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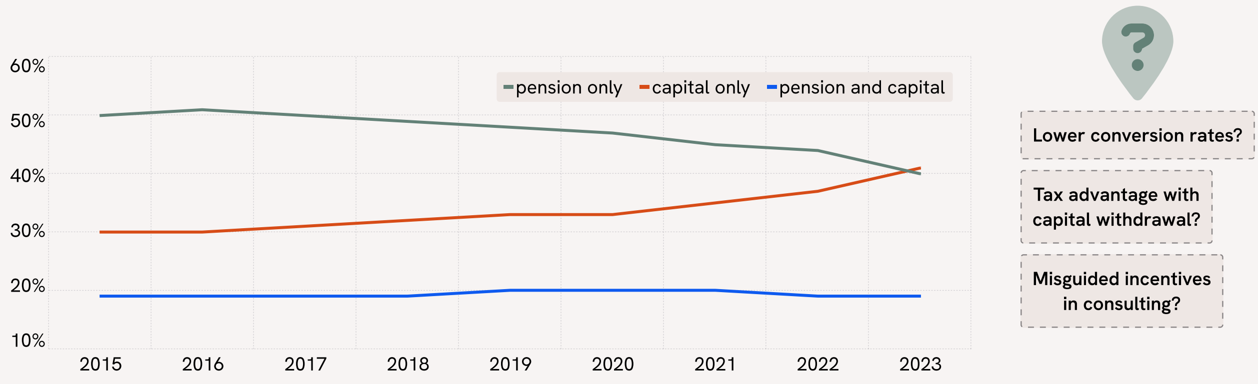
Economico Flash ⚡ #37

Why are capital withdrawals in the 2nd pillar exploding?

Chart of the week: Development of pension and lump-sum payments in the 2nd pillar from 2015 to 2023



Source: New pension statistics from the Federal Statistical Office (FSO), 2015-2023

There has been much to read recently about the rapid rise in lump-sum withdrawals in the 2nd pillar. In the search for causes, the three arguments 1) Reduced conversion rates 2) Tax advantages for lump-sum withdrawals and 3) Misguided incentives from the industry in advisory services lead the hit list by a wide margin. In the following, I will get to the bottom of these three arguments.

First of all, the following should be mentioned with regard to the chart of the week: the proportion of 100% lump-sum recipients is growing rapidly at the expense of 100% pension recipients. By contrast, the number of insured persons drawing a mixed form of pension remains at a consistently low level. This finding is irritating because there are some good reasons for a mixed form. Do insured persons make rational decisions? Now to the reasons in detail:

- **Reduced conversion rates**: A conversion rate of 5% implicitly includes a lifelong return or interest guarantee of around 2.0%. Depending on the family situation (eligible partner, individual life expectancy), this interest guarantee is higher or lower (see Flash 5 for details). In the last Flash 36, we showed that a net return of 2.0% on own investments can only be achieved with a high equity risk and cost discipline in implementation. The "Annuity or lump sum?" study by the Publica federal pension fund is also interesting in this context. This revealed that the lump-sum withdrawals of single and married persons are increasing in equal measure (see p. 12). This is despite the fact that the pension implies a significantly higher interest guarantee if one partner is entitled to it.
- **Tax advantage for lump-sum withdrawals:** As things stand today, lump-sum withdrawals have an advantage over pensions. However, the indirect tax effects of lump-sum withdrawals (see Flash 13) make this advantage smaller than many people are told. If the lump-sum benefit tax is highly progressive, as is the case in the canton of Zurich, for example, a pure lump-sum withdrawal with high retirement assets is already not the most tax-optimized solution. If, according to current plans, lump-sum withdrawals are then additionally taxed at federal level, pure lump-sum withdrawals will no longer be the tax-optimized solution in many places.
- **False incentives in advisory services**: It is a fact that bank or insurance advisors can only earn money with you or your capital if they can convince you to make a lump-sum withdrawal (and reinvest in their own products). The Publica study found that the most frequent users of external advice were pure capital withdrawers...

As a result, it must be questioned whether the decision "pension or lump-sum" is made today in the best economic self-interest.

Takeaways

- My opinion: Misguided incentives in advice are mainly responsible for rising capital withdrawals
- Independent advice on the question of "capital or pension" is crucial.