarthy et al. 2016), and towards alternative investments such as hedge funds or private equity funds in the past decade (Bonizzi and Churchill 2017). This shift has not only been the outcome of a search for return amidst the high inflation environment of the 1980s or the booming stock markets of the 1990s, but also a function of the growing importance of financial economic principles in asset management practices. In particular, ideas associated with Modern Portfolio Theory have moved pension investors to diversify their holdings across asset classes and geographic regions, thus growing the global pool of footloose capital. In this context, scholars have noted pension investors' proclivity for herd behaviour - mimicking each other's investment practices - which drives asset prices up and creates speculative bubbles (Engelen 2003).

Pension fund capitalism

Changes in pension investment practices have also had political ramifications. As global pension assets have grown to an unprecedented \$44.1 trillion (OECD 2019a), funded pension schemes have become influential financial actors within the political economy, a phenomenon also known as pension fund capitalism (Dixon 2008:249).³ Due to their enormous size, funded pension schemes hold large ownership stakes in non-financial corporations and governments across the globe. This 'universal ownership' has limited schemes' ability to 'exit' the market by selling assets

in response to disappointing returns. Instead, they use 'voice' by engaging with corporations or governments to improve performance (Hawley and Williams 2000). While some scholars welcome pension fund capitalism as a possible driver for a more sustainable financial system (Blackburn 2002; Langley 2008), others are sceptical of its potential. Sceptics argue, for instance, that pension funds are primarily driven by the pursuit of financial returns rather than social concerns (Engelen 2003); that pension funds are rarely in direct control of their own investments due to outsourcing to asset management companies and other financial services firms (Braun 2016); or that fund beneficiaries rarely have a say in how their savings are invested (McCarthy 2020).

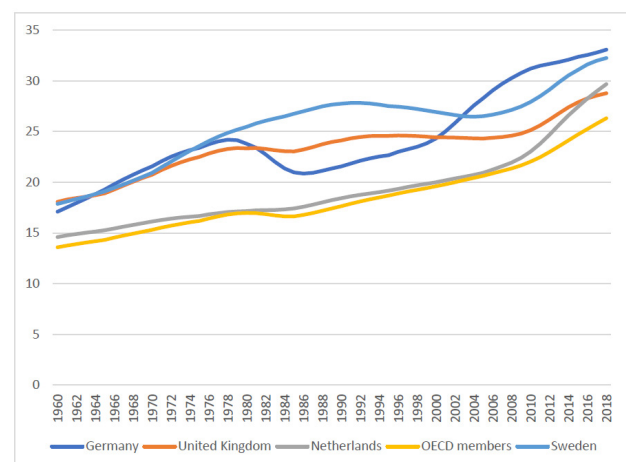
While pension fund capitalism is often linked to the declining power of organized interests such as employer groups and labour unions, its effects are not so clear-cut. Studies have shown how these groups have mobilized pension capital to serve their own self-interests, such as access to investment capital (business) or corporate control (labour) (McCarthy et al. 2016; Naczyk, 2016). According to Van der Zwan (2018), such processes of capture are indicative of a new financial politics of the welfare state, which does not revolve around distributive conflicts over benefits, but rather centres on solvency rules, investment policies, accounting rules and other policy measures affecting the distribution of financial risk. An important precondition, however, is the extent to which such actors can exert control over the investment process. For the United States, for instance, McCarthy (2017) notes that workers have limited control over pension investments due to the absence of employee representation on the boards of trustees of single-employer pension funds. In European welfare states, workers are more commonly represented on pension fund boards (Sorsa 2016). Wiss (2015) has therefore argued that labour unions have a moderating impact on financial volatility, as their board presence results in more conservative investment policies.

PATTERNS OF PENSION FINANCIALIZATION

The four countries represent diverse cases from a welfare state perspective (Seawright and Gerring 2008).⁴ The *United Kingdom* is a liberal market economy and welfare state. Its quintessential Beveridgean pension system has historically provided flat-rate public pensions, complemented by earnings-related occupational schemes. *Germany* is a coordinated market economy with a conservative welfare state. Its pension system is historically Bismarckian: highly developed earnings-related public pensions, based on social insurance, with a limited role for occupational and personal pensions. *Sweden* is a coordinated market economy with a social-democratic welfare state: its two-tiered public pension system combines

the Beveridgean flat-rate pensions with a Bismarckian second tier for income maintenance. *The Netherlands*, finally, is a coordinated market economy with a hybrid welfare state, combining elements of all three regime types. Its pension system is Beveridgean: it has a highly developed second pillar of funded occupational pensions alongside a first pillar of statutory PAYGO pensions. All cases except Germany have mature, three-pillar pension systems with long histories of capital-funding. Germany's three-pillar system dates back to 2001, when the so-called Riester reform was passed to expand coverage of funded pension schemes in the second and third pillars.

Figure 1.
Old-age dependency ratios in selected countries,
1960-2018 (aged 65 and over as % aged 15-64)



Source: World Bank (2020).

All four cases are characterized by high and increasing old-age dependency ratios, which challenge the long-term sustainability of the pension system (see figure 1). Nevertheless, the United Kingdom seems theoretically the most prone to pension financialization, because it belongs to the regime type most reliant on market provision of welfare. Liberal market economies, such as the United Kingdom, are characterized by strong institutional complementarities between the welfare state and the financial system (Hall and Soskice 2001:18). In these countries, funded pension schemes do not only provide asset-based welfare, but also serve as an important investor base for highly developed financial markets (Trampusch, 2018). In the two coordinated political economies with mature pension systems (Sweden and the Netherlands), funded pensions have traditionally served as an important source of patient capital. Here, the state introduced legal investment rules to mobilize pension capital for domestic investment (Anderson 2019; McCarthy et al. 2016). The presence of worker representation on pension scheme boards has arguably served as an institutional buffer against financialization in these pension systems

(ibid.). Germany presents an outlier case: with a historically limited reliance on capital-funding in its pension system, it should be the least susceptible to financialization of all four cases.

Table 1 compares cases across the four dimensions of pension financialization. The *scope of capital-funding in the pension system* consists of both its degree of capitalization and its coverage, i.e. the percentage of the workforce covered by funded pensions. The greater the scope of capital-funding, the more it contributes to pension financialization. Yet, the scope of capital-funding should also be coupled with the *type of plan design*: the more directly financial returns shape the pension outcomes, the greater the plan's contribution to pension financialization. In turn, financial returns are shaped by the specific *allocation of pension assets*: equity and alternative investments create more volatility in investment returns than investment in fixed income assets. Fi-

nally, the extent to which pension schemes act as *global investors* is reflected by the percentage of assets invested domestically, in combination with the presence of legal restrictions on foreign investment. Where such restrictions steer pension investment towards domestic firms, this dimension of pension financialization is limited.

The four dimensions constitute building blocks that together create a pattern of pension financialization. First, the *United Kingdom* has a high level of capitalization, yet medium coverage. This means that its scope of capital-funding is more limited than in the Netherlands or Sweden. Its combination of DC and DB pensions in the second pillar, combined with a substantial proportion of investments in fixed-income assets, further shape its financialization pattern. *Germany*, secondly, is also characterized by medium coverage, but its capitalization rate remains low. While its funded workplace pensions tend to be DC,

Table 1.
Dimensions of pension financialization in four European welfare states (2018 or latest year available)

1: Capital-funding						2: Plan design		
	Coverage of funded and private pension plans (as % working age population, 15-64 years)			Assets in funded and private pension plans as % GDP	Assets in public pension reserve funds as % GDP	Types of funded pension plans (first/second pillar)	Minimum returns on DC plans	DB pension protection scheme
	Pillar:							
	1 st	2 nd	3 rd					
DE	-	57,0	33,8	6,9	1,0	DC (II)	Y	Y
NL	-	88,0	28,3	173,3	-	DC: 8,6% DB: 88,3% (II)	N	N
SE	100,0	90,0	24,2	88,0	29,4	DC (I & II)	N	N
UK	-	46,0	5,0	104,5	-	DC: 35,7% DB: 34,7% (II)	N	Y

3: Financial management and investment					4: Pension fund capitalism		
	Allocation of assets in funded and private pension plans as % of total assets			Restrictions on certain asset classes	% of assets in private and funded pension plans invested abroad	Restrictions on foreign investments	Number of top 300 pension funds
	Fixed Income	Equities	Other				
DE	49,9	5,4	40,6	Y	N/A	N	6
NL	46,2	28,6	22,1	N	86,5	N	12
SE	16,1	13,9	5,6	N	14,4	N	7
UK	30,2	9,0	31,9	N	25,7 (2017)	N	24

Sources: DNB Statistics (2020); OECD (2019a); OECD (2019b); Office for National Statistics (2020); Thinking Ahead Institute (2019). Funded and private pension schemes include private pension arrangements (funded and book reserves) and funded public arrangements. The 'other' category of assets includes loans, land and buildings, unallocated insurance contracts, hedge funds, private equity funds, structured products, other mutual funds (i.e. not invested in equities, bills and bonds or cash and deposits) and other investments.

the presence of investment guarantees and a relatively high proportion of investments in fixed-income assets limit the impact of financial markets on pension outcomes. In *the Netherlands*, thirdly, the combination of high coverage and high capitalization arguably produces the largest scope of capital-funding of all four cases. A relatively high proportion of investments in equities and investments abroad further contribute to pension financialization. This is limited by the continued predominance of DB pension plans, although the case below will show that most occupational plans are now DB/DC hybrids. *Sweden*, finally, deviates from the three other pension systems by having a funded component in its first pillar, along with funded DC pensions in the second pillar. A relatively small proportion of assets is invested abroad.

What is the explanation behind these patterns of variegation? Existing studies stress the importance of national institutional frameworks and the political interactions of the actors within them. To complement these studies, I propose a contextualized comparison of the four cases. Contextualized comparison is an analytical approach that shows how “otherwise different struggles in fact represent (context-specific) manifestations of similar strains” (Locke and Thelen 1995: 339). It departs from traditional matched comparisons by taking into account *starting points*, *salience* and *sticking points* in processes of institutional change. Starting points refer to the moments at which common pressures confront particular countries. Salience refers to the significance of the policy challenge to the actors involved. Both starting points and salience are shaped by the rigidities and flexibilities embedded in the existing institutional framework. Together, they inform the *sticking points* of a particular policy challenge, here defined as the substantive issues over which policy conflict takes place. In short, contextualized comparison seeks to explain “cross-national variation in conflicts centering on (different, nationally specific) sticking points” (Locke and Thelen 1995: 343). In the following section, I will use the three concepts of the contextualized comparison to offer a new interpretive lens on existing studies of pension financialization for each of the cases.

FOUR CASES OF PENSION FINANCIALIZATION

United Kingdom

The United Kingdom has become one of the most studied cases of pension financialization. This is not coincidental: particularly in the early days of this scholarship, financialization was strongly associated with the market-based political economies of the United States and the United Kingdom. The presence of highly developed pension fund capitalism seemed a logical outgrowth of the two countries’ large finan-

cial markets and market-oriented welfare state. The United Kingdom has a mature, three-pillar pension system, of which the second and third pillars are capital-funded. At 104,5% of GDP, capitalization of the pension system is high compared to other European political economies, especially considering relatively low coverage rates (OECD 2019a:211). Pension financialization in the United Kingdom has manifested itself along additional dimensions, including: 1) a shift from occupational DB to occupational and personal DC pensions; 2) the marketization of pension provisions; and 3) changes in funds’ asset allocations.

The decline of DB occupational pensions in the UK has been well-documented. Occupational pensions are traditionally organized at company level. Due to the voluntary nature of workplace pensions, participation rates have been low compared to mandatory systems: they peaked at around 50% of the working population, before the introduction of auto-enrolment in 2012. The voluntary nature of the second pillar has also made it easier for employers to close DB pension schemes. Since the 2001 financial crisis, hundreds of DB schemes have closed and many employers have switched instead to DC plans (Bridgen and Meyer 2009; Langley 2004). The Great Financial Crisis has reinforced the ongoing decline in DB pensions: not only has the number of active members in DB plans halved since 2010, but most remaining DB plans are now entirely closed (40%) or closed to new members (43%). A majority of DB schemes is also underfunded (The Pensions Regulator 2018). Per 2018, the percentage of the workforce participating in DC plans equals that of DB pensions (Office for National Statistics 2020).

To explain employers’ abandonment of DB pensions, scholars have pointed at increased state intervention, which has affected employers’ perceptions of the costs associated with these plans. These changes were set in motion with the introduction of “contracting out” or opt-outs from public pension system to occupational or personal pensions (Mabbett 2012). Meant as a cost-saving measure, this increased the role of for-profit financial services providers. Events related to the mismanagement of private pensions, such as the Maxwell scandal or the misselling of personal pension products, motivated the government to tighten regulations around funded pension plans again. For DB plans, these have included, for instance, new indexation rules (1995) and minimum funding requirements (1997) (Bridgen and Meyer 2009). In 2000, the government launched an alternative pension scheme, the so-called Stakeholder Pension, a DC scheme that kept costs down and risks low thanks to legal limits on asset management fees and a passive investment strategy (Mabbett 2012). After the 2001 financial crisis, moreover, the government introduced market-based valuation of DB liabilities and increased premiums for the Pension Protection Fund (Wiss 2019).

Poor financial performance and persistent underfunding of DB pension plans created institutional sticking points for increased regulation. Langley (2006) has described, for instance, how UK pension investors first began to replace fixed-income assets with corporate stocks in the high-inflation economic context of the 1960s and 1970s. Such asset allocations proved highly lucrative amidst the booming stock markets of the 1980s and 1990s, with employers granting themselves premium holidays thanks to high investment returns. Wiss (2019:506) notes, however, that UK pension funds were more exposed to corporate equities than other European pension funds (71% of total assets) prior to the 2001 financial crisis. This made them particularly vulnerable to the stock market crash. Since the Great Financial Crisis of 2007-2008, UK pension funds have reduced their investment in corporate equities and shifted their allocations to alternative asset classes (Bonizzi and Churchill 2017).

The policy response to the Great Financial Crisis, however, has not been a reversal of pension financialization. Instead, the state has sought to broaden coverage of capital-funded occupational plans by making participation mandatory. Since 2012, auto-enrolment in occupational plans is in place, whereby employers can opt between a pension provider of their own choice or directing employees towards the state-run default provider, the National Employee Savings Trust (NEST) (Mabbett 2012). According to the Office of National Statistics (2020), three-quarters of the workforce is now covered by an occupational pension plan, the highest level since the introduction of auto-enrolment. That state intervention has driven pension financialization since the turn of the century is therefore the paradoxical outcome of particular policy challenges stemming from employer voluntarism and financial mismanagement (Berry 2016).

Germany

The German conservative welfare state is often considered the very opposite of the liberal welfare states of the United States and the United Kingdom. The quintessential social insurance system, Germany has been represented as a case of “belated multipillarization” and a “least likely case of pension financialization” (Wiss 2019:512) due to the comparatively limited scope of capital-funding within the pension system. The German first pillar consists of a means-tested statutory pension, which has been in place since 1889. The German second pillar consists of five different occupational pension vehicles, all of them voluntary. Among these are superannuation funds (*Pensionskassen*), offering DC-type pensions, and corporate book reserves (*Direktzusage*). The latter have been complimentary to Germany’s bank-based financial system, providing patient capital to firms and sheltering them from market finance (Carstensen and

Röper 2019). Due to its long existence and relative generosity, the statutory pension has crowded out second and third pillar provisions, which became an important sticking point for pension reform. In 2015, the statutory pension constituted 74% of the income for German pensioners, while the old-age dependency ratio was above the EU average (European Commission 2018). Still, capitalization rates for the German pension system remain among the lowest in Europe: 6,9% in 2017 (OECD 2019a: 211).

From the late 1980s onwards, German policymakers questioned the long-term sustainability of the pension system, due to its strong reliance on the first pillar in the face of a rapidly ageing population. Since the 1990s, therefore, several reforms have been enacted to facilitate a move away from the PAYGO first pillar and towards capital-funded occupational and personal pensions. The most notable of these, the 2001 Riester reforms, were to compensate for statutory pension cutbacks by subsidizing capital-funded occupational and personal pension plans, predominantly DC (Ebbinghaus 2019; Wiss 2019). Carstensen and Röper (2019) place the Riester reform in the context of a broader process of financial liberalization in Germany: to those in favor of moving towards a more market-based financial system, capital-funded pensions were a highly salient policy issue. Capital-funding would not only foster the growth of German financial markets, but also encourage pension privatization.

The ongoing incentivization of capital-funded pensions in Germany has meant the entrance of new players into the pension system. Banks and investment companies began to compete with for-profit insurance companies in marketizing new pension products, with Deutsche Bank proposing Anglo-American pension funds as early as in 1995 (Carstensen and Röper 2019). Six years later, American-style *Pensionsfonds* were introduced as part of the broader Riester reform. These new pension vehicles manage collective, occupational pension plans for certain sectors, such as the metalworking industry (*Metallrente*) and the chemical industry (*Chemie*), under bipartite governance by employers and trade unions. Contrary to the *Pensionskassen*, the *Pensionsfonds* have complete freedom to invest (*Pensionskassen* face restrictions on certain asset classes). In practice, however, the *Pensionsfonds* predominantly invest in fixed-term assets and guarantee the nominal value of contributions. For this reason, Wiss (2019:512) has called these pension plans “DC-light.”

Since the Great Financial Crisis of 2008, the financialization process within the German pension system has continued through 1) a further expansion of capital-funded pensions; 2) a reduction in the legally required investment guarantees (down from 3.25% in 2007 to 0.9% in 2017) and 3) the 2017 introduction of collectively bargained, auto-

enrolment DC plans without investment guarantees (Wiss 2019). These changes have further increased a financial risk shift from state and employers to wage-earners. According to Wiss (ibid: 512), this has resulted in “UK-style semi-obligatory financialization of the ‘everyday life’ of employees.” As of 2015, 70% of the working age population was covered by a voluntary pension contract (OECD 2019a:207). While the capitalization of the German pension system remains low, it shares important commonalities with the United Kingdom: a largely voluntarist second pillar and concomitant low coverage rates became sticking points for pension reform. The state responded to these sustainability challenges by introducing tax-subsidized savings vehicles and auto-enrolment. Even though Germany remains a laggard, pension financialization has taken on a liberal appearance, with individuals’ pension savings providing the foundations for a state-driven expansion of financial markets.

The Netherlands

The Netherlands has a mature, three-pillar pension system, of which the first two pillars (the statutory pension and the occupational pension) contribute most to citizens’ retirement income. The statutory pension, introduced in 1956, is financed on a PAYGO basis from social insurance contributions and general taxation. The occupational pensions, the oldest of which date back to the late 19th century, are capital-funded. Almost every Dutch employee (96% of the workforce) participates in an occupational pension plan due to the (quasi)mandatory nature of the second pillar. Occupational pension plans are predominantly DB, although the number of DC plans has been on the rise since the turn of the century. They are almost exclusively managed by pension funds, organized by company and by industry (Anderson 2011). The combination of a longstanding tradition of capital-funding, high participation rates and comparatively generous occupational pensions has resulted in a highly capitalized pension system, whose ratio of pension assets to GDP is among the highest in the world at 173,3% (OECD 2019a:211).

Its history of capital-funding notwithstanding, the Dutch pension system has long been sheltered from financial market turbulence. Two factors have contributed to the historical stability of the system. First is the specific nature of most occupational pensions as collectively organized, DB plans. This means that any investment losses incurred can be absorbed by the collectivity, rather than being carried by the individual plan member. The DB promise, moreover, binds the sponsoring employer to compensate for such losses in cases of underfunding, either by paying higher contributions or by making repair payments (Anderson 2011). A second contributing factor has been the investment practices of Dutch pension

funds, which were dominated by fixed-income investments for most of the twentieth century. When Dutch pension funds made the switch to so-called real assets, predominantly corporate equities, they benefited from fortuitous stock market conditions in the 1980s and 1990s (McCarthy et al. 2016). This means that, on the aggregate, financial performance of the system has been fairly robust.

As in the United Kingdom, however, changing asset allocations have made Dutch pension funds quite vulnerable to stock market downturns. The financial crises of 2001 and 2008 have resulted in deteriorating investment returns, which in turn have translated into declining funding levels for pension funds. This development has coincided with a broader risk shift from the employer to the employee. After reaping the fruits of the stock market boom of the 1990s in the shape of premium holidays and repayments, employers have withdrawn from the DB pension promise by capping contribution rates and rejecting repair payments. This applies to the nominal pension as well as to indexation, which was made conditional upon investment performance in 2001. Since the Great Financial Crisis, situations of underfunding resulted in a reduction of pension entitlements for millions of active and retired members. These crisis measures have been extended through the 2010 Pension Accord, the outcome of tripartite negotiations between the state, employers and unions. Consequently, Dutch occupational pensions are now DB/DC hybrids (Van der Zwan 2018; Wiss 2019).

Unlike the United Kingdom or Germany, Dutch employers and labor unions have been actively involved in the policy processes leading to pension financialization. As Anderson (2019) has pointed out, financialization does not always imply the crowding out of labour market actors, such as organized employers and unions, by financial actors. In the Dutch pension system, as in Sweden and Denmark, collectivism has characterized the historical trajectory to financialization. In the Netherlands, unions and organized employers not only negotiate occupational pension plans, but also jointly manage pension fund boards and deliberate on pension policy within corporatist fora like the Socio-Economic Council (*Sociaal-Economische Raad*, SER). However, even though the involvement of unions in pension governance is said to lead to less financial risk-taking (Wiss 2015), this does not seem to be the case for Dutch pension funds: their exposure to equity markets and markets for alternative investments continues to be relatively higher (OECD 2019a). Possible explanations include unions’ agreement with riskier investment practices to sustain higher pension benefits (McCarthy et al. 2016) or the outsourcing of asset management activities to Anglo-American, for-profit financial firms (Engelen, Konings, and Fernandez 2008).

With high capitalization, the presence of large and powerful pension funds and the ongoing dissolution of DB pension promises, the Netherlands stands out from the other three cases. First, the quasi-mandatory nature of the Dutch second pillar has resulted in very high participation rates, which means that the state has not needed to intervene with public savings options such as NEST in the UK or the Riester pensions in Germany. Second, the Netherlands has seen continued involvement of labor unions in pension management. This is important in two ways. First, employers have been unable to completely abandon DB pension schemes. Instead, the renegotiation of DB pension contracts has become a sticking point for pension reform. Second, the type of self-management that is expected of workers with individual DC pensions is absent in the Netherlands. Instead, Dutch workers have very little control over how their pension savings are invested, an issue that has increasingly become politically salient. Even though the investment practices of Dutch pension funds are very similar to those in the United Kingdom, Dutch citizens experience pension financialization very differently.

Sweden

The Swedish three-pillar pension system differs substantially from the Dutch system, particularly in the first pillar. In 2019, capital-funded pension savings were 88% of GDP. Swedish public pension provisions consist of a NDC pension (*Inkomstpension*) in the first tier, a mandatory individual DC pension (*Premiepension*) in the second tier and a supplementary guarantee pension for low-income earners. Contributions for the *Inkomstpension* and the *Premiepension* are 16% and 2.5% of wages, respectively. While the *premium pension* universalizes the scope of capital-funding in the Swedish pension system, its importance is restricted by a relatively low contribution rate. In contrast to the other cases, Sweden also has several very large pension reserve funds (AP1 through AP4 and AP6). Assets in these reserve funds equal an additional 29.4% of GDP (OECD 2019a: 211). The reserve funds face investment restrictions: AP1 through 4 have legal limits on investment in particular asset classes, while AP6 invests entirely in private equity.

Most Swedish workers (90%) participate in quasi-mandatory occupational pension schemes. Contrary to the Netherlands, most Swedish occupational pensions are DC schemes, yet collectively managed by employers and unions (Lindquist and Wadensjö 2011). Compared to the Netherlands, the starting point for the renegotiation of occupational pension contracts was much earlier: already in 1996 employer group SAF and union LO agreed to switch from a DB to a DC pension plan for the private sector, with the white-collar ITP fund following suit in 2017 (Anderson 2019). Under the new scheme,

members can make their own investment choices, although restrictions exist on how much risk they can take. Employers and unions are highly involved in financial management: they jointly own the clearing houses for the SAF-LO and ITP schemes, which allows them to screen financial services providers and keep the fee structures low (*ibid.*). In this respect, the Swedish second pillar differs substantially from the United Kingdom and Germany.

While the Swedish pension system has a capitalization rate that is well below those of the United Kingdom or the Netherlands, it is still considered highly financialized because of the universalism of the premium pension (Belfrage 2008, 2017). The premium pension scheme is self-directed: individual participants must decide themselves how contributions are invested and they may choose from around 800 mutual funds. For those participants who wish to refrain from active investment, the state offers the option of a default fund (AP7). Even more so than the NEST pensions in the UK, the Swedish premium pensions were intended to “cultivate the skills and ethos of asset-based welfare” (Belfrage 2017:15–16). The Swedish reform therefore resembles the introduction of NEST in the UK and the Riester pensions in Germany, in the sense that it aims to make pension savers into investor-subjects. Still, almost half of the premium pension savers opt for the default fund. In efforts to reduce the number of mutual funds in the marketplace, the state has tightened regulatory standards. As of 2019, 553 mutual funds were still active (OECD 2019a:35).

The Swedish first pillar is unique among European welfare states, reflecting the institutional legacies of the previous pension system. Until the late 1990s, the pension system consisted of a statutory basic pension (*Folkspensionen*, which provided a universal flat-rate benefit) and a supplemental DB scheme (*Allmänna Tjänstepensionen*, ATP). The ATP scheme was managed by tripartite funds (*Allmänna Pensionsfonderna*, AP), which served an important role in the Swedish export-led growth model. Financed by employer contributions, the AP funds purchased government and corporate bonds, thereby providing cheap capital to the public and private sectors of the economy. Investment in shares was prohibited and employers could re-borrow up to 50% of their pension contributions. The result was an important complementarity between the welfare state and the industrial economy: while the pension contributions kept wages low and inflation in check, the availability of cheap capital helped Swedish firms maintain international competitiveness (Belfrage 2008).

The dissolution of the ATP system has also meant the end of the centrality of pension capital within the Swedish export-led growth model. As in the United Kingdom, however, the pension system was not immune to financial liberalization (Belfrage 2017). The

subsequent integration into global financial markets has not only affected the AP funds, which continue to exist as public sector buffer funds, but also Swedish citizens. Average investment returns on premium pension savings have suffered in the wake of the Great Financial Crisis, although the impact has been limited to the small portion of contributions flowing into the premium pension system (Sundén 2009).

DISCUSSION AND CONCLUSION

In the preceding sections, I have conceptualized pension financialization in a limiting manner by identifying four dimensions associated with the growing role of financial markets and actors in pension provision. Pension financialization is first and foremost seen as the growing reliance on capital-funded pensions within pension systems. A large scope of capital-funding is present in both the liberal and the two coordinated market economies with mature, three-pillar pension systems (United Kingdom, Sweden and the Netherlands). Germany remains a laggard in terms of both the size and coverage of its funded pension system. Pension financialization, however, also proceeds along other dimensions. In the UK, Sweden and Germany, DC pensions have begun to replace DB schemes within the second pillar. Sweden's state pension is also based on a (N)DC funding logic in two of its three tiers. Average asset allocations reveal a more uneven picture, with equity investments having more importance in the Netherlands and alternative investments in Germany and the United Kingdom. Funded pension schemes have established themselves as large, global investors most strongly in the United Kingdom and the Netherlands.

The contextualized comparison of the four cases has revealed that these patterns of financialization have evolved out of particular sticking points, created by institutional legacies within the pension system. In the UK, retrenchment of the state pension and employers' abandonment of occupational DB plans have been major driving forces towards individual DC schemes. In 2012, the state intervened by creating a public alternative in the form of the NEST auto-enrolment scheme. In Germany, voluntarism has also complicated the state's efforts to grow coverage of occupational pensions. Tax subsidies and other incentives have so far proven insufficient to tackle the substantial sustainability challenges confronting the German pension system, with its strong reliance on the statutory pension and one of the highest (projected) old-age dependency ratios in Europe. Since 2017, the German state has followed the UK example by introducing auto-enrolment in its second pillar. In both countries, the issue of coverage has therefore been an important institutional sticking point around which pension financialization has proceeded.

In some respects, the Swedish case looks similar to the UK and, to a lesser extent, to Germany. In Sweden, as in the UK, the state has also driven financialization by introducing a new DC pension, albeit in the first rather than the second pillar. Yet, the Swedish premium pension also differs in important respects from the auto-enrolment plans in the UK and Germany. Rather than an occupational pension, it is a public savings plan that serves as a second tier on top of the NDC pension. Rather than providing a private alternative to the public pension, its goal is to increase replacement rates in the first pillar. Its relatively low contribution rate (2,5%) is indicative of the schemes' supplementary role within the overall pension system. Thanks to its universalism, the Swedish premium pension has become exemplary for pension financialization. Like the UK's NEST, it has been argued to represent a public policy intervention to create a mass investment culture, bestowing personal responsibility for financial planning and literacy upon individual citizens (i.e. Belfrage 2008; Berry 2016). The need for behavioral nudges (auto-enrolment, investment defaults) in both cases also show the limitations of these policy interventions.

At the same time, Sweden continues to have a substantial second pillar of occupational pensions, similar to the Netherlands. In both countries, quasi-mandatory participation has resulted in high coverage rates, which have considerably expanded the scope of capital-funding within these systems. Quasi-mandatory participation has also limited possibilities for employers to exit the second pillar. This has meant that pressures to reduce the reliance on DB pensions had to be renegotiated with labor unions. While undergoing a similar process, Sweden and the Netherlands have had different starting points. In Sweden, discussions over DB in the second pillar led to reform in the 1990s, with unions and employers maintaining responsibility over financial management – including limited risk-taking in investment decisions. In the Netherlands, a continued reliance on DB pensions coincided with a change in portfolio allocations towards riskier asset classes. The financial crises of 2001 and 2008 caused widespread underfunding of DB plans. Since then, social partners and the state have entered a long reform process to renegotiate occupational pension contracts. They recently agreed on the implementation of a collective defined contribution scheme by 2025.

In their review of existing literature, Mader et al. (2020) have called for a conceptualization of financialization that is mechanistic in addition to being limiting and contextualized. The contextualized comparison in this paper provides a starting point to consider the underlying mechanisms of pension financialization in the four cases. In the two voluntarist systems, the institutional legacy of low coverage created institutional sticking points for the need to re-

lieve fiscal pressures on the first pillar by expanding occupational and personal pensions. In the absence of mandatory participation, the state interventions were needed to boost individual pension savings. In the two mandatory systems, the combination of high coverage and the prevalence of DB pensions created different institutional sticking points. Here, renegotiation of DB contracts became a salient political issue in the second pillar, although the timing differs for both countries. These mechanisms are of course not exhaustive. Further research needs to shed light on whether similar mechanisms apply in other countries as well, including in welfare states where policy efforts to expand financialized pensions have failed.

Pension financialization has important repercussions for the security and adequacy of old-age pensions. When pensions are capital-funded, poor in-

vestment results will translate into lower pensions, although to what extent depends on the nature of the pension contract and institutional context. The combination of stock market volatility and low interest rates since the Great Financial Crisis has threatened both the benefit levels of DC pensions *and* the funding status of DB pensions plans. The impact on the legitimacy of funded pension systems may be profound. The higher education strikes in the United Kingdom in 2019 or the historically low public confidence in the Dutch pension system show the contentious nature of pension financialization, even in countries with long histories of capital-funded pensions. Where this is the case, pension financialization may have the paradoxical effect of increasing the burden on the state, whether in the shape of regulation or in demands for better public pensions.

NOTES

- [1] Notable cases of privatization reversals outside Europe include Argentina and Chile (Orenstein 2013).
- [2] It should be noted that some influential voices have argued that neither DB nor DC schemes are inherently unsustainable. Barr and Diamond (2009) argue, for instance, that pension sustainability depends on the successful adjustment of the particular parameters of each scheme within the specific context of a national pension system.
- [3] Dixon (2008:249) defines pension fund capitalism as “a capitalism in which pension funds, financial institutions in their own right, will increasingly become the source of corporate engagement and the providers of social welfare and public infrastructure in the twenty-first century”.
- [4] Here, I draw on two theories. Esping-Andersen’s (1990) *Three Worlds of Welfare Capitalism* identifies three types of welfare states: the liberal welfare state of the Anglo-American political economies, the conservative welfare state of the continental political economies and the social-democratic welfare states of Northern Europe. Hall and Soskice’s *Varieties of Capitalism* (2001) distinguishes Liberal Market Economies (LMEs) from Coordinated Markets Economies (CMEs). While the VoC approach relates to production regimes rather than welfare regimes, its category of Coordinated Market Economies (CMEs) overlaps with the conservative and social-democratic welfare states from Esping-Andersen’s typology.

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