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EXECUTIVE SUMMARY

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Determinants of old-age retirement during the 2000s: A register-based study

As a result of the ageing of the baby-boomers, the population of Finland is rapidly going grey. It has been estimated that the cohorts coming into working age will not be large enough to fill in the gap left in the workforce by the retiring baby-boomers. While the working-age population will reduce in numbers, the retired population will grow. This is a complicated equation. In recent years, public debate has focused strongly on whether the labour force will be sufficient and the pension provision financing sustainable. Suggestions to solve the challenges relating to the ageing population include, in particular, the increasing of the employment rate and the prolongment of working lives. To support these goals, major amendments to pension legislation have been made.

In 2005, Finland experienced its largest pension reform ever. One central change was the abolishment of the general retirement age of 65 years and the introduction of the flexible retirement age, allowing employees to retire at their own choice between the ages of 63 and 68. At the same time, the early retirement age rose from 60 to 62 years. In addition, the opportunities to retire early through various early retirement routes were restricted considerably. Pension accrual rates based on age were changed to be age-dependent in a way that strives more visibly than before to encourage employees approaching retirement age to continue working. The actuarial assumptions of pensions were clarified by basing the calculation of pensions on annual earnings rather than on employment relationships. The life expectancy coefficient was also introduced in order to reduce pensions in line with the growing life expectancy.

The aim of all these amendments was to change individuals' labour market behaviour to prolong working lives and increase employment rates. In the short term, the effects should be visible particularly among the ageing population that is approaching retirement age and has to choose between continuing at work and retiring. From this point of view, the effects of the reform on the individuals' retirement behaviour are central. Eight years have passed since the reform, but so far there is no empirical, register-based post-reform information on the actual behavioural impact of the reform.

This study investigates the labour market behaviour of the elderly. The development of employment in the 2000s among different age groups is examined, as is the transition from working life to old-age retirement or some pre-retirement stage (unemployment, outside the labour force or on some other form of pension). The study is conducted using both descriptive and econometric analysis. Econometric analysis is used to establish the characteristics of persons retiring or otherwise exiting the labour force at the beginning and end of the 2000s.

This study focuses particularly on retirement on old-age pension. It is justified to study the transition from gainful employment to retirement and underlying factors for this event since the number of persons retiring directly on old-age pension has increased throughout the 2000s. In addition, the retirement process has changed; currently, two out of three retirees retire directly on an old-age pension. Only a decade ago, the majority of persons transferred to old-age pension from a disability or unemployment pension.

The central aim of the empirical analysis is to find out whether the underlying factors of the retirement decisions and the profiles of retirees have changed in the 2000s. The study is conducted using fresh data compiled from the registers of the Finnish Centre for Pensions. This individual-level register-based data covers the entire 2000s and forms a representative sample of ageing Finnish citizens, including versatile background information on the individuals. This type of analysis has not been done before.

It should be emphasised that the analyses do not aim to assess the impact of the 2005 pension reform by calculating exact effects of the reform on the effective retirement age or the employment rate. Instead, the aim is to produce information on background factors relating to labour market transfers and possible changes that they have undergone in the 2000s. The term 'pension reform' is used at times, however, because the year 2005, in which the pension reform took effect, functions as a temporal divide in the reviews of this study.

The results show that the employment rate of the elderly has grown steadily in the 2000s. The development has been particularly positive among those aged 55 and above. In practice, this age group is the only one where the number of employed persons has increased faster than the population. The increase in the employment rate of the elderly began already before the mid-2000s, but the positive development of the employment rate of the older cohorts in particular has been strengthened towards the end of the 2000s.

For example, the employment rate of 55–59-year-olds was only 60 per cent in 2000, but in ten years, it rose to over 70 per cent. In the same period, the employment rate of 60–64-year-olds more than doubled. In 2000, only one in five persons of this age group was employed. In 2010, the figure had doubled to two in five. The employment rate of the 65–69-year-olds grew even faster in the 2000s, when it more than doubled. In 2010, the employment rate was nearly 10 per cent.

The growing labour market activity of the elderly is a considerable phenomenon. Numerically, the group of 65–69-year-old employees is still fairly small, but as the majority of the baby boomers are only about to reach this age, the choice to continue working may be pivotal in terms of having a sufficient labour force in the future. Another considerable feature of the work input offered by the elderly is that economic cycles do not seem to wobble the employment of the elderly population as fiercely as they do that of the younger population.

The descriptive analysis shows that the age profiles of continuing at work and retiring clearly deviate when comparing the early 2000s to the late 2000s. The differences are striking at ages 60, 63 and 65. Before the reform, every fifth person of those employed in the previous year left employment at age 60. Approximately half of them retired at that time. After the pension reform, the share of persons leaving employment was halved and hardly any people retired on old-age pension at age 60. Instead, an increasing number of people, approximately every third, retired at age 63 after the reform. Among those aged 64, the change is even more pronounced. Before the pension reform, only every tenth person aged 64 retired on old-age pension, while, after the pension reform, the number of new old-age retirees among this age group quadrupled.

Prior to the pension reform, practically everyone left employment and retired on old-age pension at age 65 at the latest. After the pension reform, nearly half of those employed in the previous year remained at work at age 65. Since then, the share of people continuing at work has risen steadily; some continue working at and beyond the age of 68. Thus, it would seem that a person staying at work at an older age is more likely to continue working.

The results based on the econometric analysis show that the profiles of retirees on old-age pension have changed in the 2000s. Age is a major determinant of retirement, but its impact varies clearly between the early and the late 2000s, even after the impact of other background factors have been controlled for. Closing down the route to retirement for younger persons while simultaneously opening up the doors for continued working for the elderly is also evident in practice. After 2005, the retirement rate of 60–61-year-olds and those aged 65 and above has gone down while continued working has increased. Instead, persons aged 63–64 retire more often than before.

The results show that there is a connection between education and retiring. The highly educated are more likely to retire directly on old-age pension, i.e. to continue working until the retirement age, than are those with a lower-level education. After 2005, this impact has become evident in particular among the most highly educated.

It is also worth noting that a weak health raises the risk of retirement. After 2005, the impact of the longest sick leaves, in particular, has become more pronounced. In other words, the results indicate that some of the people on long-term sick leaves can transfer from working life directly to retirement using normal channels rather than exiting from the labour force via e.g. disability pension. Good health, on the other hand, increases the likelihood for continued working.

An interesting observation is that, unlike in the early 2000s, unemployment no longer functions as a considerable hindrance for retirement at the end of the 2000s. In other words, it appears that some of the unemployed can retire normally from gainful employment rather than being covered by long-term unemployment benefits prior to retiring.

The results also reveal that there is a connection between income and retirement: mid-sized income earners are more prone to retire directly on old-age pension than those in other income classes. However, the impact of earnings has changed in the 2000s: after 2005, belonging to the highest income class clearly prevents retirement. At the same time, this means that persons with a large income are more likely to continue working than are persons with lower income.

The area of residence also affects the retirement decision. In areas with high unemployment, it is more common to retire than in areas with low unemployment rates. This feature has gained strength towards the end of the 2000s. The phenomenon may partly reflect the weak economic situation at the end of the 2000s.

This study provides basic information on the employment development of the elderly, on retirement on old-age pension and its underlying factors in the first decade of the 21st century. Although the behavioural changes by age groups are clear based on empirical analyses, it was not possible to assess the effects of the 2005 pension reform on, for example, the retirement age. Nor was it possible to clarify the impact of altered financial incentives on the retirement behaviour. These issues will be addressed in further studies.

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