INTERNATIONAL MONETARY FUND

Liechtenstein's Pension System

Rodgers Chawani

SIP/2025/048

IMF Selected Issues Papers are prepared by IMF staff as background documentation for periodic consultations with member countries. It is based on the information available at the time it was completed on March 5, 2025. This paper is also published separately as IMF Country Report No 25/77.

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Liechtenstein's Pension System
Prepared by Rodgers Chawani

Authorized for distribution by Kazuko Shirono
April 2025

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ABSTRACT: The paper analyzes Liechtenstein's three-pillar pension system, assessing its structure, funding mechanisms, sustainability and adequacy challenges. Liechtenstein's pension system operates on a three-pillar framework comprising public pensions (AHV-IV-FAK), mandatory occupational schemes, and voluntary insurance. With reserves exceeding 150 percent of GDP, the system ranks third globally in accumulated savings. Despite robust financial health and built-in intervention mechanisms, demographic projections indicate Pillar I assets will decline below statutory minimums by 2043. The research concludes that population aging and increased life expectancy will necessitate policy adjustments such as raising retirement ages or increasing contribution rates to ensure the system's long-term viability.

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Liechtenstein

Prepared by Rodgers Chawani[1]

[1] "The author would like to thank Mark Horton and Kazuko Shirono for their comments and helpful suggestions.

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PRINCIPALITY OF LIECHTENSTEIN

SELECTED ISSUES

March 5, 2025

Approved By

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LIECHTENSTEIN'S PENSION SYSTEM[1]

Liechtenstein's pension system is structured around a three-pillar framework designed to provide a balanced, sustainable, and secure retirement income. This well-capitalized system aims to safeguard a basic income level for all employees while encouraging supplemental private savings and income.

A. Overview of the Pension System

1. **Liechtenstein's pension system rests on three complimentary pillars**: (i) Old Age and Survivors' Insurance (AHV-IV-FAK); (ii) an occupational scheme; and (iii) voluntary insurance. The multi-tiered system helps secure and sustain a post-retirement minimum standard of living. The system has accumulated savings exceeding 150 percent of GDP, third globally after Denmark and Iceland, and higher than in Switzerland.

B. Pillar I

2. **The public pension aims to guarantee a secure standard of living for retirees.** It comprises mainly three distinct arms that are supervised by government and report to parliament Benefits are influenced by salary levels and duration of contributions. The retirement age is 65 years for both men and women; early retirement can be initiated at 60 or deferred until 70. The system aims at redistribution: high-income earners typically contribute significantly more to the AHV than they receive upon retirement, while low-wage earners receive higher returns relative to contributions. The system guarantees a minimum monthly pension with a replacement ratio of about 35 percent (see Figure 2), below the recommended international minimum of 40 percent, yet complemented by Pillar 2.

3. **Funding of the AHV-IV-FAK statutory pension is diverse.**

- *Old Age and Survivors Insurance (AHV)* – While a pay-as-you-go system, considerable balances have been built. The funding basis is employers (4.2 percent), employees (4.0 percent), self-employed individuals (8.3 percent), and non-active persons who benefit from state contributions.

- *Invalidity Insurance (IV)* – A pay-as-you-go disability system funded by AHV contributors. Also holds reserve. Contributions from employees (0.7 percent), employers (0.7 percent) and self-employed (1.4 percent). No funding from state resources.

- *Family Compensation Fund (FAK)* – Solely funded by employers (1.9 percent), self-employed (1.9 percent), and non-active people.

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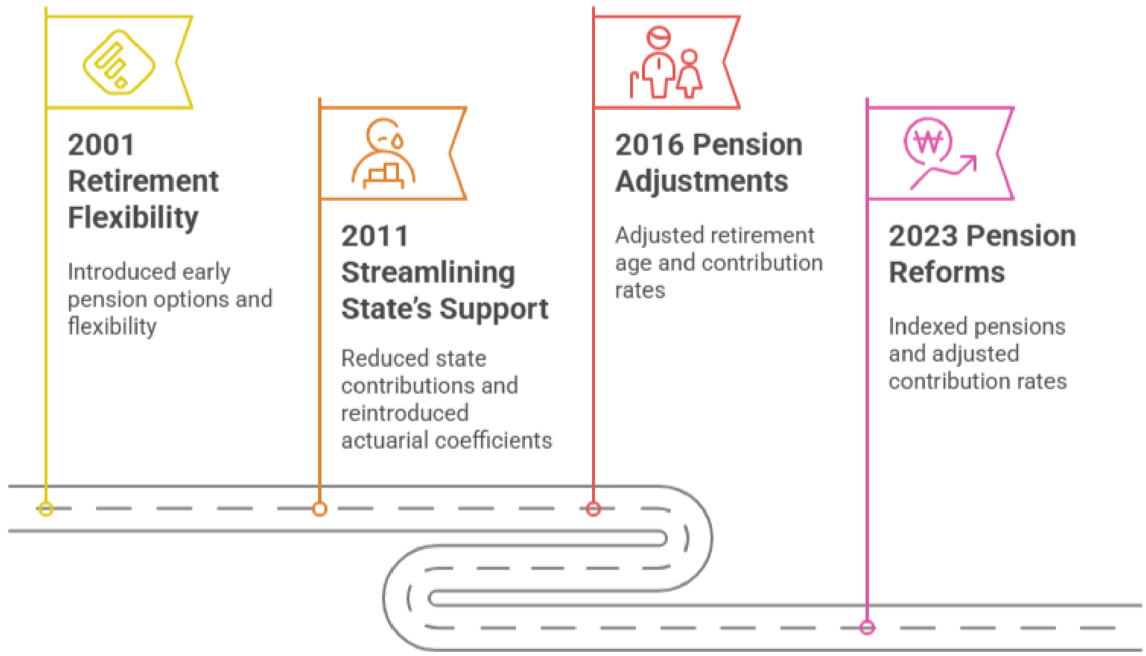
- *Additional Contributions* – The State and Municipalities provide mean-tested supplementary benefits for pensioners, vulnerable, blind, homecare, and medical rehabilitation.

Figure 1. Key Pillar I Pension Reforms



4. Several reforms have anchored sustainability of the AHV-IV-FAK. These aimed at greater retirement flexibility, streamlining state support, aligning effective retirement ages, and addressing the evolving economic landscape.

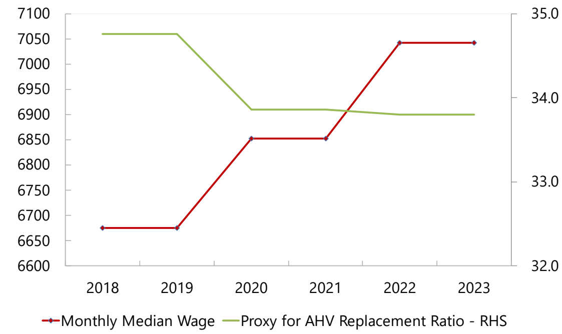
- *2001.* Reforms paved the way for early retirement at 60.

- *2011.* Reforms implemented in the context of budget pressures following the global financial crisis. Measures included reducing the state's contribution, adjusting pensions in line with the consumer price index, re-introduction of actuarial reduction coefficients for early pensioners, and re-allocation of 0.2 percent of wage contributions from the FAK which was overfunded.

- *2016.* Parliament approved an annual state contribution of CHF 30 million to AHV, with inflation adjustment, and increased and equalized the statutory retirement for men and women to 65 years. It implemented an intervention mechanism mandating a financial examination of the AHV every five years. Should the audit reveal assets below five years of annual expenditures, the government must present measures to parliament to rectify the situation within one year. The most recent report to parliament indicates that the ratio of the AHV fund to annual expenditure is projected to decline from 9.9 to below 5.0 by 2043, thereby requiring specific proposals to be presented to parliament (Government of Liechtenstein, 2024).

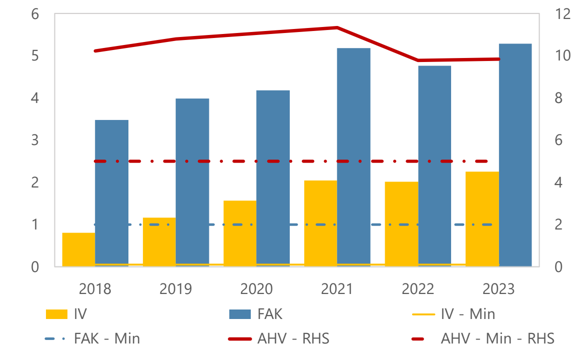
Figure 2. The Pillar I Pension System

Average Monthly Wage and AHV Replacement Ratio
(CHF, Percent)

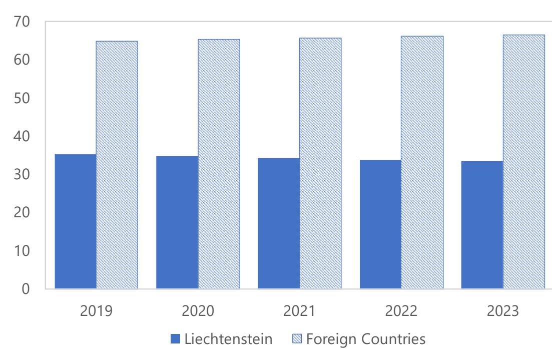


Source: Office of Statistics & Financial Markets Authority

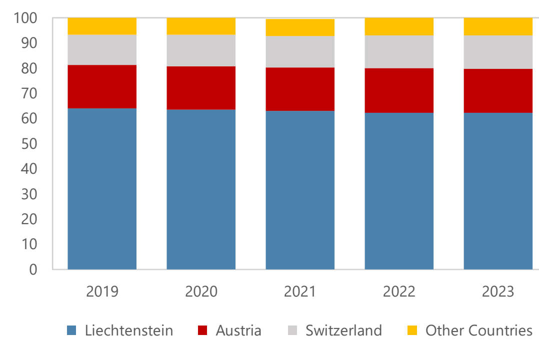
Assets Relative to Annual Expenditure
(Percent)



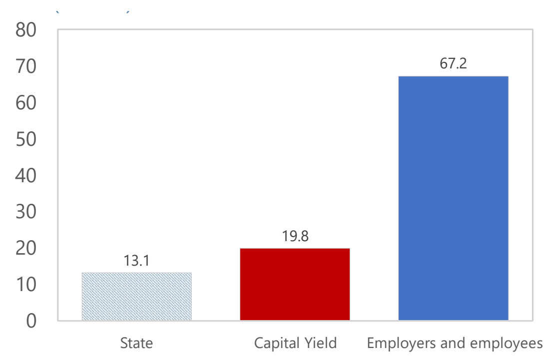
Pension Recipients by Residence
(Percent of Total)



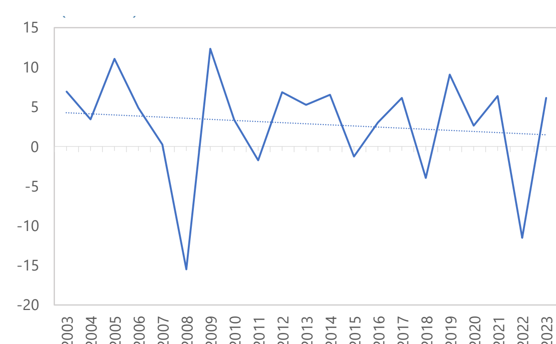
Pension Payments by Nationality
(Percent of Total)



Source of Funds for the Pillar I Pension Fund
(Percent)



Pillar I Pension Investment Performance
(Percent)



- *2022–23.* Shifted contribution rates from the overfunded IV towards the FAK and indexed pensions to an arithmetic average of consumer price index and wage index.

- *Future reforms.* The EU directive on work-life balance for parents and carers will become effective in January 2026 and includes guaranteeing four months of parental leave for each parent for children up to three years; financial compensation for two months (about CHF 4,900 per month); additional leave of 10 days for fathers including compensation of 80 percent of wages.

5. **The pension system embeds several intervention mechanisms to ensure stable financing.** Should reserves decline to below five times the annual expenditures, the ability to adjust pensions according to inflation is halted. The IV includes a financing mechanism that guarantees a state contribution will be made in accordance with the Disability Insurance Act if reserves decline to below 0.05 of annual expenditures. Current annual expenditures are at a ratio of 2.25 (see Figure 2). The FAK includes a mechanism that stipulates a defined state contribution to the Fund if reserves drop below one annual expenditure. Current reserves are at 5.29 times the annual expenditure.

6. **Foreign participation is a unique characteristic of the pension system.** About 66 percent of Pillar I's recipients are from foreign countries (Figure). This reflects labor force characteristics and foreign commuters. Still, most payments are made to residents given the short-term nature of most of the employment (Figure 2).

7. **Pillar I is funded predominantly by employer and employee contributions.** Contributions from insured persons and employees are 67.2 percent; the government contributes 13.1 percent. Capital gains constitute 19.8 percent. In terms of asset allocation, the AHV-IV-FAK targets: bonds (50 percent, of which Switzerland accounts for 67 percent); shares (33 percent, of which Switzerland accounts for a third); and alternative investments and real estate 7 percent each.

C. Pillar 2

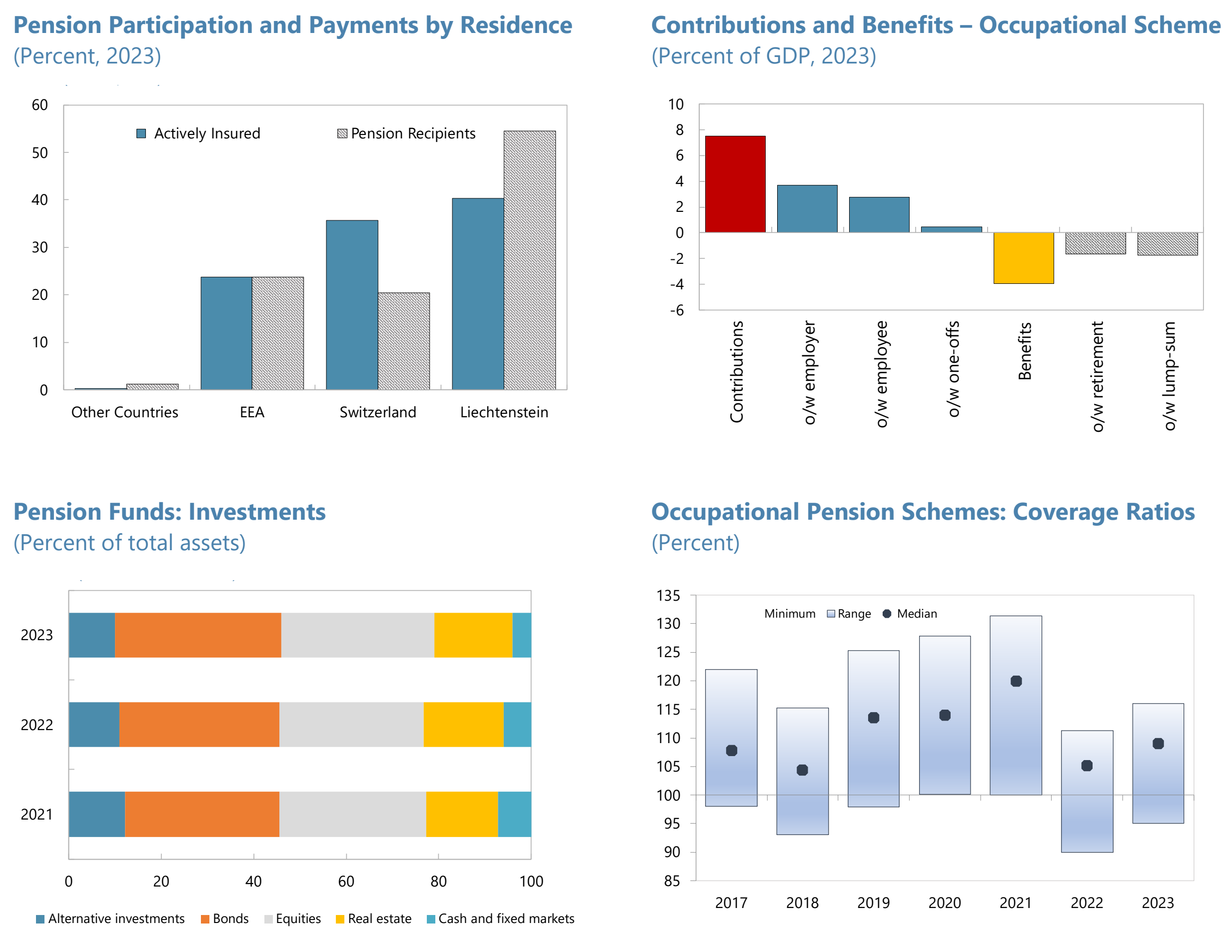
8. **The public Pillar 1 is complemented by a second pillar, a mandatory occupational scheme for employed individuals.** Introduced in 1989, this accounts for over CHF8.4 billion or 118 percent of GDP in 2023. It is fully funded by employer and employee contributions as well as interests and deposits. Pillar II comprises autonomous legal entities that are subject to the Occupation Pensions Act and are under the supervision of the FMA. The pillar has experienced significant consolidation, decreasing from a peak of 33 occupational plans in 2010 to 15 in 2024 driven by challenging financial market conditions, including prolonged low interest rates, and heightened regulatory demands resulting in elevated administrative costs. Small (mostly single employer) plans transferred to larger plans (or insurers).

9. **Non-resident participation is also a distinct feature of Pillar II.** The pillar covers 45,500 people, of which 32,547 or 83 percent were actively insured, and 6,462 or 17 percent were pensioners in 2023. Sixty percent of the actively insured are foreigners (Figure 3), although

commuters comprised 46 percent of total pension payments in 2023. Once no longer employed in Liechtenstein, benefits are transferred to a vested benefit account, except for Swiss where vested benefits move to a new pension fund.

10. Employer and employee contributions and investment income finance Pillar 2. Total contributions amounted 7½ percent of GDP in 2023, of which 53 percent was employer contributions and 47 percent was employee contributions. The occupational funds, consisting of nine company foundations and six collective foundations, are defined-contribution plan (DCP), except for one entity; 96.8 percent of actively-insured individuals are covered under DCP, which provides flexibility, portability, and ownership. The final pension is influenced by contributions, accrued interest, and a conversion rate.

Figure 3. Occupational Pension Scheme



11. Coverage ratios improved following a decline in 2022. The system is responsive to fluctuations in equity and interest rates. After the global financial crisis, funding ratios stabilized and reached 120 percent in 2021, with increased investment income. Market turbulence and lower valuations caused the coverage ratio to decrease to 106 percent in 2022; some funds fell below the requisite 100 percent coverage ratio due to adverse equity performance. Median coverage ratios rebounded to 109 percent in 2023, facilitated by market recovery and higher interest rates.

12. Dependence on investment income exposes the system to fluctuations in interest rates. Equity and fixed-income assets dominate the occupational funds investment assets. Investment in bonds were 36 percent of total assets and equities 33 percent in 2023. Exposure to real estate was 17 percent, while alternative investments were 10 percent (Figure 3). A return to sustained low or even negative interest rates could affect the funds and may lead to accumulation of risks due to search for yield.

13. Several reforms have underpinned resilience of Pillar II.

- *EEA Accession***.** With EEA membership, legislative amendments were introduced, including, equal treatment for men and women, early retirement provisions, division of entitlements in the event of divorce, and introduction of risk insurance for the unemployed.

- *2005.* Introduced information and transparency regulations, strengthened accounting conventions, and created a security fund.

- *2017–2018.* Increase in retirement contributions, lowering of the entry thresholds for compulsory insurance while strengthening governance of the pension funds.

D. Pillar 3

14. Voluntary individual pension savings constitute the third pillar. Pillar 3 covers the provisions of pensions through private savings or private voluntary old-age insurance policies. Income from these products supplement state and occupational pension schemes.

E. Issues for Further Consideration

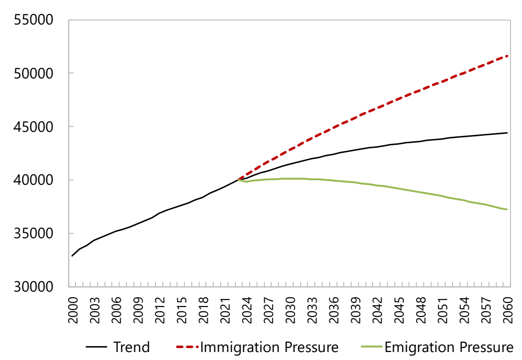
15. Demographic changes will result in additional costs. Most of the baby boomer generation has reached retirement age and exited the labor market. The population is anticipated to grow by 11 percent by 2060, but the number of individuals over the age of 65 is expected to increase by 59 percent. This will increase pension costs.

16. Higher life expectancy will increase pension spending. Life expectancy at birth has increased from 81.8 years in 2020 to 84.6 years in 2023. Life expectancy after 65 years of age has increased from 19.8 in 2020 to 23.3 years in 2023. According to the EU's 2024 Ageing Report, an increase in life expectancy at birth of around two years as compared the baseline scenario assumptions would push up average pension expenditure by 0.4 percentage points of GDP in 2070.

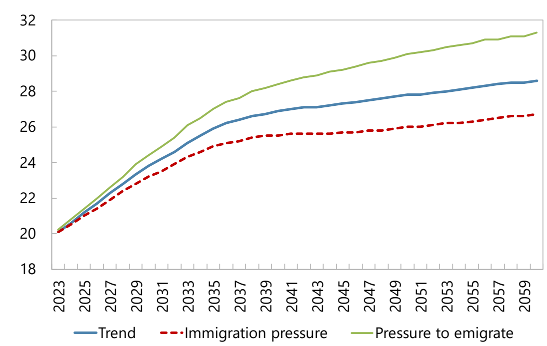
17. Closing future financing gaps in line with mandatory actuarial forecasts is important. Pillar I projections indicate that assets will fall from 9.8 to 3.1 years of annual expenditures by 2043, well below the statutory 5-year minimum. If reserves fall below the minimum threshold, the law suspends the inflation adjustment of the old-age, survivors' and disability insurance benefits. Options to address gaps include increasing the effective retirement age and/or raising contributions for employers, insured persons, or the state.

Figure 4. Demographic Changes

Population Projections 2024–2060



Proportion of 65-year Olds and Over
(Percent)



F. Conclusion

18. The pension system has substantial buffers, but actions will be needed to close future financing gaps. The system has a three-tiered structure with high accumulated assets. Yet aging will pressure the system going forward, calling for measures to ensure sustainability, including raising the retirement age and/or contributions.

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