

Eurogroup Statement on the structural reform agenda - thematic discussions on growth and jobs: benchmarking pension sustainability

Following our agreement in June 2016 on common principles guiding euro area Member States' reforms to strengthen pension sustainability, the Eurogroup has discussed benchmarking as a tool to provide further support and impetus to reforms in this area, so as to foster the fiscal sustainability of pension systems and economic convergence.

The Eurogroup recalls that in times of high public debt, the importance of pension sustainability from a financial, economic and social point of view renders developments in this field a matter of common concern in the euro area. The Eurogroup considers that significant progress has been achieved in improving pension sustainability in the euro area. However, it also acknowledges that considerable risks remain in many Member States and that further policy action is needed. Against this background, the Eurogroup considers benchmarking to be a useful tool for highlighting the possible need and scope for further reform in this field.

Today the Eurogroup has agreed to benchmark the fiscal sustainability of euro area Member States' pension systems against the best performers of the euro area according to the indicators presented in the table below. Such benchmarking will rely as a matter of priority on two commonly agreed indicators measuring the gap to a sustainable fiscal position, including the impact of pension spending. These benchmarks are measurable and under the control of policy makers. In order to have a comprehensive and balanced view, they will be complemented by the following flanking indicators: the comparative level and evolution of the legal and effective retirement age, the coverage ratio and the pension benefit ratio.

While acknowledging the competences and the work carried out by other Council formations, in particular EPSCO, the Eurogroup will conduct every three years starting in 2018 this benchmarking exercise within the context of existing processes and surveillance mechanisms, in particular the Ageing Reports and the assessment of the Stability Programmes.

As the key features of pension systems interact with labour market institutions and social safety nets, the approach needs to be comprehensive. Pension sustainability also needs to be examined in its full country-specific policy context, including the existence of automatic adjustment mechanisms. The resilience of pension systems to adverse macroeconomic and demographic prospects and their social adequacy should also be taken into account in the overall benchmarking exercise, in line with the common principles adopted in June 2016.

List of indicators for the pension sustainability benchmarking exercise of the Eurogroup

Key fiscal sustainability indicators

The S1 and S2 indicators provide the backdrop to the benchmarking exercise. They are used in annual multilateral surveillance of fiscal sustainability under the Stability and Growth Pact and are based inter alia on the projections in the Ageing Report jointly prepared by the European Commission and the Economic Policy Committee. They measure medium-term and long-term fiscal sustainability risks, respectively. They are influenced by a number of parameters and technical assumptions. Hence they should be accompanied by an economic reading.

S1 with a focus on the contribution of pension expenditure

The S1 indicator shows the upfront adjustment effort required, in terms of a cumulated improvement in the structural primary balance over 5 years (starting from the year after the forecasts, currently 2019), and then sustained for 15 years (currently 2031) to bring debt ratios back to 60% of GDP, including financing for any additional expenditure arising from an ageing population. Explicitly focussing on the contribution from pension expenditure allows identifying the extent to which it contributes significantly to the fiscal gap over the projection horizon.

Sources

: Commission services, 2015 Ageing Report, 2015 Fiscal Sustainability Report, Commission forecasts.

S2 with a focus on the contribution of pension expenditure

The S2 indicator shows the adjustment to the current structural primary balance required to fulfil the infinite horizon inter-temporal budget constraint, including paying for any additional expenditure arising from an ageing population. Explicitly focussing on the contribution from pension expenditure allows identifying the extent to which it contributes significantly to the fiscal gap over the projection horizon.

Sources

: Commission services, 2015 Ageing Report, 2015 Fiscal Sustainability Report, Commission forecasts.

Flanking indicators

The flanking indicators are intended to complement the key indicators for a more comprehensive assessment of pension systems in individual euro area Member States, taking account of country-specific situations. They should also be accompanied by an economic reading.

Comparative level and evolution of legal and effective retirement age

The legal retirement age measures the age, by gender, for taking up a standard pension according to current legislation in place.

Sources

: Commission services, 2015 Ageing Report.

As a proxy for the effective retirement age, the average age at which people, by gender, leave the labour force in the age group 51-74 is chosen. When available for all euro area countries administrative data for taking up a pension will be used.

Sources

: Commission services, 2015 Ageing Report, Information provided by Member States.

Coverage ratio, level and evolution

The indicator shows the ratio of pensioners relative to persons aged 65 or more.

Sources

: Commission services, 2015 Ageing Report.

Pension benefit ratio, level and evolution

The indicator measures the average pension (public and where relevant and available private) in relation to the average wage. A high value suggests a relatively generous system, while a low value indicates the opposite.

Sources

: Commission services, 2015 Ageing Report.

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