CHALLENGES OF REFORMING THE ACCUMULATED PENSION SYSTEM IN GEORGIA

David Tchiotashvili
Doctor of Economics, Professor
Gori State University, Gori, Georgia

Khaliana Chitadze
Doctor of Economics, Assoc. Professor
Gori State University, Gori, Georgia

Summary: Implementation of well-timed and successful reforms is an important cornerstone of economic strength in Georgia. An important element of economic development and long-term economic growth is the reform of the compulsory cumulative pension system, which began in Georgia in 2019 and is being successfully implemented to this day. But, the problem is that the implementation of any long-term and large-scale reform faces certain challenges that require a deep analysis of the reform and the development of effective mechanisms for sustainable development. Due to the low investment culture of the society, the reform of the cumulative mandatory pension system has great social importance and is characterized by high public interest.

Keywords: Pension system, cumulative pension reform, pension insurance, pension risk, pension scheme.

Introduction:
Due to society’s low investment culture, people often do not or cannot save voluntarily to ensure a stable and happy old age. The financial stability of the society at the retirement age is an important achievement of any country and is a solid foundation for the development of the social economy.

It is known that voluntary pension schemes did not work in many countries, including Georgia. Therefore, from January 1, 2019, a new mandatory cumulative pension system entered into force in Georgia, in which all employed citizens of Georgia and citizens of foreign countries permanently residing in Georgia automatically joined.

Mandatory pension system can be considered as the best way to achieve financial stability and poverty at retirement age, but still there are problematic issues and questions regarding the reform:

- How well and effectively was the establishment of the pension reform in Georgia and whether it ensured the growth of the country’s social and economic situation;
- How well the existing and expected risks were identified and managed, what
is the society’s attitude towards the development of the pension system, and is it fair to have a uniform approach to pension services for different layers of the population;

• How purposeful and efficient is the investment policy of the accumulated financial resources;

• What problems and challenges does the pension system face and what prospects are planned for the next stages of its development and regulation.

In recent years, the need to change the pension system was actively discussed in Georgia, which was dictated by the current social, financial and economic situation in the country. Despite the fact that insurance companies operating in the insurance market of Georgia have been offering private pension insurance products to the public for years, a large part of the public was skeptical about the issue. This is due to the society’s low or non-existent insurance and investment culture.

In 2014, the Ministry of Economy and Sustainable Development of Georgia established the Pension Reform Service, the purpose of which was to develop and implement the concept of reform of the Georgian pension system. In just 4 years, Georgia was able to develop and implement the concept of pension reform, by establishing the appropriate legal framework, involving governmental and non-governmental organizations, a wide range of society and following the principle of public dialogue. While other countries took ten to fifteen years to transition to an accrual pension system.

With the participation of the French Development Agency (AFD) and the French International Technical Cooperation Agency "Expertise France", the implementation of the technical support project for the pension reform in Georgia has started, in order to share the experience of the pension reforms in France. For two years, the project was implemented by the French international technical cooperation agency "Expertise France", with the technical and financial support of the French Development Agency (AFD) in the amount of 500,000 euros. This was a big challenge for Georgia, because it was the first project of the French Development Agency in the field of social protection in Georgia and also the first project for "Expertise France" in the country. At the same time, quite a large French investment in Georgia.

Pension reform is a large-scale reform that requires a deep analysis of the concept of the reform, consideration of possible consequences, complex understanding of threats and development of effective mechanisms to prevent these threats. The reform of the pension system has a high social value, is vulnerable to the country’s financial capabilities and is characterized by a high public-political interest.

**Methodology**

The work includes the introduction and implementation of the pension system reform in Georgia, which in turn provided for its replacement with the cumulative pension system. Its relevance, mutual dependence and mutual influence on the improvement of the economic and social condition of the society and inclusive and sustainable economic development of the country.

Quantitative and qualitative approaches are used in the work to determine the existing reality. It is based on statistical materials, data received from various governmental organizations, non-governmental agencies and international organizations. Motivation and actions of governmental, non-governmental and insurance agencies in relation to existing problems, socio-economic reality and
psychological factors of society. Verbal interviews with representatives of the Georgian government, friendly countries, strategic partners and international organizations were used. The conclusion is based on the analysis of existing and received data about the current situation and international experience.

**Review and discussion:**

An important prerequisite for the reform of the compulsory cumulative pension system is the high level of compliance with the directives within the framework of the Association Agreement with the European Union, because today our country is closer than ever to the prospect of EU membership.

All employed and self-employed citizens, as well as foreign citizens permanently residing in Georgia, are obliged to take advantage of cumulative pension insurance in Georgia. For the benefit of the employee participating in the pension scheme, 2% of the accrued salary is credited to the individual pension account of the participant in the pension agency. Additionally, the employer and the state treasury contribute 2%-2% of the accrued salary each to the participant’s individual pension account. An important positive factor here is that the risk-free investment and immediate withdrawals of the pension scheme participant are effectively 275%. On the other hand, within the framework of the pension reform, the pension agency ensures the collection of contributions, the investment policy of the pension fund, the calculation and issuance of pensions to the beneficiaries. The reform will contribute to the development of the Georgian financial market.

Participating in an accumulated pension scheme ensures a financially secure and dignified old age for participants. The amount accumulated in the Participant's Individual Retirement Account is the unconditional and inviolable property of the Participant, which is protected by law and is not subject to seizure, set-off, or any other means of enforcement. The amount accumulated in the participant's individual pension account is subject to inheritance.

In recent years, the level of savings in Georgia has been characterized by growth dynamics, and it is important to maintain this trend. One of the important prerequisites for the development of the financial market is the existence of long-term investments, and the pension reform plays an important role in this respect.

The dynamics of the mandatory accumulative pension system fund volume over the years looks like this:

![Chart 1](https://www.Pensions.ge)
As of today, pension assets have already created a significant investment capital base in the country and amounted to 3.5 billion GEL. The number of participants in the pension scheme is 1 million 405 thousand people. 3,781 persons of different categories benefited from the cumulative pension, and the amount paid was 10,668,997.13 GEL.

Funds in individual retirement accounts are invested in reliable financial instruments for participants. Investment activities are carried out by highly qualified specialists in accordance with the investment policy approved by the Investment Council and the Pension Agency. During the first 5 years after the introduction of the Accumulative Pension Scheme, the funds of the participants will be placed only in the low-risk investment portfolio, and after 5 years, the participants will be allowed to choose a low-risk, medium-risk or high-risk investment portfolio. As for risk control, relevant structures monitor the investment process of participants’ funds, identify risks and evaluate them, in order to ensure that investment risks are in full compliance with the risk profile defined in the investment policy approved by the Pension Agency.

The distribution of the investment portfolio of the accumulative pension system fund looks like this:

![Portfolio distribution chart](Chart N2 - Georgian pension agency www.Pensions.ge)

Which are: certificates of deposit 51%; Foreign corporate shares (foreign currency) 16%; Georgian treasury bonds 15%; Interest accounts 14%; Foreign government securities (foreign currency) 2.15%; Time deposits 0.85%; Interest accounts (foreign currency) 0.75%; Eurobonds (foreign currency) 0.67%; Local corporate bonds 0.33%.

As of today, the net proceeds amounted to 584.5 million GEL, which will be decisive for the development of the capital market in Georgia and will lead to a significant acceleration of the growth of the Georgian economy. The beneficiary of this development is every citizen and resident of Georgia, regardless of whether he participates in the accumulated pension scheme or not.

French experts positively evaluate the introduction of pension reform in Georgia. The working visit of the Executive Director of the French National Reserve
Fund, Oliver Rousseau, to Tbilisi speaks of this. "Pension reform is long-term. The public should understand how important this reform is for investment, infrastructure and capital market development in the country. On the other hand, the pension agency should ensure the process of constant communication with the population", said Oliver Russo while talking to the media.

The advantage of the cumulative pension system and the importance of the reform itself are also positively assessed by the NATO and EU Center’s representation in Georgia and support for future cooperation.

Accumulative pension provision model has caused criticism from the non-governmental sector as well as from the political opposition and in general from specialists in the field. There are questions and different opinions, intense discussions are going on from the public and between various governmental and non-governmental agencies.

Some non-governmental organizations, based on certain studies, believe that the new pension model is indeed accompanied by a number of challenges. According to them, these challenges can be: the existing pension rate creates a very high budgetary pressure on the public finance sector; A number of questions arise regarding the level of inflation and the purchasing power of the accumulated funds after certain years; The mandatory nature of the proposed reform creates financial pressure on private businesses; The new pension system still cannot provide "dignified and happy old age insurance", because the population will not be able to create high pension savings due to low incomes; Today's socio-economic environment does not provide a basis for the success of the reform of the pension system, and the expectations that exist regarding the development of the capital market are exaggerated.

A certain part of the society also critically assesses the pension reform and calls it an uncertain financial risk in time, and most of the society has a hard time answering this question. Because they prefer to refrain from excessive obligations, in the conditions of today's already scarce financial resources. It is important to conduct a large-scale information campaign in order to make the benefits of the said reform much more understandable and easy for the population to improve their social and economic situation in the long term, which is quite difficult to achieve.

**Conclusion:**

Despite the great differences of opinion and criticism, the cumulative pension reform has no alternative. It is known that many sub-regions were unable to implement the said reform voluntarily, and Georgia is no exception. The reform has already been able to maximize the number of participants in the pension scheme, create a significant pension assets and multi-billion dollar base of investment capital, and have yielded practical results, which are reflected in the number of beneficiaries, disbursed funds and investment returns.

In addition to the fact that the reform in the long term ensures financial stability of people at retirement age and insurance of a happy old age, the investment capital base will be an important factor for the development of the capital market in Georgia and will contribute to the significant acceleration of the economic growth of Georgia, the long-term growth of foreign exchange resources in the country and the activation of financial markets. The beneficiary of the said development will be every
citizen of Georgia, regardless of whether he participates in the accumulated pension scheme or not.

The most important issue is to conduct an even wider information campaign, so that the benefits of the said reform become much more understandable and easy for the population to improve their social and economic situation in the long term.

Based on socio-economic goals and high public interest, the reform of the pension system is of great importance for a country like Georgia, which on the one hand has a relatively unstable economic, social and political environment, and at the same time is considered an aspirant country of the North Atlantic Alliance "NATO" and declares to claim full membership of the European Union.

References: