Why are Politicians Resisting Mandatory Savings as Pay-As-You-Go Welfare Falters? An NZ Case Study

Leonard Hong*
Economics Department, University of Auckland

Robert MacCulloch**
Matthew S. Abel Professor of Economics
University of Auckland

This version: 28 May 2026

ABSTRACT

Why are nations failing to resolve the fiscal crisis caused by population ageing? Many economies are struggling with rising costs to the government budget of pension and healthcare due to population ageing. A potential solution is greater emphasis on mandatory private savings so future generations are not so dependent on a dwindling proportion of youth to pay taxes to support their welfare needs. However, few nations have buttressed Pay-As-You-Go (PAYG) public systems the past two decades in this way. We use New Zealand as a case study to highlight three salient political-economy barriers. First, ideology leads many right wingers to oppose mandatory savings due to a desire not to curtail personal economic freedoms, as well as left-wingers who prefer reliance on State welfare. Second, politicians have been largely unable to design reforms that minimize loss of current disposable income to the median voter as savings are built for workers, whilst at the same time PAYG pensions continue for the existing retired paid out of current taxes. Third, the long time period required to deliver significant savings boosted by compound returns deters politicians with short horizons.

Corresponding authors: * Leonard Hong. Economics Department, University of Auckland Business School, 12 Grafton Rd, Auckland 1010, email: lhon250@aucklanduni.ac.nz. ** Robert MacCulloch, University of Auckland Business School, 12 Grafton Rd, Auckland 1010. Email: r.macculloch@auckland.ac.nz. We thank Larry Kotlikoff, Arthur Grimes and Stefan Olson for helpful comments, and Eric Zhao for research support.

1. Introduction

Across many countries, ageing populations have caused the cost of publicly funded pension and healthcare programmes to put rising pressure on government budgets. Threats of large cuts in welfare generosity, tax hikes, or both, are now common. However, over the past two decades as such pressures intensify, few, if any, nations have reformed welfare to place significantly greater reliance on private mandatory savings. This paper uses a New Zealand case study to answer the question as to why so many governments have refrained from ensuring individuals build greater savings to enable them to have more funds for their own welfare needs, particularly in retirement, given the public system is in such jeopardy. The macroeconomic backdrop to this reluctance includes NZ Treasury forecasts of the public debt to GDP ratio rapidly rising to nearly 100% of GDP by 2045, driven by outlays chiefly on pensions and healthcare.[1]

Why has adoption of mandatory savings-based pensions schemes not occurred these past two decades, not only in New Zealand but around the world, as population ageing accelerated in so many places, especially when nations ranked as having the most sustainable systems did implement such schemes long ago? We provide three reasons rooted in political economy to explain the reluctance - the ideologies of NZ's left and right-wing parties, pressure from pivotal voter groups, and short government time horizons. These factors may now threaten long-run social welfare.

2. The Fiscal Crisis Enveloping Nations with Ageing Populations that are Reliant on Pay-As-You Go Welfare: A Brief Background

The problem of fiscal sustainability has become so challenging that the prospect of sovereign debt default is being raised, even in America.[2] In his 2025 Feldstein lecture, Greg Mankiw addressed its *"fiscal future"*. About half of the budget is Federal spending on healthcare and pensions. In NZ it is 56%. He notes the Department of Government Efficiency's (DOGE) public servant downsizing initiative, driven for a time by Elon Musk, would only ever have had *"limited"* impact since the *"compensation of government employees makes up only about 4 percent of the federal budget"*. In NZ it is a similar figure. Downsizing has been the response, both here and in America, probably since, as Mankiw notes, *"Enacting large cuts in entitlement programs [like health and pensions] is politically treacherous"*.

A reform that can help fiscal sustainability due to an ageing population, without endangering the

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[1] See, *He Tirohanga Mokopuna, Log Term Fiscal Statement 2025*, September, Te Tai Ōhanga, NZ Treasury, Wellington.
[2] See Poot (2026) and Buckle and Creedy (2014) for other economic impacts and need for an electoral reform mandate.

welfare state, is more emphasis on mandatory savings. This approach can have desirable effects in terms of long-term fiscal discipline, since with more private funds dedicated to retirement, more substitution away from public assistance can occur as those in need falls due to greater self-reliance.

A leading example is Australia, where Labor Prime Minister Paul Keating enacted mandatory savings in 1992, supplementing an existing means-tested PAYG public pension. Keating argues its advent slashed reliance on taxpayer-funded pensions, noting *"France spends 14% of its GDP on public pensions, Germany 10%, and the US 7%. Australia's pension-call on the budget is currently just 2.3% of GDP - a sunken level thanks entirely to universal superannuation"*.[3] Australia's reform is lauded by its citizens and press as a *"superannuation system that became today's extraordinary financial force - one increasingly powerful internationally as well as domestically, with more massive growth guaranteed into the future"*.[4] Super wealth is estimated to reach $8 trillion by 2035, becoming the second-largest in the world (after the US).

Indeed, pension systems ranked as highest quality combine PAYG social security, together with mandatory individual savings or occupational pension schemes, and supplemented by voluntary savings.[5] Ageing population nations like Japan and Italy have the lowest grades, *"D"* and *"E"*, respectively, for the sub-category, *"sustainability"*, in Mercer's (2025) ranking. They have PAYG systems without mandatory private components. The highest grades for this sub-category include the likes of Australia, The Netherlands, Iceland and Singapore, which all have mandatory features.[6]

However, Australia's reform has not been matched by others these past two decades as ageing population pressures rose. Led by academics like Peter Diamond in America, mandatory accounts were set up in Chile in 1981, but under dictatorship without democratic mandate. After the Soviet Union's fall in 1989-90, Barr and Diamond (2016) note how other nations started down this road in Latin America and East Europe. There has since been backward regression. After the 2008 Global Financial Crisis, Estonia, Latvia, Lithuania, Poland and Romania either, *"retained individual accounts but changed the balance of contributions so that less went to individual accounts and more to finance PAYG benefits"* or, like Hungary and Argentina, *"abandoned individual accounts altogether"*, transferring contribution flows and asset stocks to the PAYG system.[7]

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[3] See, "Paul Keating Says Young Australians are Guaranteed to have $3 Million in Super by Retirement - But Not Everyone Agrees", *The Guardian*, Monday 30 June 2025.
[4] See, "Australia's Super Juggernaut is Just Getting Started", *The Australian Financial Review*, 7 September 2022.
[5] For an example of a ranking, see the Mercer CFA Institute Global Pension Index 2025.
[6] Although there is no statutory obligation for employers to offer a pension scheme in The Netherlands, industrial-relations agreements mean about 90% of employees are covered so *"these schemes are best thought of as quasi-mandatory"* (*OECD Pensions at a Glance*, 2023). See Feldstein (1998) and Shiller (2003).
[7] For detailed accounts of the retreat, see Bielawska et al. (2016) and Simonovits (2011).

3. Why has Mandatory Savings Met with Stiff Political Resistance? An NZ Case Study

Using New Zealand as a case study, we highlight three reasons why politicians have been unwilling to implement mandatory savings to bolster its PAYG flat rate (not means-adjusted) pension.

3.1 Political Ideology Restraining a Shift to Mandatory Savings

New Zealand's voluntary KiwiSaver individual retirement savings accounts scheme was introduced by Prime Minister Helen Clark's Labour government in 2007. It is automatic enrolment whereby a person has the option not to join, but to do so must formally opt out. The scheme is an example of *"benign paternalism"*, pioneered by the likes of Thaler and Sunstein (2009). Although PM Clark's government promoted savings in this way, a mandatory scheme was a step too far. Part of the reason may be related to suspicions about "privatizing welfare". The preference of many politicians on the left in NZ is still to prioritize reliance on a PAYG public pension.

On that note, prominent New Zealand academics and retirement experts who are more associated with the left of politics, like Emeritus Associate Professor Susan St John, remain wary of adopting Australian-style mandatory savings. St John argues adopting such accounts would be *"deeply scary"*, based on the view that doing so would weaken the existing flat-rate PAYG state pension by leading to the country instead adopting a means-tested pension to alleviate strains on the public purse, a feature former Australian PM Keating regards as a great virtue of his nation's scheme (see above).[8]

On the other side of politics, mandatory savings have also not sat comfortably with National Party ideology. In 1976, during the oil shocks, Prime Minister Sir Robert Muldoon abolished the scheme set up two years previously by Labour PM Norman Kirk.[9] When KiwiSaver was first proposed, National opposition leader Sir John Key called it a *"glorified Christmas club"*. His party voted against it. Although the current National government increased minimum contributions by employees and employers from 3% to 3.5% of wages in 2026, it also ended subsidies and amended the KiwiSaver Act (2006) to create new first-home withdrawal pathways. The party currently states, *"KiwiSaver contributions would [still] be much lower than the equivalent scheme in Australia"*.[10]

Ironically, the NZ Initiative, a "free market" think-tank arising from the Business Round Table of

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[8] See, "It is Time for Economists to Stop Trying to be Accountants", October 2025, https://susanstjohn.substack.com/p/it-is-time-for-economists-to-stop

[9] It was not based on individually managed accounts, but instead a State fund into which contributions were paid.

[10] Australia's mandatory scheme requires employers to pay 12% of employee wages into their individual accounts.

the 1980s, whose initial members funded the formation of the (self-described) "classically liberal" ACT Party, concurs with many on the left of politics in critiquing mandatory savings, but for very different reasons.[11] It emphasizes the rationality assumption of classical economics, whereby people optimally choose consumption and savings. The Initiative writes, *"In 1954, Franco Modigliani showed households plan their savings across a lifetime. If forced to save through one account, they save less through others"*, thereby expressing the view mandatory savings maybe offset one-for-one by cuts in voluntary savings.[12] Forced savings can reduce welfare in such models. For those who do not defend rationality so strongly, believing myopia is common-place, and wish to promote saving, but only with gentle State "nudges", KiwiSaver-style schemes are an acceptable option.[13]

The importance of political ideology in favouring mandatory savings is seen in the ethos underlying Singapore's mandatory savings system which was created in 1955 on a founding principle of people taking *"responsibility for themselves and their families"* (see Prime Minister Lee Kuan Yew, 2000, and Hong, 2024). In a different setting, the Netherlands' quasi-mandatory private work-place pensions, together with its PAYG welfare system, established after World War II, reflected a national unity Polder model of consensus decision-making by firms, government and unions. Australian PM Keating also invokes a unity ideal, arguing savings accounts for all are, *"like Medicare, an Australian community standard, binding the whole population as a national economic family, with each person having a place"*.

3.2. Loss of Disposable Income for Politically Influential Voter Groups

When implementing mandatory savings reform, contributions are made by employees, employers, or both. Adding these payments onto taxes paid to fund existing PAYG welfare payments to the elderly can cause cuts in disposable incomes for workers. So how can majority support be won? Former Australian PM Keating argues politically feasibility depended on his reform being included in a package that included tax cuts, tariff cuts and a shift to union enterprise bargaining. His 1995 Budget proposed 3 per cent tax cuts that would be paid into people's super accounts to increase contributions by the same amount. However that leaves government with less revenue, so to maintain fiscal balance must be accompanied by cuts to groups currently receiving public support.[14]

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[11] See, "David Seymour: From Frontier Centre for Public Policy to the Heart of New Zealand Politics", *The News Wire*, Winnipeg, Manitoba, Canada, August 14, 2023. https://www.thenewswire.com/press-releases/1AJ6Fv9JQ-david-seymour-from-the-frontier-centre-for-public-policy-to-the-heart-of-new-zealand-politics.html

[12] See, "A $110 Billion Illusion", *Insights Newsletter*, 20 March 2026, NZ Initiative, Wellington. A former staffer of the Initiative served as Prime Minister Luxon's Chief Policy Adviser from 2024 to 2025.

[13] Shiller (2004) endorses NZ's KiwiSaver in his *Project Syndicate* (2004) article, "Saving a World that Doesn't Save".

[14] In 1997 a referendum in New Zealand gave voters the option to choose an Australian-style compulsory retirement scheme, which was rejected. For a history of the debate, see Andrew Coleman, *Interest.co.nz*, July 2025. Keating's 1995 Budget plan was rejected the following year by the incoming Liberal government under PM John Howard.

In NZ's case, this could be done by targeting high income groups receiving welfare, like tertiary students from wealthy families on interest-free loans and fee subsidies, movie grants, winter energy subsidies to the wealthy and accelerated depreciation allowances to chosen industries.[15] Although these groups are a minority, ending such subsidies would be met with fierce resistance. Interest-free tertiary loans were offered leading up to NZ's election in 2005, won by PM Helen Clark's Labour. Upon National later gaining power, the policy continued. Ending movie subsidies has met with threats to go elsewhere, even though grants totalling $300 million have already been made for Avatar films and Amazon's Lord of the Rings. All political parties appear keen to continue them.

3.3. Short Time Horizons of Political Parties

The Australian 1992 mandatory savings reform has achieved prominent status in the world due to its size. For a person who is 65 years old, the average balance is now $A 421,000 ($NZ 505,000).[16] Compound returns of about $255,000 contribute over 60 per cent of that value. However, given it took 34 years, "selling" such a reform in NZ with its three-year government terms, and probably elsewhere, maybe unappealing to politicians. Either their own myopia, or that of voters, appears a barrier. Nineteen years after NZ's voluntary KiwiSaver was set up, its relatively low default rate of (employer and employee) contributions of 3% of wages (from 2009 to 2025) has meant the average balance is now $NZ 69,100 for someone aged 65 years old, with incomplete coverage and 39% of people in the scheme not contributing due to legally permitted circumstances. In Australia, average super savings at 65 years is nearly 5 times the average annual salary, whereas in NZ closer to one.

4. Conclusion

Whatever one's views on the best structure of a pension system, it is hard to deny relying on each young generation to support the elderly through current taxes ("Pay-As-You-Go") is more than ever threatened by population ageing. Prospects of severe cuts in welfare, or steep tax rises that would be fought, are now faced throughout the world. This future notwithstanding, the past two decades have witnessed few, if any, moves to mandatory savings. We highlight three salient reasons for NZ's reluctance. First, both left and right political ideology has opposed it. Second, no party has proposed a popular design of a transition that minimizes a cut in disposable income to the median voter. Third, myopia by politicians underestimating compound returns maybe prevalent.

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[15] See Douglas and MacCulloch (2020) for a proposal along these lines. Coleman (2011) gives an excellent discussion of different transition paths.

[16] See Keating (2007) and Love (2009) for an overview of Australian compulsory superannuation.

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