



Pareto-Improving Social Security Reform when Financial Markets are Incomplete!?

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Article Information

Abstract

This paper studies an overlapping generations model with stochastic production and incomplete markets to assess whether the introduction of an unfunded social security system leads to a Pareto improvement. When returns to capital and wages are imperfectly correlated, a system that endows retired households with claims to labor income enhances the sharing of aggregate risk between generations. Our quantitative analysis shows that, abstracting from the capital crowding-out effect, the introduction of social security represents a Pareto-improving reform, even when the economy is dynamically efficient. However, the severity of the crowding-out effect in general equilibrium tends to overturn these gains. (JEL D58, D91, E62, H31, H55)

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Additional Materials

Replication Package (458.15 KB)

JEL Classification

D91 Intertemporal Household Choice; Life Cycle Models and Saving

H55 Social Security and Public Pensions

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