

The Impact of Pension Reform on Households' Educational Investment

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Abstract

This paper examines the impact of a policy of reducing pension on household investment in human capital. Among the primary sources of income for retirees, pensions and personal savings are paramount. In China, a nation deeply influenced by Confucianism and a culture rooted in filial piety, legal obligations mandate the younger generation to provide support to their parents. Consequently, this implies the existence of a third income source for elderly individuals in China: intra-family financial support from their offspring. Hence, any alterations in pension policies could potentially impact the educational investments made by current employees in their children's future. This paper employs a difference-in-difference analysis to scrutinize the effects of China's 1997 urban pension reform on household behaviors concerning investments in human capital and savings. The 1997 pension reform notably decreased pensions for enterprise employees while leaving the pensions of institutional employees untouched. Empirical findings reveal that households anticipating lower pension benefits augment their investments in education by approximately 2%. Furthermore, a 10% reduction in the pension replacement rate corresponds to a 1.1% rise in households' investments in human capital. The study also extends its analysis to the 2015 pension policy, which aimed to reduce pensions for institutional employees without affecting corporate employees. Nevertheless, due to the policy's 10-year transitional period, the empirical results suggest a moderate increase in human capital investments among corporate employee households, albeit not statistically significant. In circumstances where expected pension income is diminished, households seek to compensate through increased investments in the human capital development of the next generation.

Key words: pension reform, investment in education, intra-family transfer

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