Spain

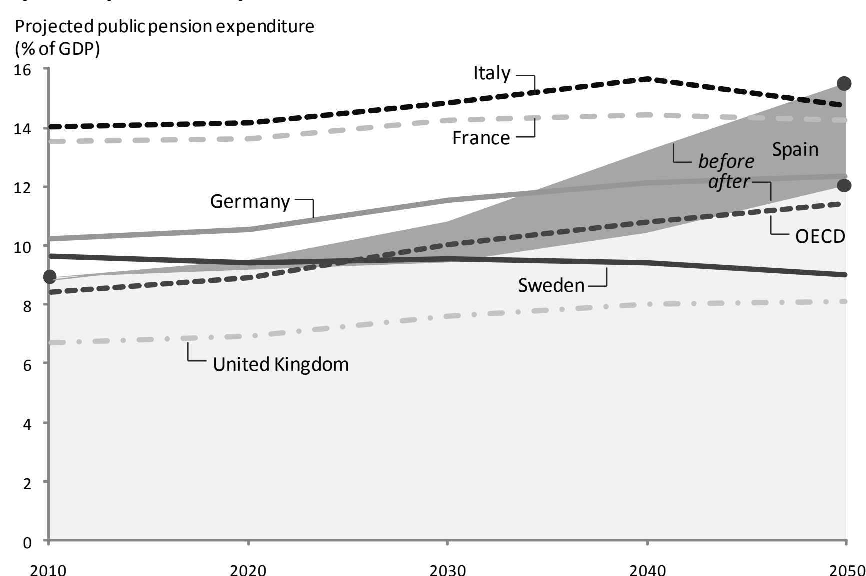
Country note: *Pensions at a Glance 2011*

Impact of the reforms: financial sustainability

The 2011 pension reform in Spain will significantly improve the long-term financial sustainability of Spain's retirement-income system. The bill, approved by the government in January and agreed with the social partners, will cut pension spending by the equivalent of 3.5% of gross domestic product (GDP) in the long term.[1] Figure 1 compares the long-term cost of public pensions in selected OECD countries.

Currently, Spain spends about 9% of GDP on pensions, a little above the OECD average, but about the same as the OECD once the demographic situation is taken into account. Current spending is much higher in France and Italy than it is in Spain. The EU's 2009 *Ageing Report* showed pension spending in Spain increasing to over 15% of GDP by 2050 (the top of the shaded area in Figure 1), surpassing France, Germany and Italy. The effect of the reform proposals, on the Government of Spain's estimates, added to the baseline forecasts in the EU *Ageing Report*, is shown by the bottom of the shaded area. This shows lower spending than France, Germany and Italy, only a little above the OECD average.

1 Projected pension expenditure in selected OECD countries, 2010-2050



Source: OECD (2011), *Pensions at a Glance: Retirement-Income Systems in OECD Countries*; OECD simulations based on Government of Spain briefing.

Impact of the reforms: pension entitlements

Disposable incomes of people aged 65+ in Spain are on average 79% of those of the population as a whole (adjusting for differences in households sizes). This is a little below the OECD average of 82%. The aggregate replacement rate, a measure that looks at the actual pensions paid out to pensioners today, is 48% which is close to EU average.

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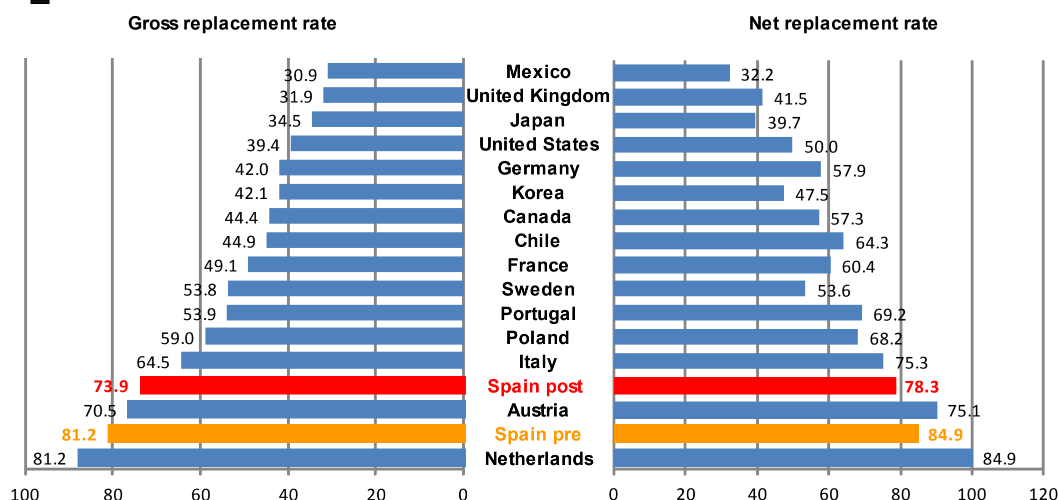
1. Note that this was after *Pensions at a Glance 2011* was finalised, and so the results in the report relate to the parameters and rules before the reform. However, revised information is included in this country note and in the on-line country profile at www.oecd.org/els/social/PaG.

The projected pension replacement rate for Spain for a full-career worker entering the labour-market in 2008 is 81.2% (Figure 2, left-hand panel). This replacement rate – pension relative to earnings when working – averages much less in the 34 OECD countries: 57.3%. The main impact of the reform on a full-career worker is the change in the measure of earnings used to calculate benefits. This is expected to reduce the replacement rate to 73.9% (on the OECD's standard assumptions of 2.5% price inflation and 2% real earnings growth). The right-hand panel shows the net replacement rate, taking account of taxes and contributions paid on retirement benefits and on earnings when working. The average net replacement rate in the OECD-34 is 68.8%.

2 Pension replacement rates for new labour-market entrants, average earners

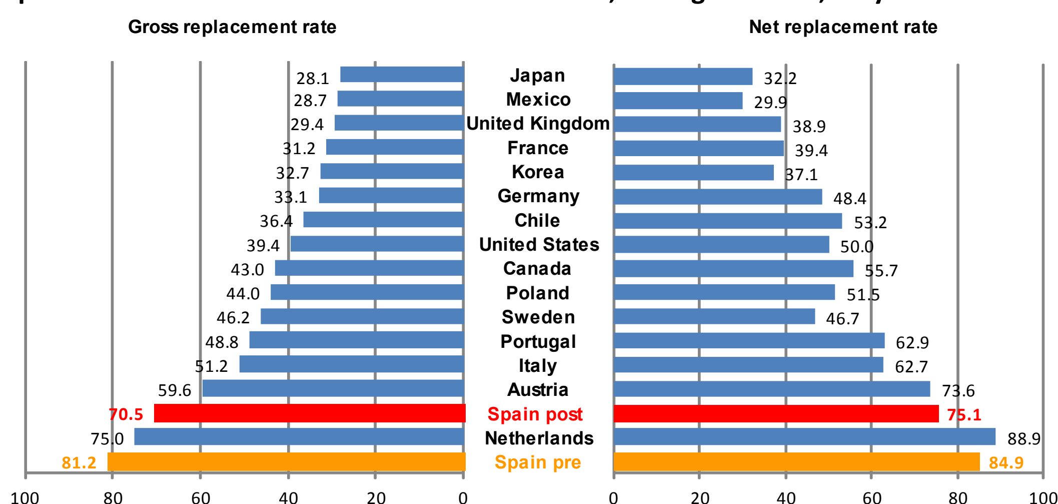


Source: OECD (2011), *Pensions at a Glance: Retirement-Income Systems in OECD and G20 Countries*; OECD pension models.

Note: In practice, many people will not have full careers, and so the actual replacement rates received will be lower than those shown by the simulation model.

The reform will reinforce the link between contributions and benefits compared with the current system. For example, the number of contribution years needed to receive a full benefit at age 67 will increase from 35 to 37 years. Only with 38.5 years of contributions will retirement at age 65 still be possible. Thus, the reform's impact will be strongest people with interrupted careers. This is illustrated in Figure 3, showing the theoretical replacement rate falling further, to 70.5%, than in the full-career case.

3 Pension replacement rates for new labour-market entrants, average earners, 10-year career interruption



Source: OECD pension models.

Note: In practice, many people with long career interruptions will receive credits (for periods of unemployment, caring for children *etc.*). These are not taken into account in this simulation.

In other countries where there are conditions related to the number of years of contributions for retiring with full (actuarially unreduced) benefits before the normal pension age, the rules are generally stricter. France is increasing the number of years to 42, while in Italy and Luxembourg, for example, the number is 40. When pension age reaches 67 in Germany, full benefits from age 65 will only be available to those with 45 years' contributions.

It is important to note that these simulations do not include further adjustments to parameters after 2027 under the automatic-review mechanism that will take place every five years, relevant to sustainability and adequacy of future benefits . These adjustments will be in line with the change in life expectancy at age 67. Life expectancy at age 67 is expected to grow by about 2.3 years for both men and women between 2027 and 2055, approximately when a recent labour-market entrant will be eligible to retire. However, the Government of Spain has not set out in detail which parameters would be adjusted (pension age, contribution years, accrual rate *etc.*). For this reason it is not possible to simulate the impact of these changes on pension entitlements. Note that the adjustment accounts for one percentage point of the 3.5 points of public pension expenditure reduction projected for 2050.

Income poverty

In the mid-2000s, 23% of older people (aged 65+) in Spain were poor, according to the OECD's standardised definition of income poverty. This compares with an OECD average of 14%. In Spain and on average in the OECD, older people were more likely to be poor than the population as whole. The poverty rate for the whole population is 14% for Spain and 11% on average in the OECD.

The value of minimum pensions in Spain has risen substantially since these data were collected. Between 2004 and 2008, these benefits increased by between 12% and 19% in real terms. This is likely to have reduced old-age poverty.

Income poverty rates do not give a complete picture of living standards in different countries. For example, they do not take account of the differences in home ownership between countries. More than 80% of people in Spain live in owner-occupied housing, a little more than in other southern European countries, such as Greece and Italy. It is a little less than the average for central and Eastern European countries, such as Estonia, Hungary and the Slovak Republic. However, it is substantially higher than much of continental Europe and the Nordic countries.

Older owner occupiers have generally paid off their mortgages, and so face much lower housing costs than people paying rent. Including the value of this so-called 'imputed rent' in evaluating living standards suggest that poverty rates for older people in Spain would be about one sixth ($^1/_6$) lower, compared with a reduction of less than one twentieth ($^1/_{20}$) for the population as a whole. The size of this effect is similar in Estonia and the United Kingdom and rather larger in Ireland than in Spain. Overall, the reduction in old-age poverty rates from including imputed income is only 40% that of Spain in 25 EU countries.[2]

4 Key facts

		Spain	OECD
Pension replacement rate	Average earner (%)		57.3
	Low earner (%)		72.1
Life expectancy	at birth	80.8	78.9
	at age 65	84.3	83.1
Population over age 65	% of working age population	26.8	23.6
Average earnings	EUR	23 200	27 800

Note: replacement rate is pension entitlement from all mandatory sources of retirement income relative to individual earnings. Calculations for a full-career worker entering the labour market in 2008. Low earner is assumed to earn 50% of the average.

Source: OECD (2011), *Pensions at a Glance: Retirement-Income Systems in OECD and G20 Countries*

2. Source: Törmälehto, V.M. and H. Sauli (2010), "The Distributional Impact of Imputed Rent in EU-SILC", Eurostat Methodologies and Working Papers, Luxembourg.

Notes to editors

Pensions at a Glance 2011:
Retirement Income Systems in OECD and G20 Countries

Published 11.00am Paris time on 27 March 2011

The report includes 36 indicators of retirement-income systems for the 34 OECD member countries and nine further G20 economies. There are five special chapters on (i) trends in pensionable ages; (ii) patterns of working and retirement at older ages; (iii) incentives to retire embedded in pension systems; (iv) helping older workers find and retain jobs; and (v|) linking pensions to life expectancy.

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