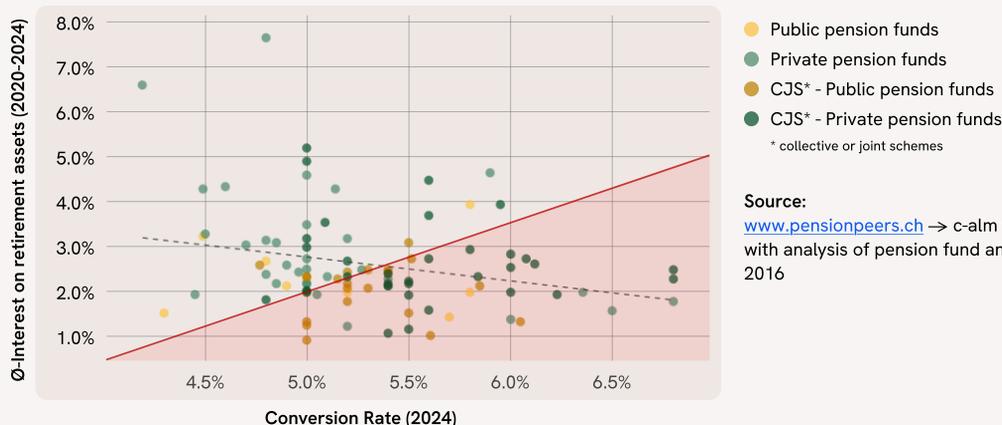


# Economico Flash ⚡ #51

Cost-benefit ratio of a pension fund: Benefits



Chart of the week: Assessment of a pension fund's performance



The core function of a pension fund is to generate the highest possible retirement benefit from the contributions paid in. The **two key factors** in this process are the **annual interest rate on the retirement savings** of the employees and the **conversion rate**, which is used to convert the available retirement savings into a guaranteed, lifelong pension upon retirement. We have illustrated precisely these two key factors in this week's chart, using the average interest rate for the last five years (2020-2024).

You want to be in a **pension fund with high benefits!** Referring to this week's chart, this means you want to be insured with a pension fund that ranks in the upper right corner, meaning it offers both above-average interest on retirement savings and an above-average conversion rate.

The **fairness of a pension fund's benefit structure** is also crucial when evaluating benefits. A pension fund located in the bottom right of this week's chart has a high conversion rate, but its retirement savings accrue below-average interest. Great for retirees, less so for working members.

We consider **benefits fair** when, on average, working members receive at least the same (interest) benefit as retirees. The compensation for active members can certainly be somewhat higher, as they, along with their employers, share the risk of having to restructure the pension fund in the event of a stock market downturn.

To compare the benefits and interest rates of active members and retirees, the guaranteed interest rate – according to [Economico Flash 5](#) – must be derived from the conversion rate. A **conversion rate of 5%** implies a lifelong **interest rate guarantee of approximately 2%**, while a conversion rate of 6%

implies a guarantee of 3.6%. You can determine the guaranteed interest rate for your conversion rate using our [calculation tool](#).

If you repeat the calculation of the guaranteed interest rate for different conversion rates, the red line illustrated in this week's chart emerges. Pension funds located on this line have, over the past five years, granted an average interest rate on retirement savings that exactly matches the guaranteed interest rate from the current conversion rate. However, for those pension funds located within the red-hatched triangle, the interest benefit for active members has not reached the guaranteed interest rate from the conversion rate. These pension funds have a so-called "redistribution problem": The (new) retirees are overcompensated compared to the actively insured, which in our view should be avoided in the long term.

## Takeaways

- **High benefits = High interest rate & high conversion rate**
- **Fair benefits: Interest rate  $\geq$  interest rate guarantee from conversion rate**