Chapter 4
Financing Sustainable Development in an Emerging Economy:
The Private Pension System in Turkey

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ABSTRACT

The purpose of this chapter is to review the Turkish private pension system as a key determinant of sustainable development of the country. The private pension system is of great significance in order to promote sustainable development. This is attributable to the fact that high level of total savings which are secured through individual savings are conducive to investments and in turn finances sustainable development and growth. Turkey, as an emerging economy, is considered to be one of those economies with low level of total savings. In an effort to deal with this issue, governments paid attention to an increasing level of savings of households. Individual retirement system (private pension system) is devised so as to increase savings and to fund investments with national sources. Therefore, it is safely argued that the very rationale behind the introduction of private pension system is associated directly with the aim of increasing total savings in the economy and ensuring sustainable development.

INTRODUCTION

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1. INDIVIDUAL RETIREMENT (PRIVATE PENSION) SYSTEM IN GENERAL

Firstly, it is necessary to know the level of savings ownership rate and savings instruments. Apart from the statistical information provided by Turkish Statistics Institution (*TUIK*), another study is needed for searching this issue. 'Turkey's Savings Trend Research', a quarterly-report released by ING Banking Group & Ipsos and Bilkent University, studies regularly level of savings and provides data in detail. According to the 4Q2020 report of this research, the ratio of savings ownership rate declined to 18% with 2.2% decrease when compared to 3Q2020 results when it was 20%. It is argued in the report that considering a long period of time, the latest rate is still remarkably high.

As clearly stated by Turkish Monitoring Authority official website, Individual Pension System was entered into force pursuant to Individual Pension Savings and Investment System Law No. 4632. The IPS is based on the principle of the collection and investment of savings and then making a lump-sum payment or regular payments to the individual. IPS does not offer health or other services provided by the Social Security Institution. It was devised as a supplement and not an alternative to the compulsory social security system.

Individual Retirement System can be classified into two kinds: Voluntary Participation (IPS) and Auto Enrollment System (AES). Introduction of these systems is necessary in order to reduce the burden of social security systems on the public budget in Turkey (public economy dimension), to fund large-scale projects by directing individual savings to investments (for strong and sustainable economy), and finally to protect participants' purchasing power in their retirement (insurance function).

Individual retirement (the system) is covered under insurance industry. Therefore, the system is considered as both savings system and insurance system. The very nature of the fact that insurance is not a means of creating wealth but a system designed to compensate the damage incurred and to ensure that the economic life of the insured value remain the same. In view of the fact that the system is considered a business line under insurance services, one must bear in mind that IPS is not introduced in order to create wealth in a very short time. When this very fact is not taken into account, some clients expect great returns in a very short period of time from the system, which is against the rationale behind the establishment of the system. It is a saving tool that will eliminate the risk of losing purchasing power in the retirement period (long run perspective) and especially at the end of the working age. Investors who ignore this fact tend to compare IPS with conventional, short-term financial (investment) instruments, and evaluate this product with wrong expectations and then leave the system. On the other hand, those who understand the product correctly with the right expectations and stay in the system (for long term) can use the advantage of the IPS against income losses in retirement (with returns above inflation).

This system was not created with the aim of providing a great fortune to participants in the short term. In the scientific method, wrong assumptions cause incorrect models, resulting in wrong policy implication. In Turkey, with the help of participants who understand IPS correctly will provide individual resources to the economy and maintain their purchasing power during their retirement days. It would be the best starting point for reform attempts and resolve some issues arising out of the application of the system.

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