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Finnish Centre for Pensions, Studies

Summary

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Pension reform 2017: Impact of rising old-age pension age on employment and other labour market states

In this study, we examine how the rising retirement age that was agreed on in the 2017 pension reform has affected the shares of individuals in different labour market states. The retirement age has risen by three months per year as of those born in 1955. The aim of the research is to examine how the declining number of pensioners due to the rising retirement age has been reflected in the shares of people employed, unemployed, disabled, and otherwise outside the labour force.

Study based on monthly data on different labour market states

The data used includes all Finnish citizens born between 1954 and 1956 who live in Finland. For those born in 1954, the retirement age is 63 years. For those born in 1955, it is 63 years and 3 months, and for those born in 1956, it is 63 years and 6 months. The inspections are based on data on different labour market states per calendar month. The individuals are followed from when they turn 60 until they turn 64 years. Due to the rising retirement age of three months per year, individuals born in different years reach their retirement age at different ages. In our investigation, we utilise this variation in retirement age and a differences-in-differences analysis. The results can be interpreted as causal effects of the rising retirement age. As far as we know, this is also the first Finnish study which gives an overall picture of the

development of different labour market states before the old-age retirement age at a monthly level and including the whole cohort.

The share of employed has risen 1.7-fold as a result of the rising retirement age

The results show that following the three-month increase in the retirement age, the share of persons drawing an old-age pension has decreased, on average, by 37 percentage points between the old and new retirement age. At the same time, the share of employed persons has risen from the previous 29 per cent by, on average, 20 percentage points. In other words, the decrease in retirement caused by the rising retirement age is not fully reflected in employment. Overall, 54 per cent of the decrease in retirement caused by the rising retirement age is reflected in an increase in employment.

As a result of the rising retirement age, the employment rate has increased 1.7-fold. The three-month increase in the old-age retirement age has raised the employment exit age by 0.6 months, and a six-month increase in the old-age retirement age has deferred the exit by 1.3 months. Most of the increased employment can be explained by the fact that employed persons have remained in work longer due to the rising retirement age.

Unemployment and disability retirement also increased as a result of the pension reform

The reform and the rising retirement age have significantly impacted on employment but, at the same time, there are considerable substitution effects on unemployment, disability and being outside the labour force. Due to the three-month increase in the retirement age, the share of persons who are unemployed between the old and new retirement age has risen by six percentage points to almost 11 per cent. At the same time, the share of persons on a disability pension has risen from previous zero to nearly seven per cent. The share of others outside the labour force has risen by an ample four percentage points to more than six per cent. A total of 46 per cent of those who would already have retired had it not been for the rising retirement age are outside the labour market states as a result of the reform.

Passive substitution the main underlying reason for changes in unemployment and disability but active substitution also occurs

The substitution effects are mainly due to passive substitution. In other words, people remain in the same labour market state as before the rising retirement age. For example, the increase in unemployment between the old and new retirement age is mainly due to the fact that the unemployed have remained unemployed for a longer time. The same applies to disability.

Due to the rising retirement age, some active substitution has also occurred. All in all, 12 per cent of the employed who, without the rising retirement age, would be retired

have become unemployed, transitioned to disability pension or otherwise outside the labour force. Active substitution has also occurred among the unemployed, that is, some of the unemployed have become employed or have retired on a disability pension or otherwise transitioned to outside the labour force. Since the employed outnumber the unemployed, transitions from employment are considerably more significant than transitions from unemployment.

New review when retirement age has increased more

The results of the study depict the effects of the rising retirement age in the very short term, that is, in a situation where the retirement age has not risen very much. Nevertheless, the largest impact of the rising retirement age on employment and other labour market states occurs at the point of the rising retirement age. In that respect, the conducted study offers a view of the effects of the pension reform that points in the right direction. Despite this, the investigations should be repeated when the retirement age has increased more.

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