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# Mizuho Economic Outlook & Analysis

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## *Reforms to social security system for all generations*

*Both benefits and burdens should target people of all generations*

### < Summary >

- ◆ Japan is now in the midst of reforming its social security system. The aim is to rework the existing social benefits focused primarily on the elderly to benefits that can support all generations, with the cost burden shouldered by people of all generations based on their capability.
- ◆ Concerning benefits for the working population, although improvements in education cost support, including free early childhood education, are on the list, the elimination of the waiting list for children to enter a nursery is another important issue that needs to be addressed.
- ◆ The key to shifting the current social security burden to all generations is the realization of an ageless society where people can continue working regardless of age. It is expected that legislation will be revised to ensure employment opportunities up to the age of 70. But with a view to offering options other than employment, it is necessary to provide support for the working population as early as possible.

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Mizuho Research Institute Ltd.

**Naoko Horie**, Senior Economist, Research Department - Public Policy

[naoko.horie@mizuho-ri.co.jp](mailto:naoko.horie@mizuho-ri.co.jp)

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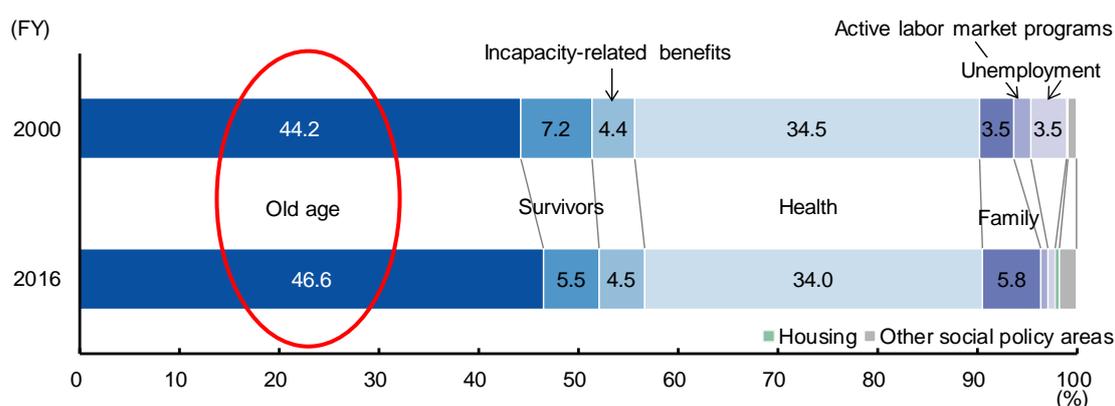
## 1. Breakdown of social security benefits

According to the breakdown of social expenditures by policy area in the “Financial Statistics of Social Security in Japan” compiled by the National Institute of Population and Social Security Research (**Chart 1**), the ratio of expenditures for “old age” is the highest. As the number of elderly people increases, the ratio has continued to rise from 44.2% recorded in FY2000 to 46.6% in FY2016. Although expenditures for “health” should basically target all generations, about half of all health expenditures in FY2000, and about 60% in FY2016, were likely spent on seniors. It should be noted that although spending on “family” including child allowances and early childhood education support, is low, spending increased slightly from 3.5% in FY2000 to 5.8% in FY2016, thanks to the recent enhancement of measures to improve the falling birthrate.

“Social security system reform to benefit all generations” is positioned as the greatest challenge for the Abe administration. This challenge is aimed at correcting the current social security system, with its tendency to focus benefits primarily on seniors, to one that would also benefit the working population by providing free education and child-rearing support, among others.

In order for the social security system to target all generations, it is essential that benefits and burdens be borne by all generations. This means that people of all generations should support each other based on their capability and not on their age.

**Chart 1: Breakdown of social expenditures by policy area**



Note: The chart depicts the ratio of expenditures by policy area when total social expenditures are 100%.

Source: Made by MHRI based upon the National Institute of Population and Social Security Research, *Financial Statistics of Social Security in Japan FY2016*.

In this report we focus on both benefits and burdens of the social security system targeting all generations and examine the benefits of the main improvement plans targeting the working population, along with measures to be taken to revise the social security system to the one where financial burden is shouldered by all generations, a goal

currently being promoted by the Abe administration. We will then consider the issues that the nation will face in the future.

## **2. Enhancement of social benefits for the working population**

The representative social benefit for the working population is education cost support. The main reforms planned ahead are (1) free early childhood education/nurseries, (2) free higher education, and (3) effectively free private high school tuition.

### **(1) Free early childhood education/nurseries**

Beginning from October 2019, early childhood education and nurseries will be free of charge. According to a 2015 survey conducted by the National Institute of Population and Social Security Research, while the ideal number of children married couples want to have is 2.32 on average, this ideal figure deviates from the number of children couples actually plan to have, which is 2.01. As the main reason for not having the ideal number of children, the biggest number of 56.3% answered “because child-rearing and education costs are too expensive” (multiple answers allowed). This reflects the heavy economic burden of child rearing as one of the main factors behind the declining birthrate.

While making early childhood education free step by step mainly for low-income households, the Japanese government decided to use the consumption tax increase (rising to 10% in October 2019) as a source to fund free early childhood education and nurseries for all children aged 3 to 5, in principle, and children up to 2 years old for households exempt from residential tax payments.

### **(2) Free higher education**

From April 2020, a new higher education enrollment support system will be implemented by enhancing benefit-type scholarships. In terms of higher education, an income divide based on academic achievement has been observed, and the ratio of low-income family students attending college is low. In light of these circumstances, the government will reduce the burden of class tuition and enrollment fees, and provide deserving students with a benefit-type scholarship. The tuition-free higher education program targets students of households exempt from residential tax payments or their equivalent.

### **(3) Effectively free private high school tuition**

From April 2020, class tuition fees of private high schools will become effectively free. Today, the government offers financial assistance to support class tuition payments for students of high schools, technical colleges (from first to third grade), specialized

training colleges (post-secondary courses), and other types of schools. This financial assistance is provided to students of families with a taxable income below a certain level (annual income under around 9.1 million yen as a model household<sup>1</sup>), with the maximum amount of 118,800 yen (class tuition of public high schools) per year.<sup>2</sup> But for students attending a private high school, additional support is provided depending on the family income level. With the program revision the government plans to pay an additional amount that takes into account the average class tuition of private high schools, which is expected to make class tuition effectively free of charge for families with an annual income under roughly 5.9 million yen.

### **3. Reform of the financial burden for people of all generations**

To make the social security system beneficial for people of all generations, the financial burden must also be borne by people of all generations. In the “Action Plan of the Growth Strategy” (“Growth Strategy”) approved by the Cabinet on June 21, 2019, three items are listed under “Reforms to the Social Security System for All Generations”: (1) securing employment opportunities up to the age of 70, (2) promotion of mid-career hiring and experienced personnel hiring, and (3) preventing disease and nursing care. All of these reforms are intended to contribute to a higher rate of employment and expected to boost the number of people supporting the social security system.

#### **(1) Securing employment opportunities up to the age of 70**

According to the Growth Strategy, the physical stamina and motor abilities of seniors have been rolled back by five years of age during the course of the past 10 plus years. The report states that an analysis of people’s health condition alone indicates sufficient room to significantly increase the current employment rate of seniors.

Also, while 80% of seniors who are age 60 and older desire to work until after the age of 70, there is little difference in the actual employment rate and the desire to work for seniors aged 60 to 64, but a significant difference for seniors aged 65 or older (**Chart 2**). Considering this situation, if the working environment were improved to enable seniors aged 65 or older to work, the employment rate could be increased even further.

Currently, companies are obliged to adopt measures to offer employment opportunities for employees wanting to work up to the age of 65, but the expected revision to the law will secure employment opportunities for seniors aged 65 to 70.

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<sup>1</sup> Annual income assumes one working parent for a family of four that includes one high school student and one junior high school student.

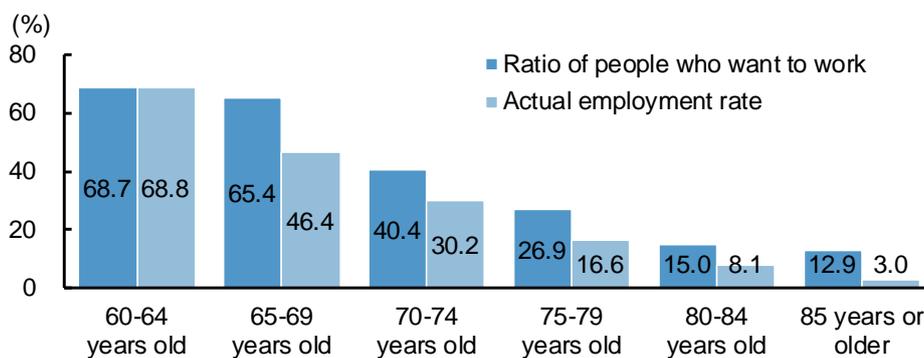
<sup>2</sup> The maximum amount provided differs for national, part-time, and correspondence high schools. If the class tuition fee is less than the maximum amount provided, the actual class tuition is paid as the maximum.

According to the draft proposals outlined in the Growth Strategy, diverse options are expected to be set out in legislation, and consideration will be given to a framework where companies determine which options to offer based on discussions between labor and management. Consideration will also be given to a framework where companies consult with individual employees about which option to take and then make this option available.

It should be noted that the options for legislation include (1) eliminate mandatory retirement age, (2) extend mandatory retirement age to 70, (3) introduce continuous employment system (including continuous employment at a subsidiary or affiliate, similar to the current system up to the age of 65) , (4) re-employment at another company other than a subsidiary or affiliate, (5) provide funding for freelance contracts with individuals, (6) support start-ups by individuals, and (7) provide funding for participation in social contribution activities by individuals. The extent of company responsibilities in these options and the detailed approaches to company involvement will require further deliberation in the future.

Legislation will be developed in two stages: in stage one, provisions will require efforts by companies, and in stage two, provisions will become mandatory. The bill for stage one legislation is expected to be submitted to the ordinary session of the Diet in 2020, but the report did not reveal the enforcement date and the timing to submit the bill for the stage two legislation.

**Chart 2: Ratio of people who want to work and actual employment rate**



Notes: 1. Ratio of people who want to work depicts the ratio of people “who wish to (continue to) work for payment” in the Cabinet Office, *8th International Comparison Survey on Life and Attitude of the Elderly* (FY2015). The elderly covered in the survey are men and women aged 60 or older.

2. The actual employment rate is the actual figure taken from the Ministry of Internal Affairs and Communications, *Labour Force Survey* (2018).

Source: Made by MHRI based upon the Ministry of Internal Affairs and Communications, *Labour Force Survey* (2018), and the Cabinet Office, *8th International Comparison Survey on Life and Attitude of the Elderly* (FY2015).

Also, the “Basic Policy on Economic and Fiscal Management and Reform 2019” (the “Basic Policy”) approved by the Cabinet on the same day as the Growth Strategy carries the policy to “promote social security system reform for all generations to realize a society where people can work throughout their entire lifetime by securing employment opportunities up to 70 years of age, and develop an environment for people of all generations to actively participate in society based on their free will and capabilities.” The main pillar to have the financial burden borne by people of all generations is to secure employment opportunities up to the age of 70.

### **(2) Promotion of mid-career hiring and experienced personnel hiring**

The Growth Strategy points out that large companies have a high ratio of new graduate hiring and a low ratio of mid-career and experienced personnel hiring. This means it is necessary to review the current hiring system and create opportunities for employees who want to work to demonstrate their abilities. More specifically, it states that the traditional focus of large companies on bulk hiring of new graduates should be reexamined, and mid-career and experienced personnel hiring should be expanded through year-round hiring. For this reason, the Growth Strategy calls on large companies to disclose information about their ratio of mid-career and experienced personnel hiring.

### **(3) Preventing disease and nursing care**

Given that more than one-third of medical care expenditures are related to lifestyle diseases, including preventable diseases, and that the ratio of preventive healthcare programs in public medical insurance and nursing care insurance is low,<sup>3</sup> the Growth Strategy states it is essential to promote measures to prevent disease and nursing care. For measures to promote disease prevention, since the role of communities and company insurers in disease prevention is important, it is essential to increase the preventive healthcare incentives for insurers. Also, concerning measures to promote nursing care prevention, given the importance of the insurers (municipalities) and their prefectures in nursing care prevention, preventive healthcare incentives will be increased for both insurers and prefectures.

According to the Growth Strategy, the effects of disease prevention and health promotion include (1) alleviating future concerns by improving individual health, (2) extending healthy life expectancy and increasing people working in good health, and increasing the bearers of social security, and (3) restraining medical and nursing-care

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<sup>3</sup> The preventive business of the national health insurance of municipalities accounts for 0.8% of total expenditures (as of FY2017), and the preventive business of nursing care insurance is 1.1% (as of FY2016).

expenditures related to lifestyle diseases to increase the sustainability of the social security system.

#### **4. Issues toward realizing a social security system for all generations**

With a view to realizing a social security system for all generations, from a benefits perspective it is important to offer more generous social security benefits to child-rearing households by providing education cost support. Given that Japan is characterized by its relatively low national burden of early childhood and higher education compared with the US and major European nations, providing free early-childhood education and expanding the scope of tuition-free higher education carry great significance.

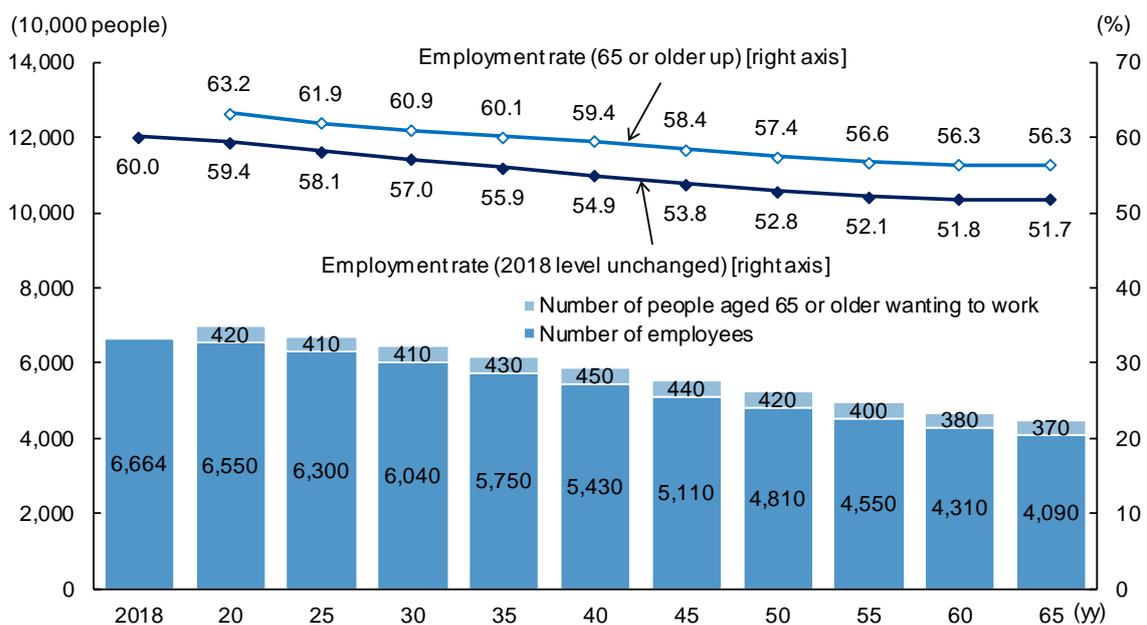
Nonetheless, for early childhood education, priority should also be given to eliminating the waiting list for children to enter a nursery. According to the Ministry of Health, Labour and Welfare, the number of children waiting to enter a nursery stood at 47,198 as of October 2018, a high number despite the decrease by 8,235 from the same month in the previous year. Also, the burden placed on parents to secure a nursing facility is quite heavy. According to a survey on “nursery hunting” (actions taken by parents to place their children in a licensed nursery school, etc.), 23.0% (the highest figure) of respondents answered that the timing to begin nursery hunting was 6 months or later after childbirth, 22.1% of respondents said they started looking for a nursery within 6 months after childbirth, and 19.6% answered “during or before pregnancy.” This suggests that parents start looking for a nursery far earlier than when their children actually attend a nursery, and many of these parents feel the heavy burden of nursery hunting. Furthermore, only 56.8% of parents could “secure the nursery they requested” after nursery hunting. Allowing parents trouble-free access to the nursery of their choice might prove an effective measure to tackle the low birthrate problem.

Meanwhile, the key to sharing the cost burden among all generations is to realize a society where people can work throughout their lifetime. If expanded availability of nurseries became a reality, as mentioned earlier, couples with children would find it easier to continue working, which would in turn boost the number of people in employment. Also, realizing the elderly’s wish to continue working would increase the number of employed people even further. As mentioned earlier, the Japanese government is moving to revise legislation to secure employment opportunities for seniors until the age of 70, but it may take considerable time to make this compulsory. As options to change the legislation to enable job opportunities up until age 70, the government lists such methods as providing funds for firms entering into freelance contracts with individuals, granting assistance to business start-ups by individuals, and so forth. But for all of the employees who wish to continue working until 70 to get job opportunities,

companies will need to prepare as early as possible for their employees to line up job options other than being a company employee before they reach 60 or 65 years old.

As shown in **Chart 2**, a gap begins to emerge between the actual employment rate and the ratio of people who want to work after workers become 65 years old. The number of employees in 2018 stood at 66.64 million with an employment rate of 60.0% (ratio of employees in the total population over 15 years of age). If we assume the 2018 employment rate remains unchanged in the future for the male/female category and the five-year age groups, the number of employees in 2065 will decrease to 40.9 million, reducing the employment rate to 51.7%. But if the employment rate of age groups older than 65 years old rises to the level of the ratio of people who want to work, the number of employees will increase by about 4 million people. This would even increase the number of employees in 2065 by around 3.7 million people, with the employment rate expected to increase from 51.7%, the expected rate in the existing employment rate scenario, to 56.3% (**Chart 3**).

**Chart 3: Outlook of the employment rate**



Note: The employment rate is the ratio of employees in the total population aged 15 or older. Data in 2018 are actual figures, and data later than 2020 are calculated by multiplying the estimated population by gender and the 5-year age groups by the 2018 employment rate for each category. The number of seniors aged 65 or older wanting to work is calculated by multiplying the difference between the ratio of people aged 65 or older who want to work (**Chart 2**) and the actual 2018 employment rate by the estimated population. The employment rate (65 or older up) means the employment rate in the case where all people aged 65 or older wanting to work actually become employed.

Sources: Made by MHRI based upon the Ministry of Internal Affairs and Communication, *Labour Force Survey (2018)*, the Cabinet Office, *8th International Comparison Survey on Life and Attitude of the Elderly (FY 2015)*, and the National Institute of Population and Social Security Research, *Population Projections for Japan (2017)*.

The expected employment rate in 2065 is expected to be lower than the rate in 2018 (60.0%) even if the elderly's desire to work becomes a reality. But if the number of two-income families increases, and the government takes actions such as promoting the employment of people under the age of 65 who have not been able to work despite their desire to do so, and improving the health condition of workers, it may be possible to maintain the current level of employment rate in the future.

In a society where its population is declining, it is also important to secure the proper income level of individual employees, in addition to enacting measures to halt the declining number of employees. Such efforts would help maintain the quality of employees' lives and ensure that all generations share the cost burden of social security, which depends on the income level of each employee. Given the significant gap in the working conditions between regular and non-regular employees,<sup>4</sup> it is important to eliminate the inequality of treatment, enhance the level of skills training for non-regular employees, and promote the conversion of non-regular employees to regular employees if they wish to change their status, among other measures. These measures should ultimately contribute to realizing a social security system for all generations.

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<sup>4</sup> The difference in income level between regular and non-regular employees is not so significant when workers are young, but the difference widens as they become older. According to the Ministry of Health, Labour and Welfare's "Basic Survey on Wage Structure" (2018), the hourly wage of non-regular employees remains about half that of regular employees when they are in their 50s.