

THE CHANGING FACE OF RETIREMENT

THE AEGON RETIREMENT READINESS SURVEY 2012
JAPAN FACT SHEET



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KEY FINDINGS

The AEGON Retirement Readiness Survey 2012 reveals a stark set of findings for Japan.

THE NEED FOR A STEP-CHANGE IN SAVINGS BEHAVIOR

- Japan finds itself in an exceptional position in acknowledging the need to save to a greater extent than in other countries surveyed. Yet, it also reveals that few people are actually undertaking personal retirement planning and only 2% feel they are currently saving adequately.
- 62% of Japanese employees strongly agreed with the statement that the value of their future state pension benefits is likely to be reduced as a result of the financial crisis. This compares with 46% of employees across the ten country survey.
- Half (50%) of Japanese employees strongly agreed with the statement that their employer is likely to reduce the value of workplace pension benefits as a result of the financial crisis. This compares with 27% of employees across the ten country survey.

A MORE FLEXIBLE APPROACH TO ENTERING RETIREMENT

- Japan's working age population shows significant flexibility on how they expect to transition into retirement. Whilst 50% of current retirees surveyed immediately stopped all work upon retirement, only 14% of current employees believe they will do so, and 11% believe retirement age will have no impact on their working patterns at all.
- That Japanese respondents do not equate retirement with stopping working altogether is not surprising given that while the formal retirement age in Japan is set at age 60, effective retirement ages are much higher as employees typically choose to remain in paid employment beyond that age with another employer.
- Against the backdrop of current government pension reforms which seek to increase retirement ages from 60 to 65 years, we find the public supportive, only 13% of Japanese respondents think that retirement ages should remain unchanged.
- In every other country surveyed, including the US where respondents were generally quite flexible in their approach to working and retirement, we found that people were more wedded to current retirement ages than is the case in Japan.

- Among Japanese respondents the consensus view is that people should keep working until they reach age 65. This figure was in line with most other countries though lower than the UK, who are willing to work to 67 and where retirement ages are currently being increased to 68 years (by 2043).

LEVELS OF PERCEIVED RETIREMENT READINESS

- In the AEGON Retirement Readiness Index, a measure of how employees perceive their preparedness for old age, Japan scored just 4.6 out of 10. This was the lowest level of preparedness across the ten countries, lower even than Hungary which scored 4.8 even though it does not share Japan's historically high savings ratios.
- Currently, just one-in-five people (20%) claim that they are regularly saving for retirement which, along with Poland, was the lowest level of habitual savings behavior in our ten countries. By contrast, in Sweden habitual savers made up 45% of respondents.

FILLING JAPAN'S FUTURE RETIREMENT INCOME NEEDS

- Japanese people have a high level of awareness about the need to save for retirement, with 50% claiming to feel 'very responsible' for ensuring themselves a sufficient retirement. They also show a high level of understanding about the need for greater personal responsibility.
- Despite the high awareness about the need for personal responsibility, and the general belief that the value of state pensions will decline, 67% still think that the state will make up part of their retirement income with 46% who think that the state will provide the biggest single source of retirement income – this level is twice the global average across the ten countries surveyed.
- Personal pensions are not seen as a mainstream solution to funding retirement. Typically less than 1-in-6 people mentioning defined benefit plans (provided by the employer) and fewer still citing a defined contribution plan. Many more people – 58% - think that they will instead rely on cash savings with less than one-third using insurance policies.

CHANGING HOUSEHOLD ATTITUDE TO INVESTMENT RISK

- Five years of financial crisis has made respondents more risk averse. 50% of employees are now less willing to countenance investment risk than they were before the financial crisis.
- As a result, in Japan we see a demand for investment products which can mitigate the risks inherent in volatile markets. 55% of respondents agreed that the financial crisis has made such investments more important to them while nearly half (47%) felt strongly that financial products which protect their capital against poor investment returns are important to them.

INTRODUCTION

JAPAN'S 'SILVER CENTURY': ADDRESSING THE GROWING NEEDS OF AN AGING POPULATION

All of the countries researched as part of the AEGON Retirement Readiness Survey 2012 are faced with an AGING society. Yet, Japan finds itself at the forefront of this demographic trend in experiencing what has been called its "Silver Century". The country already enjoys the highest life expectancy in the world. Life expectancy at age 65 is currently 20.7 years, compared with an OECD average of 18.1 years.ⁱ Life expectancy is predicted to exceed 90 years for women by 2050.ⁱⁱ According to data released in September 2012, Japan now has more than 50,000 centenarians while Japan's women rank second in the international life expectancy table behind only Hong Kong.ⁱⁱⁱ

This trend towards an AGING society has combined with one of the lowest birth rates.^{iv} As a result, Japan's population is not only aging but it is also set to shrink in the coming century.

By 2050, the population is projected to decline from 128 million in 2011 to just 97 million. At the same time, the percentage of persons 65 years and older will according to The Institute of Population and Social Security Research account for 40% of the total population in 2060. In 2010, the elderly accounted for 23% of the population.^v The number of persons in the workforce will decline by half from current levels.^{vi} The Japan Institute of Population and Social Security Research (IPSS) projects that, by 2050, there will be 31 million fewer Japanese between ages 15 and 64, and that this group will shrink from two-thirds of the population today to just over half.^{vii}

Japan is addressing these demographic problems by developing policies to help extend working lives beyond current retirement ages and efforts to boost fertility rates.^{viii} The passing of the Child Care and Family Care Leave Law in June 2010 provides fathers with an opportunity to take up to eight weeks of leave after the birth of a child and allows employees with pre-school age children additional allowances such as up to five days of leave in the event of a child's injury or sickness and opportunity for shorter working hours and flex time for employees.^{ix} Japan is also seeking to increase retirement ages from 60 to 65 years in line with other countries.

THE SURVEY

The research was conducted among more than 10,000 people in ten countries.^x Respondents were interviewed using an online panel and interviews were conducted during 2012. The interviews dealt with a wide range of issues covering attitudes towards retirement preparedness, the roles of government and employers in providing pensions, and the impact of the financial crisis on attitudes to issues such as investment risk and retirement planning.

The survey included 9,000 employees and 1,000 retired people to provide a contrast between the responses of current employees and those already in retirement. The research did not include the unemployed, long-term disabled or the self-employed as each of these groups faces specific challenges in planning for retirement. Instead, the objective for this survey is to provide a broader perspective based on the mainstream working population.

PART 1: THE CHANGING NATURE OF RETIREMENT

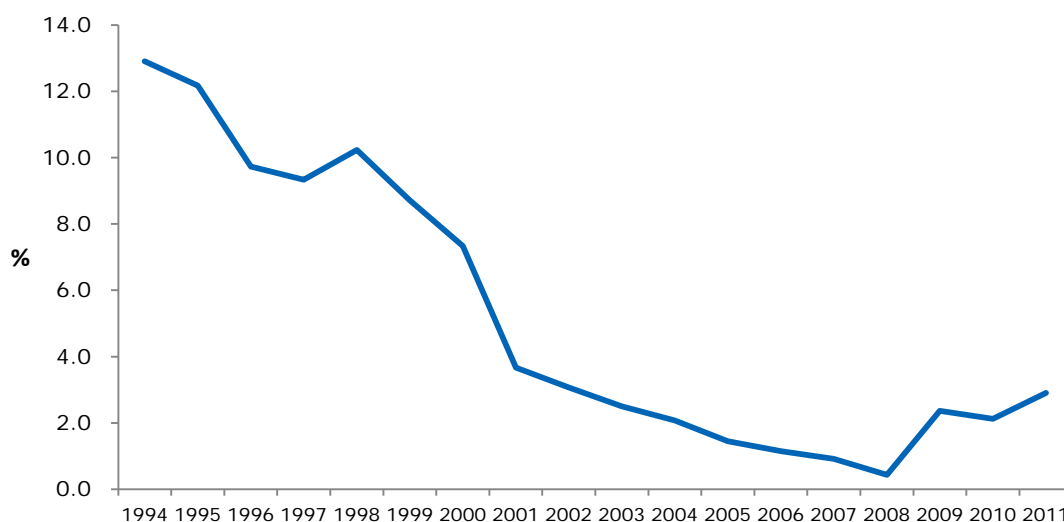
THE RAPID DEMISE OF HOUSEHOLD SAVINGS RATIOS IN JAPAN

Throughout the latter half of the Twentieth century, the Japanese were internationally renowned for their appetite to save. As a nation which was rapidly industrializing, a large part of the increasing levels of household incomes were invested for the future. The household savings ratio during the 1980s saw the Japanese save around 15% of their after-tax incomes.^{xi} Similar behaviors are being observed now in countries like China and India as they too develop and their economies generate improvements in household incomes.

Since the turn of the late 1990s, Japan has witnessed the sort of collapse in the savings culture seen in other developed countries. From the mid-1990s

through to today we can see this trend has accelerated. Partly this is simply due to the impact of a demographically aging society: life-cycle theory suggests that as more Japanese people enter retirement their propensity to save declines as they start to spend their past savings. This has the effect of dragging down the overall average savings ratio. Data shows that the collapse in Japan's savings has been particularly concentrated among older employees and those above the age of 60 who are now using up their lifetimes savings at a much faster rate than during the mid-1990s.^{xii} Other factors have also played a role including the economic impact on household incomes as a result of the lost decade and housing costs. Put simply, savings rates are declining as income growth rates stagnate.^{xiii}

Chart 1: Japan's household savings ratio as a percentage of disposable household income (1994-2011)^{xiv}



The AEGON Retirement Readiness Survey 2012 findings show how the collapse in Japan's savings rates has been so stark that household savings behavior now lags behind that in all of the other countries we surveyed. Today, less than 20% of Japanese people claim "I always make sure that I am saving for retirement". This figure was towards the bottom of the international rankings alongside Poland. This compared with a peak of 45% witnessed in Sweden and rates in excess of 40% in the US and Germany. However, there was a silver lining in these findings. While Japan had a relatively high number of people who are not currently saving for retirement it also displays a relatively large number of people who said that "I am not saving for retirement though I do intend to" which made up 34% of all Japanese respondents.

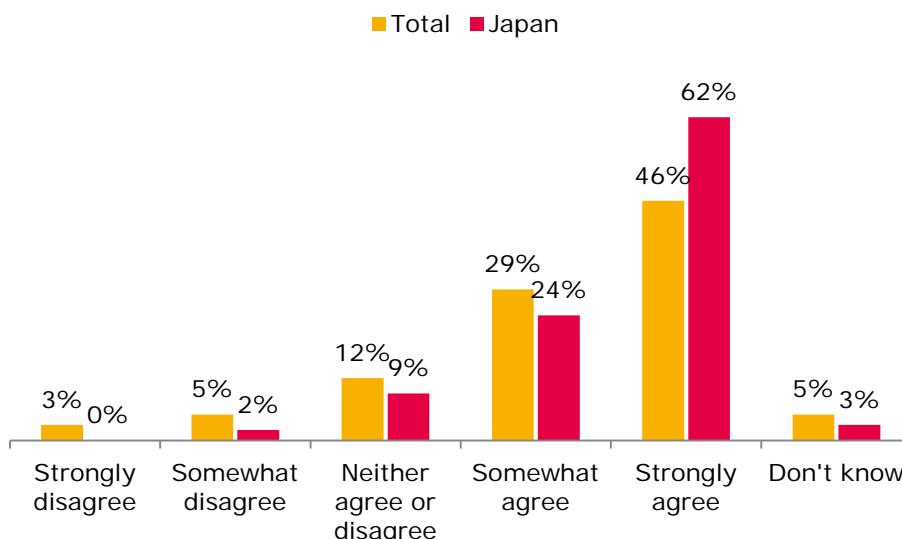
This demonstrates that while Japan needs to change its current household savings behaviors, there is high awareness of the need to save for retirement alongside a willingness to do so. These findings reveal Japan to be a nation of subdued savers: people aren't saving enough, possibly because of financial constraints created by stagnating household incomes, but they recognize the importance of saving and intend to do so at some point in the future. It is vital for Japan that these savers can be encouraged to change their ways.

PESSIMISM ABOUT ACHIEVING A COMFORTABLE RETIREMENT

It is vital because without a boost to household savings it looks uncertain that Japan will be able to provide the sort of income replacement ratios in retirement that will be necessary to ensure that people can maintain a comfortable lifestyle. While Japanese people share broadly similar aspirations for retirement as in the other survey countries, such as spending more time with friends and family, pursuing new hobbies and travelling, they are less optimistic about enjoying a comfortable retirement in their old age. Only 6% of Japanese employees think that they are on course to achieve their retirement income compared to 15% in the other nine countries. Not surprisingly therefore, one-third (31%) are somewhat or very pessimistic about when they will be able to retire. Nor are the worries about retirement simply financial with 34% pessimistic about maintaining good health.

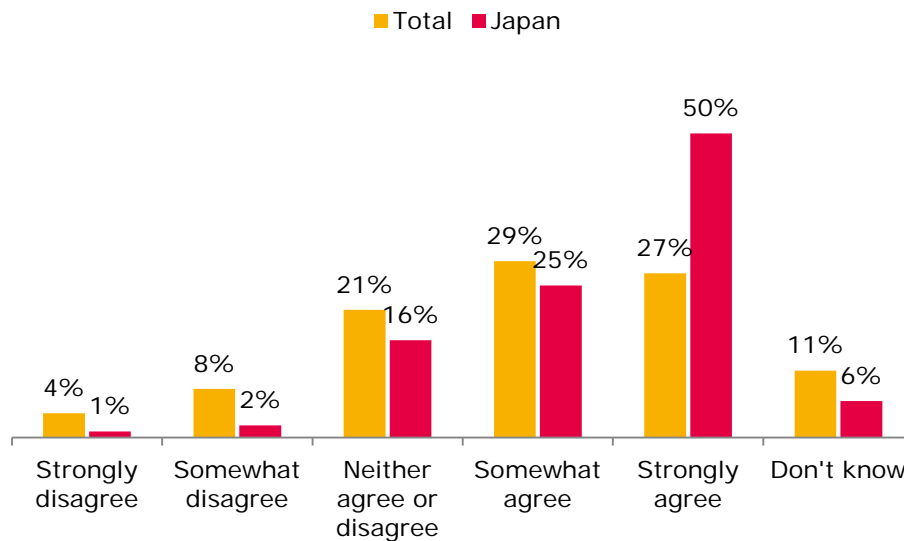
When looking at the three main sources of potential retirement income it is clear to see what is driving this concern, namely fears about the future prospects for current levels of state and workplace pension benefits. Even though state replacement income rates in Japan are lower than in the other countries we surveyed^{xv} (though this does not take into account Japan's generous company pension schemes), many people feel that the current levels of benefits are no longer sustainable as a result of the impact of the financial crisis on retirement plans. 62% of Japanese respondents thought that their state benefits would be reduced due to likely cuts in government spending compares with 46% in the rest of the world. Even more strikingly, 50% strongly agreed with the statement that employers would be more likely to cut back on workplace pensions, which compares to just 27% in the rest of the world. Given the importance of the state and employers in generating Japanese retirement incomes, the fact that respondents were far more pessimistic about what will happen to those two sources of income illustrates part of the major challenge facing Japan.

Chart 2: The Japanese believe their state pensions are to be cut



Q: To what extent do you agree with the following statements concerning the impact of the financial crisis on your retirement plans – My state pension benefits will be less valuable due to government cutbacks

Chart 3: Japanese respondents agree that their workplace pension benefits are likely to become less generous in future

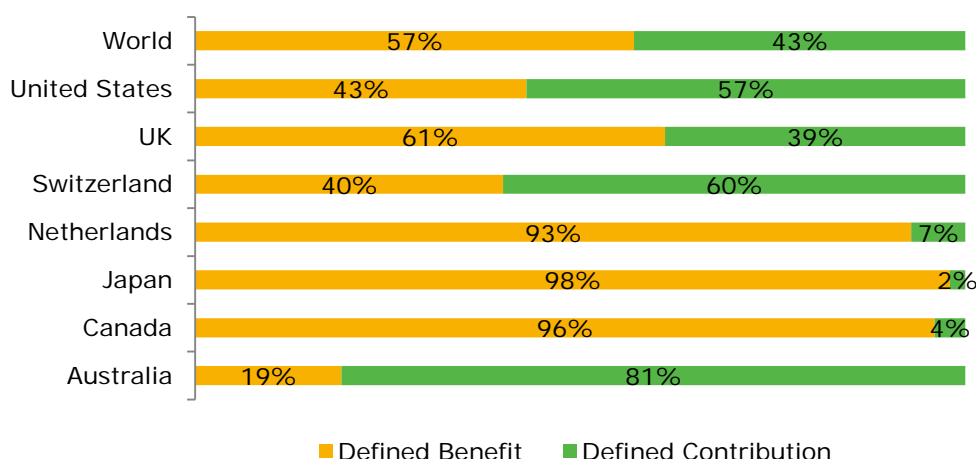


Q: To what extent do you agree with the following statements concerning the impact of the financial crisis on your retirement plans – My employer or pension fund is more likely to cut back on workplace pension benefits

That the fears about the future role of the employer is so strong as a major concern given that employers play a more prominent role in Japan than almost anywhere else, as can be seen in the strength of defined benefit pension plans, where an employer promises a specified benefit in retirement based on factors such as earnings and tenure of service.

Much of the rest of the developed world has moved towards defined contribution plans, where employer's (and usually employees) contribute a specified amount to a fund over time, and the eventual benefits fluctuate based on investment returns. Whereas 81% of Australians pensions assets are in defined contribution pensions, demonstrating the importance of its state-mandated defined contribution scheme, in Japan that figure falls to just 2%: more traditional forms of employer-sponsored pension provision remain dominant.

Chart 4: Defined Benefit pensions dominate in Japan compared to defined contribution^{xvi}



This heavy reliance on defined benefit schemes has many positive results in terms of boosting incomes in retirement, especially in terms of higher contribution levels from employers as we examined in greater detail in our recent report The Changing Face of Retirement: The Workplace Perspective (2012).

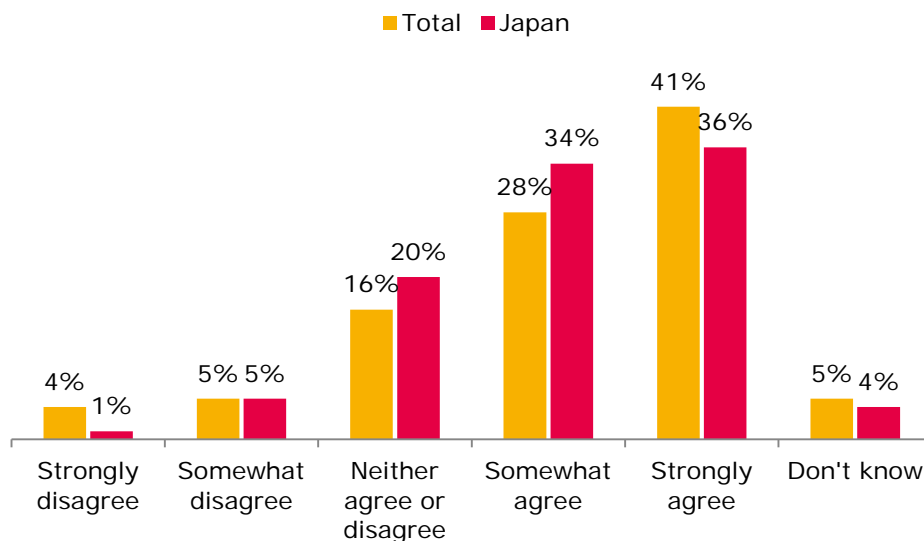
However, it can also lead to some negative outcomes such as lower employee engagement in pension planning. As one employer case study commented in our workplace perspectives report "Defined Benefits do not encourage people to think about their retirement".

**CHANGING PATTERNS OF RETIREMENT:
ENCOURAGING FLEXIBLE RETIREMENT**

A significant outcome arising from the financial crisis and its potential impact on Japan's pension system is the acknowledgement that people will just have to keep working in order to make good any shortfalls in income. 70% of Japanese employees believe that the

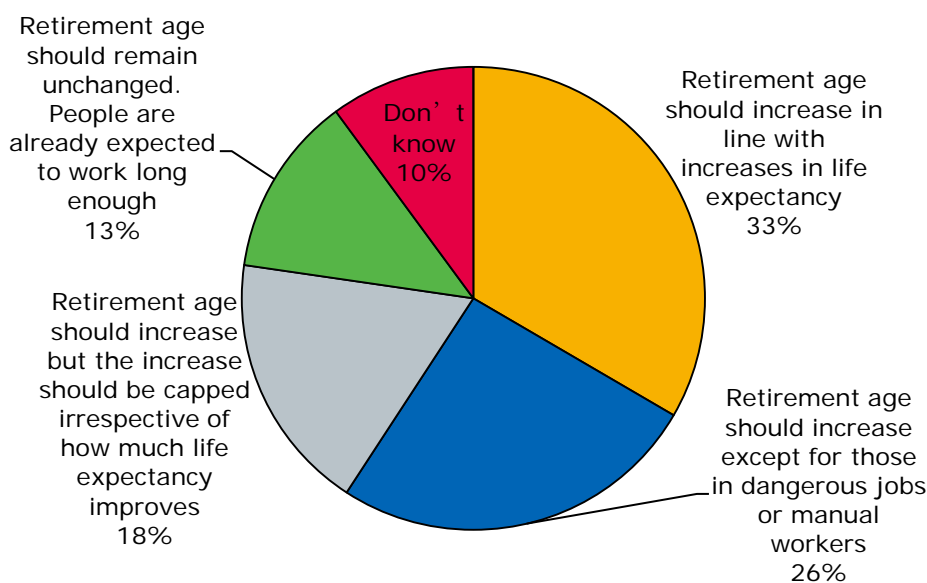
economic turmoil of the last five years will result in them having to work longer. However, unlike in some other surveyed countries – particularly in continental European countries, many of which have recently undergone unpopular pension reforms – we see that Japanese employees are generally willing to accept this change.

Chart 5: A majority agree that the financial crisis has created a need to work for longer



Q: To what extent do you agree with the following statements concerning the impact of the financial crisis on your retirement plans - I will have to work longer to provide my desired income in retirement

Chart 6: Few Japanese employees believe that retirement age should remain unchanged

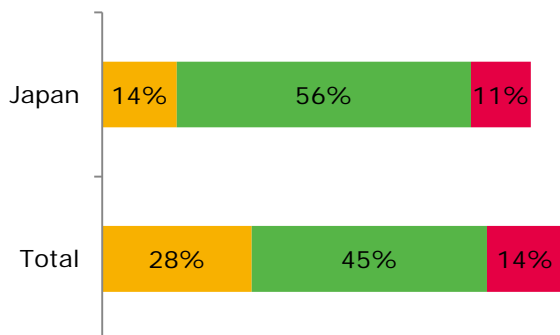


Q: To what extent do you feel that people should expect to work longer into old age as a way to offset the costs of people living longer?

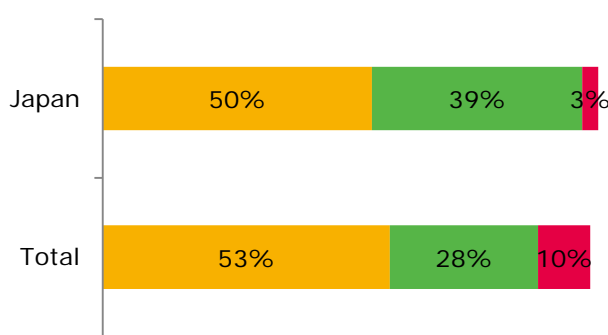
Charts 7 and 8: Japanese employees are willing to work into retirement

CURRENT EMPLOYEES

RETIREES



- Immediately stop work
- Change work patterns
- Continue working



- Immediately stopped work
- Changed work patterns
- Continued work

Q: Looking ahead, how do you envision your transition to retirement/Looking back, how did your transition to retirement take place?

Given the AGING Japanese population, it will likely be necessary in future for steep increases in retirement age if the current retirement benefits system is to remain intact. Therefore it is fortunate that the population is on the whole accepting of the need for such change, with only 13% believing that retirement

ages should remain unchanged. Moreover, less employees in Japan than anywhere else surveyed see the transition to retirement as a straightforward end to work. Instead, they are willing to change work patterns or indeed simply carry on working for as long as possible.

PART 2: THE AEGON RETIREMENT READINESS INDEX IS JAPAN SAVING ENOUGH?

In spite of decades in which Japan achieved high levels of household savings our findings show how the country is lagging behind other countries. By 2011, Japan's pensions system had successfully accumulated US\$3.3 trillion in assets (Table 2). While this potentially constitutes a major source of retirement income, when taken as a proportion of GDP (55%) Japan lags behind other major economies with a number of countries where pension assets are

currently larger than GDP (among countries included in our survey this included the UK (where pension assets total 101% of GDP), the US (107%) and the Netherlands (133%). This demonstrates that at a macro-level Japan is less prepared to meet the challenges of an aging society. Based on current trends this preparedness gap with other major economies is potentially growing.

Table 1 – Total pension assets in 2011 as a proportion of GDP^{xvii}

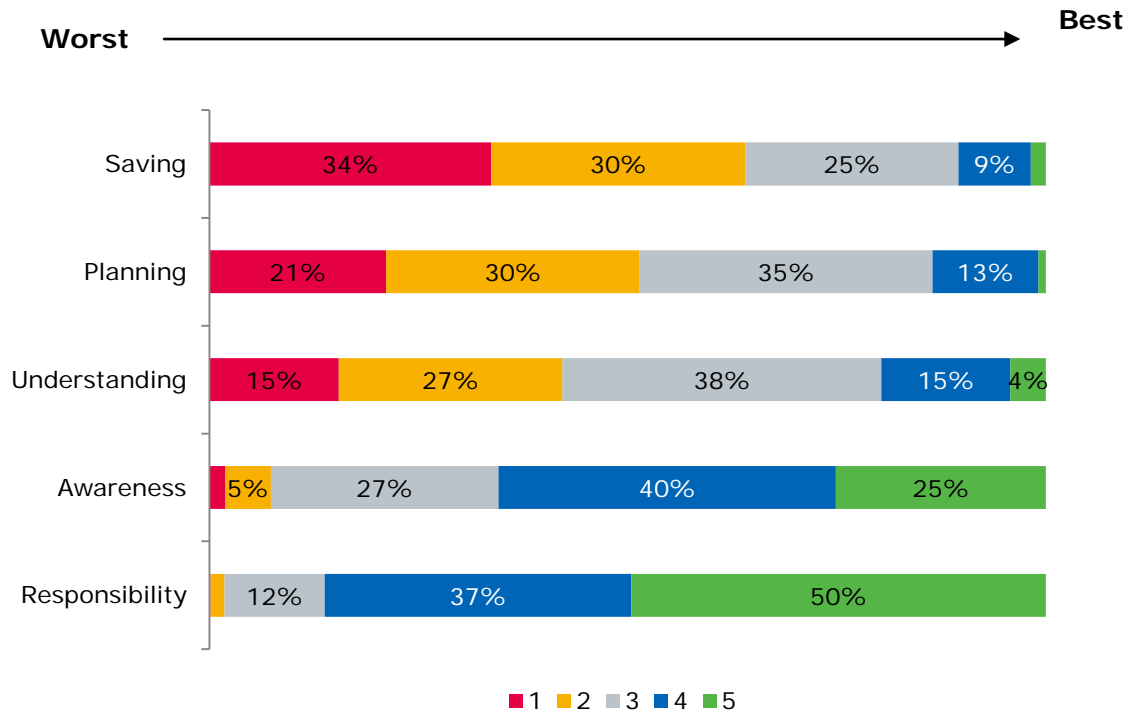
	Total Assets 2011 (USD billion)	% GDP (local currency)
Australia	1,301	96%
Brazil	321	15%
Canada	1,303	78%
France	129	5%
Germany	468	14%
Hong Kong	84	34%
Ireland	101	50%
Japan	3,363	55%
Netherland	1,046	133%
South Africa	227	62%
Switzerland	693	115%
UK	2,394	101%
US	16,080	107%
Total	27,509	72%

THE NEED TO INCREASE PERSONAL RESPONSIBILITY FOR PLANNING RETIREMENT

We can also see how at the micro-level how household behavior is also reflecting negatively on people's perceptions of their retirement preparedness. The AEGON Retirement Readiness Index (ARRI) revealed that Japanese respondents feel that they are less ready for retirement than in any of the ten countries we surveyed. To calculate

the ARRI score we asked employees to score themselves from one to five on a series of issues, from their understanding of the need to save towards retirement to the extent to which they are actively doing so. As Chart 9 shows, whilst there are high levels of personal responsibility in Japan, this is not translating into adequate planning or savings behavior when it comes to retirement, with 34% admitting that they are hardly saving at all towards their old age.

Chart 9: A lack of adequate savings behavior in Japan



Respondents were asked to rank their retirement attitudes and behaviors in terms of responsibility, awareness, understanding, planning and saving on a scale of 1 to 5, with 5 being best.

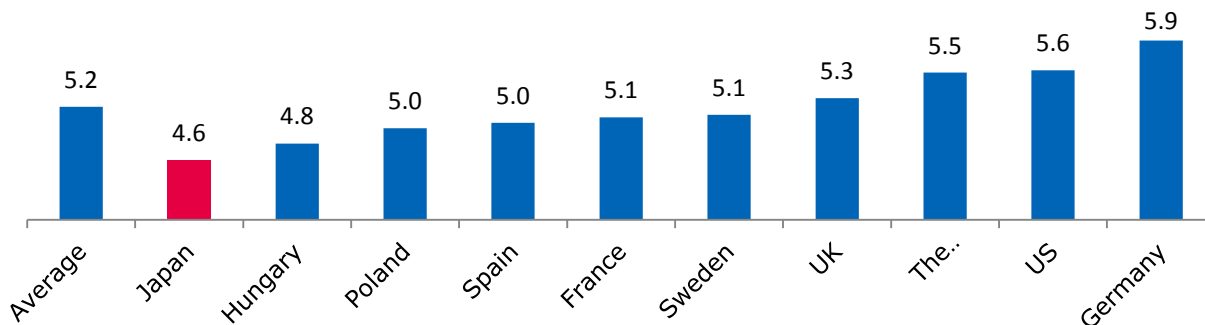
The responses to these six questions were weighed in the ARRI based on their importance in determining a respondent's saving profile, and an overall score out of ten for each respondent generated. The most important determinants were found to be their behaviors towards their own planning and saving, as well as how on course they were to achieve their desired replacement income.

As Chart 10 shows, Japan placed last out of the ten countries surveyed. Mention responses to Q7. Japanese respondents are taking responsibility for their retirements, as shown by Chart 9 above, however this seems not to be translating into proactive savings behavior, and this is putting retirements at risk.

The AEGON Retirement Readiness Index (ARRI)

To calculate the index scores, the index incorporates the responses of 9,000 employees surveyed across the ten countries. Each of the respondents was asked a series of questions to provide a cognitive assessment of their current retirement attitudes and behaviors. The survey asked three questions covering attitudes: whether employees accept personal responsibility their retirement income, whether they are aware of the need to plan for retirement, and their understanding of retirement related financial matters. It also asked three questions covering behaviors: the extent to which employees have put retirement plans in place, whether they are adequately saving for retirement, and whether they are on course to achieve their required replacement income in retirement.

Chart 10: Japan scores the lowest on the AEGON Retirement Readiness Index (out of 10)



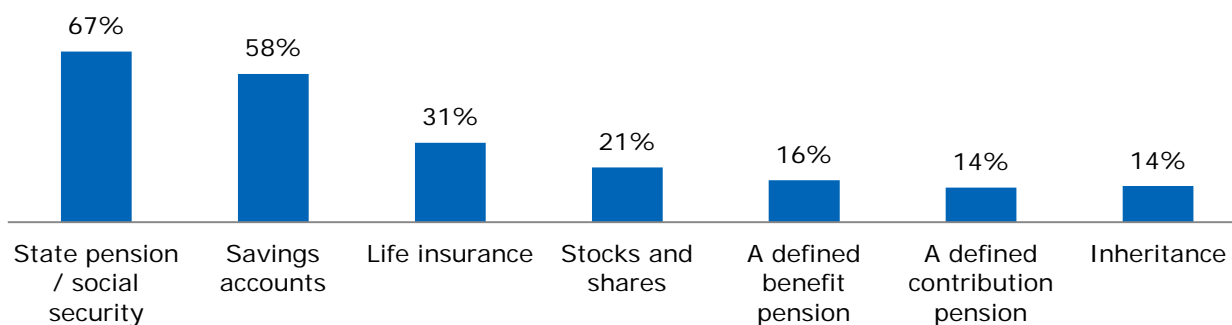
Q: AEGON Retirement Readiness Index created by weighting the responses to six questions related to retirement readiness according to statistical importance.

Based on current performance Japan needs to undertake a step-change in its approach to how it plans for retirement. Even without taking into consideration the decline in household savings ratios, the fact that Japan has been experiencing lower economic growth since the beginning of the 'lost decade' in the early 1990s, along with lower performing equities markets reducing returns to pension funds, will have a serious long-term impact on the retirement prospects of Japanese citizens.

WHICH PRODUCTS WILL HELP FILL JAPAN'S FUTURE RETIREMENT INCOME NEEDS?

When looking at what kind of insurance products could potentially help Japanese households better prepare for their retirement it is clear that the concept of 'pensions' remain secondary in people's estimations. This could be largely because there is a general perception that the state will provide an important source of retirement income with 67% saying that this will make up part of their retirement income. 46% think that the state will provide the biggest single source of retirement income – this level is twice the global average across the ten countries surveyed.

Chart 11: Sources of retirement income for Japanese employees



Q: What financial means are you currently using to prepare for your retirement?

The next most popular source is savings accounts on 58%. Only one-third mentioned life insurance. The various forms of employer and private pensions are not seen to be mainstream sources of future retirement income with typically less than 1-in-6 people mentioning defined benefit plans (provided by the employer) and fewer still citing a defined contribution plan. Personal pensions are seen as being as important as financial bequests.

In spite of this potential reliance on the state and cash savings, there was widespread acknowledgement – supported by 74% – that it is important to have as many sources of retirement income as possible to spread out any risk. This issue of managing risk is something which many people are keenly aware of, particularly post-financial crisis with an environment of low interest rates and investment returns.

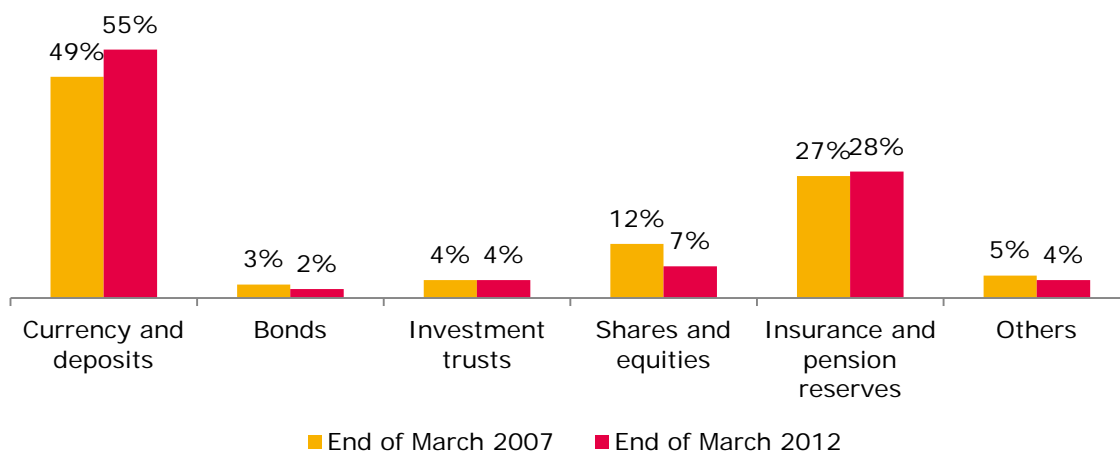
- In spite of Japan's recent experience of low inflation (and deflation) we still find that there are 43% who would be interested in protecting their investments against inflation. This might seem high but is very low by international comparisons. For example, 74% of respondents in Poland would be interested in protecting against inflation.
- Perhaps more significantly, nearly half (47%) felt strongly that financial products which protect their capital against poor investment returns are important.

- 41% would like a product which continues to provide an income to their spouse in the event that they should die before their spouse.

CHANGING ATTITUDES TO INVESTMENT RISK

Whichever financial products are used to help Japanese people prepare, it is not simply a matter of encouraging Japanese people to save more for their retirement but also recognize that the way they are saving is changing as Japanese households seek to "de-risk" their long-term savings and investments.

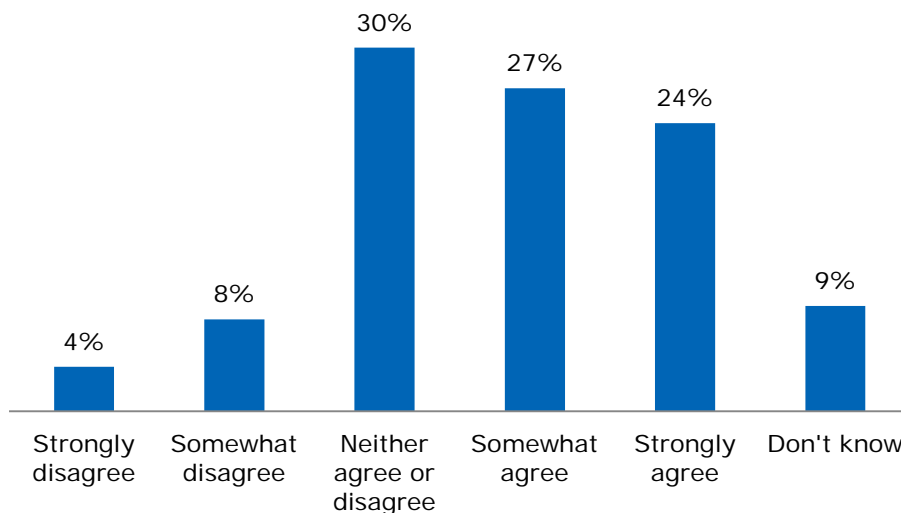
Chart 12: A shift towards lower risk savings products^{xviii}



There has also been a significant shift since the onset of the financial crisis towards lower risk savings products with over half (55%) of Japan's household financial assets now held in currency and deposits. This has increased by 6% in just 5 years. Insurance and pension reserves make up 28% of household assets with relatively low household exposure to investment trusts and equities. Confidence in equities

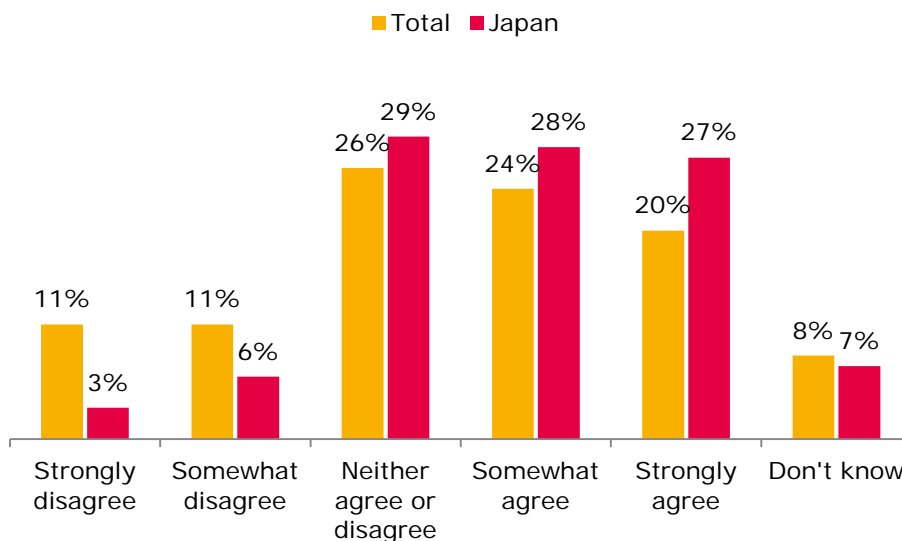
has been particularly hit by the recent financial crisis, demonstrating a lack of consumer faith in the potential for higher long-term returns from equity investments. Our survey findings reveal that exactly 50% of Japanese employees say that as a result of the financial crisis they will take fewer investment risks when it comes to saving for their retirement.

Chart 13: A half of Japanese employees are now more risk averse than before the financial crisis



Q: To what extent do you agree with the following statements concerning the impact of the financial crisis on your retirement plans – I will take fewer risks when it comes to saving for my retirement.

Chart 14: Employees want investments which protect against volatile markets



Q: To what extent do you agree with the following statements concerning the impact of the financial crisis on your retirement plans - I am looking for investment products which offer greater protection against volatile markets

As a result of this more risk-averse investment approach Japanese households are more likely than in other survey countries to be looking for investments which protect against volatile investment markets. This change in investment risks appetites meant that 55% of Japanese respondents either strongly or somewhat agreed with the statement that it was now more important to them to protect their

investments against volatility as a result of the financial crisis. A large minority of respondents also acknowledged that the financial crisis had given rise to greater need for professional financial advice to help them make sense of uncertain investment markets. Over one-quarter (26%) somewhat agreed that they now needed more advice and one-in-six (16%) strongly agreed.

CONCLUSIONS: LOW RETIREMENT READINESS AND ITS WIDER IMPLICATIONS

Japan urgently needs to review how it approaches retirement planning. This is true at the government level – as can be seen with the ongoing reforms to make the retirement age more flexible – as well as with the need to reform the relationship between all of the social partners including employers and employees. This highlights the potentially growing role for the private insurance model in meeting future funding requirements. The dramatic fall in household savings will have wider implications not only for individual households but there will also be significant ramifications for the government.

If households continue to save at the low levels witnessed in recent years, and employers cut back on the generosity of existing final salary pension funds, as anticipated in our findings by today's working population, then the pressure on the government to fill the income shortfall through more generous provision of public pensions will become even greater. As our findings show, even though nearly two-thirds of respondents actually expect the value of state pensions to fall, 46% still expect the state to provide them with their main source of retirement income. Given the state of the fiscal deficit, relying on the state to this extent could be difficult to sustain. By 2011, Japan's government debt to private GDP was 230%, having moved sharply higher during the financial crisis^{xix}.

The collapse in Japanese household savings ratios could have wider implications beyond the state of household finances in old age. The Financial Times reported in 2010 that Japan could face problems in running a fiscal deficit arguing that it has only survived this long because foreigners don't buy Japanese bonds. Through savings and insurance companies that are directly or indirectly controlled by the state, 94% of all JGBs have been bought by the Japanese. The three largest holders of Japan Government Bonds (JGB) are the Japan Post Bank, Japan Post Insurance and the Government Pension Investment Fund (GPIF).^{xx} In the recent past, Japan has been able to manage its high levels of public debt by having a ready supply of domestic savers keeping interest rates low. Even now, high levels of savings in the corporate sector have meant that Japan is still able to export capital in spite of its fiscal deficit and low household savings ratios.

However, there is a risk that rising interest rates and reductions in net business saving will bring Japan's current-account surplus to an end. And Japan will be left to finance levels of public debt which are already highly unfavorable when compared with Eurozone countries such as Greece (where public debt equals 161% of GDP), Italy (120%) and Spain (68%)^{xxi}. If Japanese households choose to continue to spend today rather than save for tomorrow, then funding Japan's public deficit will become markedly more challenging in future years compared to the recent past.

DISCLAIMER

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- ^{viii} Ministry of Health, Labour and Welfare, "Introduction to the Revised Child Care and Family Care Leave Law," <http://www.mhlw.go.jp/english/index.html>
- ^{ix} *Ibid*
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