

03/2017

FINNISH CENTRE FOR PENSIONS, REPORTS

SUMMARY

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Scenario calculations on the impact of changes in work on the pension system and public finances

This report uses scenario calculations to assess the impacts of changes in work on the outlook for the pension system and for public finances as a whole. Three of the scenarios are based on the Demos Helsinki report *Work 2040 – Scenarios for the Future of Work*: they are called *honourable toilers*, *flexible producers* and *magicians' economy*. The fourth scenario is called *high employment* and it is based on the publicly-floated idea of targeting an 80 per cent employment rate.

For the present projection purposes the major distinctive feature of the honourable toilers scenario is the stagnation of economic growth. In the flexible producers scenario, the accent is on self-employment and entrepreneurship. The most characteristic feature of the magicians' economy scenario is the growth of income inequalities. Finally, as its name implies, the main distinctive feature of the high employment scenario is a much increased employment rate compared with the current level.

For each scenario the report presents calculations based on the Finnish Centre for Pensions long-term projection model. In addition, calculations are provided for the development of pension differences in the magicians' economy using the Finnish Centre for Pensions ELSI microsimulation model.

The outlook for public finances is assessed using the Ministry of Finance framework for sustainability gap analysis. These calculations are presented for the honourable toilers scenario and for the high employment scenario.

In the honourable toilers scenario, real earnings do not increase at all and investment returns are half a percentage point lower than in the baseline scenario. Statutory pension expenditure is about 3 percentage points of GDP higher than in the baseline scenario in the long term. Accordingly, the earnings-related pension contribution would be some 3.5 percentage points higher than in the baseline scenario. Average pensions show no increase from their current level, and fall well behind the development projected in the baseline scenario. The public finances sustainability gap is over one percentage point, i.e. 3 billion euros higher than the figure in the baseline scenario.

The flexible producers scenario includes two alternative projections. By 2040, the proportion of the self-employed is predicted to rise from the current figure of 13.5 per cent to either 17.5 or 25 per cent. This scenario has hardly any impact on the development of statutory pension expenditure or average pensions. The growth of self-employment has the effect of reducing the number of wage earners, creating pressure to raise pension contributions under the Employees Pensions Act. Increasing numbers would be paying contributions under the Self-Employed Persons' Pensions Act, which under current rules for the determination of pension contributions would also generate pension assets for self-employed persons.

In the magicians' economy scenario, income inequalities would widen, with 5 per cent of the employed population accounting for 60 per cent of gross income by 2040. This scenario would have no effect on earnings-related pension expenditure or contributions. It would lead to unprecedented income inequality in Finland. In the long term the income differences would translate into pension differences. In 2080 the average pension would be even slightly higher than in the baseline scenario, but the median pension would be more than one-third lower than the baseline figure. The biggest pensions would be several times higher than in the baseline scenario. With the growing incidence of small earnings-related pensions, national and guarantee pensions would have an increasing role in providing pensioners' minimum income.

Two alternative calculations are presented for the high employment scenario. In the first, baseline option, most of the positive effects on the pension system would come through the reduced volume of disability pensions. In the second alternative there is the same improvement in employment, without any decrease in disability pensions compared with the baseline scenario. In the first option earnings-related pension expenditure as a proportion of GDP would in the long term be some 1.5 percentage points lower than in the baseline scenario. The pension contribution under the Employees Pensions Act would be over two percentage points lower than in the baseline scenario. In the alternative projection these effects would be smaller. In the high employment scenario the public finances sustainability gap would be around 2.5 percentage points, i.e. six billion euros lower than in the baseline scenario.

The Publication is available only in Finnish:

Skenaariolaskelmia työn muutoksen vaikutuksesta eläkejärjestelmään ja julkiseen talouteen.
Eläketurvakeskuksen raportteja 03/2017.

Ordering of publication:

www.etk.fi > Publications > Reports > Scenario calculations on the impact of changes in work on the pension system and public finances
or aineistotilaukset@etk.fi

ISBN 978-951-691-272-4 (PDF)

ISSN 1798-7490 (online)

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