



An Roinn Airgeadais  
Department of Finance

## Submission to Commission on Pensions

March 2021

Prepared by Economics Division  
Department of Finance  
[finance.gov.ie](https://www.finance.gov.ie)

## Executive Summary

The scientific evidence is clear and unambiguous: Ireland's population is ageing and this natural process is set to accelerate over the medium- and longer-term. Structural reforms to address the fiscal cost of population ageing are essential in order to keep the public finances on a sustainable path.

While Ireland's demographic structure is relatively favourable at present, shifting demographics in the coming decades will result in a slower pace of economic expansion and increased expenditure pressures putting significant pressure on the public finances. Indeed, recent projections from Eurostat point to Ireland having one of the most rapidly ageing populations in the EU over the coming decades.

Ireland's old-age dependency ratio – the number of retirees as a fraction of the number of workers – is set to nearly double over the next 30 years, increasing from 24 per cent at present to 47 per cent by the middle of this century. Put another way, there are currently around 4 persons of working age for each person aged 65 and over; by 2050, the equivalent figure will be just over 2. This will involve increased outlays in demographically-sensitive components of public expenditure, such as pensions and healthcare.

Analysis undertaken by the Department suggests annual age-related expenditure is set to increase by 8 percentage points of GNI\* by the mid-point of the century. In other words, this means by 2050 the annual cost of age-related expenditure is set to be €17 billion higher, in today's terms, than in 2019.

Revenue increases will not be sufficient to fund all of these additional costs. This is because growth in the productive capacity of the Irish economy is set to slow significantly, as demographic trends weigh on additional labour supply. As public revenue evolves in line with economic growth, slower revenue growth will make it more difficult for the public finances to absorb the increase in age-related spending.

Without policy intervention to mitigate the inevitable implications of ageing demographics, independent of the impact of the Covid-19 pandemic, the public finances will be on an unsustainable trajectory.

Simulations show that, in a hypothetical scenario in which there were no further policy responses, the impact of population ageing would contribute to a significant increase – of the order 90 percentage points – in the debt-to-GNI\* ratio by 2070.

Analysis by the Department shows that maintaining the State Pension Age at 66, compared with proceeding with previously legislated increases, could result in additional costs of approximately €50 billion over the long-term. Policy reforms such as linking the State Pension Age to life expectancy could significantly reduce the cost burden.

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<sup>1</sup> The data and analysis set out in this document are compiled by Department of Finance staff. Every effort is made to ensure accuracy and completeness. When errors are discovered, corrections and revisions are incorporated into the digital edition available on the Department's website. Any substantive change is detailed in the online version.

## Section 1: Introduction

A projected shift in the demographic composition of the Irish population in the coming decades will pose significant challenges for the public finances. Under standard assumptions, the old-age dependency ratio – the number of retirees expressed as a fraction of the number of people of working age – is set to double between now and the mid-part of the century. This means that while there are currently around four persons of working age for each person aged 65 and over in Ireland, by 2050 the equivalent figure will be around two. Population ageing will involve increased outlays in demographically-sensitive areas of public expenditure, such as healthcare, pensions and long-term care. It will also involve a moderation in the pace of economic growth, as a key source of growth, namely labour supply, becomes less prominent.

In November 2020, and consistent with the *Programme for Government*,<sup>2</sup> the Government established the *Commission on Pensions*. The remit of the Commission is to examine sustainability and eligibility issues with the State Pension and the Social Insurance Fund. The Commission will also consider the issue of retirement ages in employment contracts and consider how the pension system can further accommodate carers.

This document is the submission of the Department of Finance to the Commission. Sound public finances are a pre-requisite for economic growth. A key strategic goal of the Department of Finance is therefore the achievement of a “sustainable macroeconomic environment and sound public finances.” In this context, it is important to understand, assess and report on the impact of shifting demographic trends on the public finances in Ireland and, in particular, on the long-term sustainability of the public finances.

The purpose of this submission is to highlight the likely economic and budgetary impacts of demographic change in Ireland. The analysis set out in the document attempts *inter alia* to quantify the likely budgetary costs of population ageing in order to inform the appropriate policy response. It builds on work undertaken by the Department of Finance in conjunction with other Finance Ministries in the European Union, together with the European Commission, through the EU Ageing Working Group (AWG).<sup>3</sup> The long-term expenditure projections underpinning this submission will be made public in full in the *2021 Ageing Report*, expected to be published in Q2 2021. Further detailed analysis will be included in the Department of Finance’s triennial publication on the impact of population ageing on the public finances in Ireland, which will be published over the summer.

It is important to note that detailed analysis of the impact of the Covid-19 pandemic is not included in these projections. The projections contained in this submission are underpinned by long-term demographic projections produced by *Eurostat* and macroeconomic projections produced by the European Commission. The demographic projections, published in early 2020, do not take account of the impact of the pandemic on demographic indicators, while

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<sup>2</sup> *Programme for Government: Our Shared Future*, available at: <https://www.gov.ie/en/publication/7e05d-programme-for-government-our-shared-future/>

<sup>3</sup> Officials from the Department of Finance are members of the Ageing Working Group (AWG), a sub group of the Economic Policy Committee (EPC), contributing to the triennial EPC Ageing Report, a set of long-term budgetary projections underpinned by population projections provided by Eurostat.

the macroeconomic projections assume a V-shaped recovery entailing a sharp decline in output in 2020 followed by a return to strong economic growth in 2021, with no long-term structural impact. In these circumstances, risks to the projections presented herein are, if anything, to the downside.

Officials from the Department presented a provisional version of this analysis to the Commission on Pensions on December 4<sup>th</sup> 2020. This submission updates and expands upon that presentation.

This submission is structured as follows. Section 2 describes the projected demographic shift in the composition of the Irish population over the coming decades. This section also details the projected impact on the productive capacity of Irish economy of such a change in the demographic structure. In section 3, the budgetary cost of an ageing population is outlined, with particular attention paid to the development of future pension expenditure. Section 4 analyses, for illustrative purposes, the potential impact of demographic change on key fiscal metrics, on a hypothetical no-policy change basis. In section 5, the consequences of making changes to the State Pension Age is explored. Section 6 concludes.

## Section 2: Demographic and macroeconomic developments

As outlined in the Department of Finance's report *Population Ageing and the Public Finances in Ireland* (2018), an ageing population is now a notable feature of many advanced economies.<sup>4</sup> In this regard, Ireland's current age structure compares favourably to other EU countries.

Ireland currently has the highest share of population aged under 20 years old (27.1 per cent), the joint lowest median age (37.7 years) and the lowest share of the population aged 65 or above in the EU (14.1 per cent). However, the composition of Ireland's population is set to change significantly over the coming decades with a notable increase in old age dependency ratios.

### 2.1: Eurostat population projections

Projections outlined in this submission are underpinned by Eurostat's long-term demographic projections, EUROPOP 2019.<sup>5</sup> On this basis, the share of the population aged 65 and over is set to steadily rise – nearly doubling from 14.3 per cent in 2019 to 27.5 per cent in 2070.<sup>6</sup>

The projection for the population at a point in time is determined by the evolution of three variables:

- the number of births
- the number of deaths
- migration flows

Eurostat projections suggest fertility rates in Ireland, which have historically been comparatively high, are expected to remain well below levels seen in the early and mid-part of the last century, while the natural increase in the population, i.e. births versus deaths, is expected to decelerate – eventually turning negative in 2063 (figure 1).

Between 2019 and the mid-point of the century, these projections assume net migration to average approximately +20,000 per annum, broadly in line with the CSO's M2 migration scenario.<sup>7</sup> From 2050-2070, net migration is projected to average +12,000 per year.

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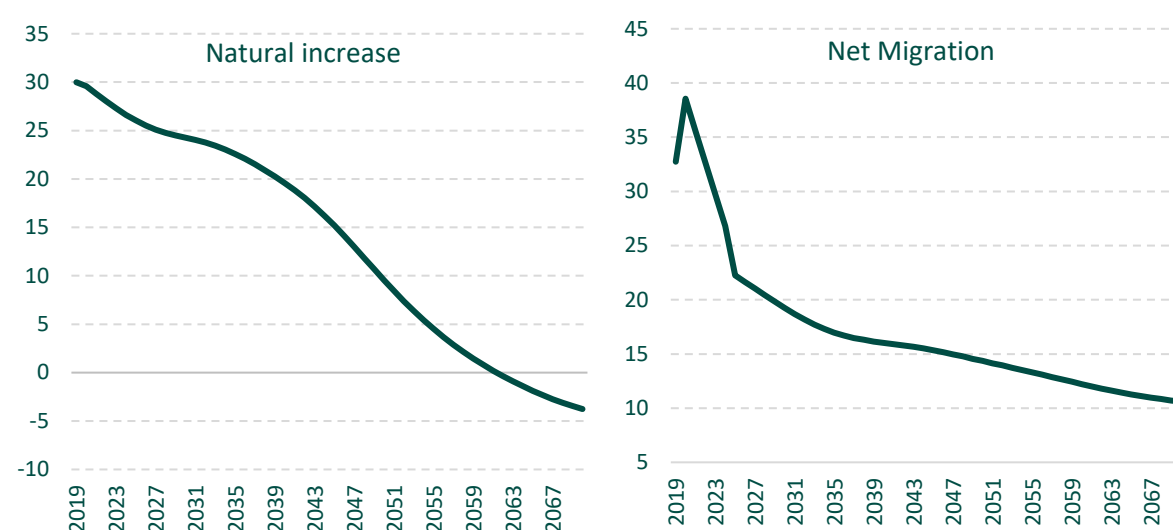
<sup>4</sup> <https://assets.gov.ie/4147/101218131007-cdad7ec478c4467290c52008da8f536d.pdf>

<sup>5</sup> <https://ec.europa.eu/eurostat/web/population-demography-migration-projections/population-projections-data>

<sup>6</sup> EUROPOP 2019 includes projections out to 2100, however, in the context of this work, we concentrate on a projection period from 2019-2070, in line with the framework of the 2021 Ageing Report.

<sup>7</sup> Migration assumption from the CSO's Population and Labour Force Projections 2017-2051. The CSO used three migration assumptions to underpin their long-term pension projections. The M2 migration scenario represents the midpoint scenario with net inward migration of 20,000 per annum assumed (M1 assumed net migration of +30,000 and M3 assumed +10,000 per annum. As highlighted by the CSO, annual average net inward migration for the 20 year period from 1997 - 2016 was 21,400. Therefore, the M2 scenario reflects both current and twenty year average net inward migration trends. More details available at: <https://www.cso.ie/en/releasesandpublications/ep/p-plfp/populationandlabourforceprojections2017-2051/>

**Figure 1: natural increase and net migration, thousands**



Source: Eurostat.

Turning to life expectancy, this is expected to continue rising. Male life expectancy is expected to increase by 5.7 years from 2019 to 86.8 by 2070, while female life expectancy is expected to increase by a similar degree, 5.6 years, to 90.4 by the same point (figure 2).

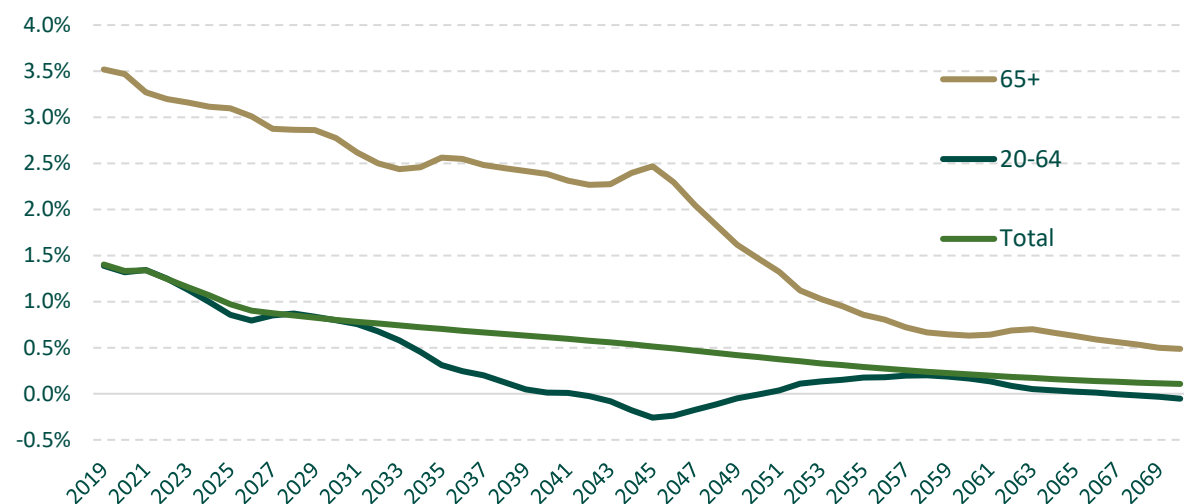
**Figure 2: male and female life expectancy, years at birth**



Source: Eurostat.

Putting all this together, the Irish population is projected to grow by 1.0 per cent on average each year until 2030, before growing at 0.6 per cent on average per annum until the mid-point of the century, reaching 6.2 million. Thereafter, the pace of annual population growth is expected to more than halve to 0.2 per cent, with the population reaching 6.5 million in 2070. Critically, however, the population aged 65 and over is set to grow significantly faster than the population aged 20 to 64, i.e. the working age population, over this period.

**Figure 3: annual population growth by age cohort, y-o-y growth**

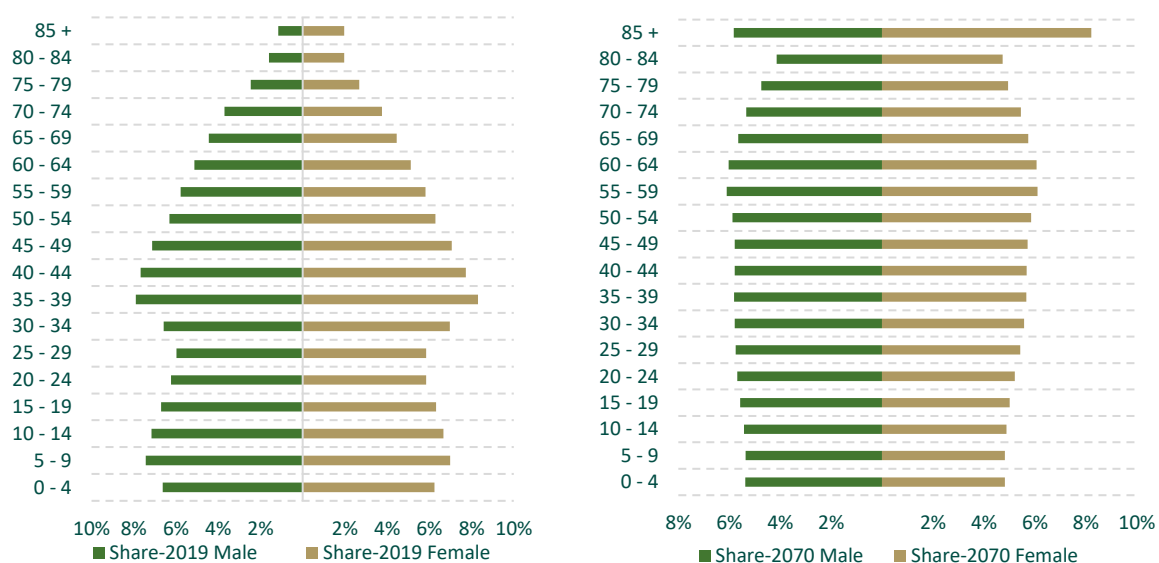


Source: Eurostat.

While the demographic projections expect a large rise in the Irish population out to 2070, the composition of the population will be very different by this point. Figure 4 below, sets out the so-called ‘population pyramid’ – the share of the population accounted for by each five-year age cohort in 2019 and in 2070. The projected shift in the composition of the Irish population is clearly visible in this figure. Indeed, the share of those aged 85 is expected to be roughly 4 times higher than was the case in 2019. While the share of the Irish population in the 85 and over bracket was the smallest of all the cohorts in the pyramid in 2019, by the end of the projection period, it is projected to become one of the largest.

It is unavoidable that this will have sizable implications for the public finances given the expected demand on pension-related spending, in particular.

**Figure 4: population pyramids in 2019 and 2070**

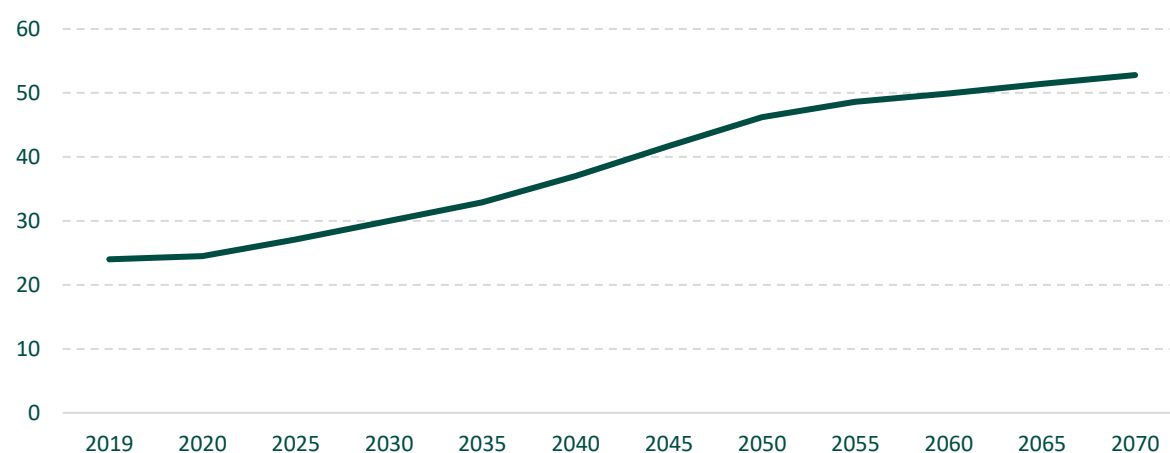


Source: Eurostat.



In addition, the share of the working age population (WAP), defined here as those aged 20-64 relative to the total population, is set to decline consistently over the projection period, from 58.8 per cent in 2019 to 51.9 per cent in 2070.<sup>8</sup> Reflecting these changes, the Old Age Dependency Ratio (OADR), which essentially sets out the size of the population considered to be at or above retirement age compared to the working age population, is set to more than double from 24.2 per cent in 2019 to 53.0 per cent in 2070.<sup>9</sup> These developments will make Ireland one of the most rapidly ageing EU Member States.

**Figure 5: old-age dependency ratio (population 65 + / population 20 to 64), per cent**



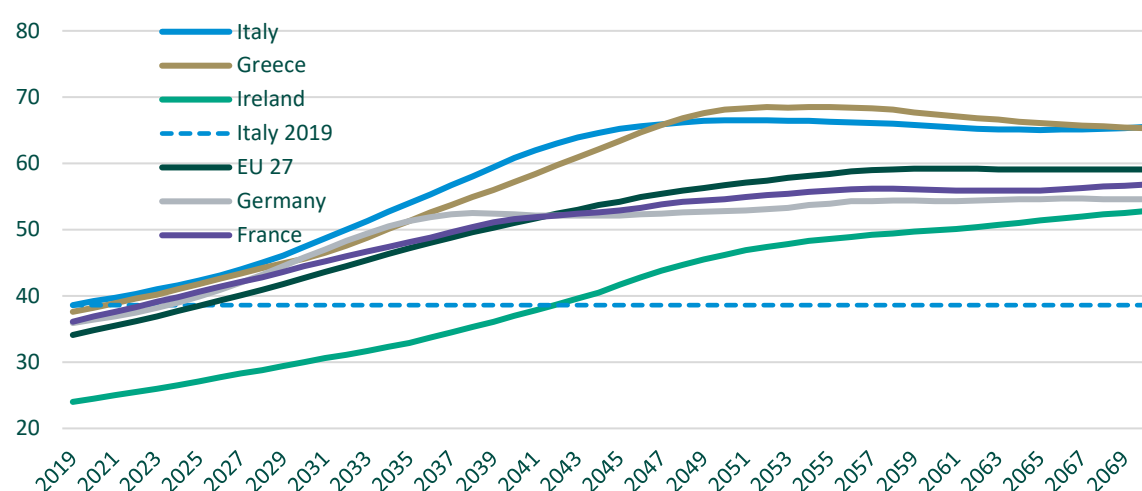
Source: Eurostat.

This ageing process is expected to see Ireland converge towards EU norms in terms of demographic structure by 2070, with the OADR in Ireland set to overtake the current equivalent figure in Italy, a country viewed as currently battling the adverse effects of an aged population, over the next 20 years.

<sup>8</sup> While the State Pension Age in Ireland is currently 66 years of age, the working age population is defined here as 20-64 to allow for cross-country comparison.

<sup>9</sup> The Old-Age Dependency Ratio (OADR), a key metric in demographic analysis, is defined here as the population aged 65 and above divided by the population aged 20-64. The OADR is often used internationally as a proxy indicator of the ratio of the non-working to the working population.

**Figure 6: old-age dependency ratio - comparison with other EU Member States, per cent**



Source: Eurostat.

## 2.2: Macroeconomic projections

Long term economic forecasts rely on the assumption that output moves in line with the growth rate of labour input (labour supply) together with an assumption of how productive each unit of labour is (labour productivity).

While labour productivity across the EU is assumed to converge, the growth rate of labour supply is expected to slow significantly by the mid-point of the century, as a result of population ageing. Consequently, GDP growth over the next half century is projected to slow relative to current growth rates. The baseline outlook envisages a Covid-related fall in GDP growth from 5.5 per cent in 2019 to -8.0 per cent in 2020 before recovering in 2021 (6.0 per cent).<sup>10</sup> Following this, growth is expected to slow to an average of 2.5 per cent from 2022 to 2030, stabilising thereafter at an average of 1.6 per cent per annum over the rest of the projection period to 2070.

<sup>10</sup> As highlighted in Section 1, this is based on the European Commission's Spring 2020 forecast. This forecast assumes a V-shaped recovery, entailing a sharp decline in output in 2020 followed by a return to strong economic growth in 2021, with no long-term structural impact. While the assessment of GDP growth for 2020 in Ireland has changed since the time of these forecasts (May 2020), the view of the long-term trajectory has not altered significantly since then.

## Section 3: Age-related expenditure projections

This section outlines the projected long-term expenditure projections related to the demographic changes discussed in the previous section. Under the Ageing Report framework, total age-related spending is made up of pension, health care, long-term care and education expenditure.<sup>11</sup> The expenditure projections outlined in this section will form the basis of the 2021 Ageing Report and will be expanded upon in the Department of Finance's forthcoming paper on the impact of population ageing on the public finances in Ireland.

### 3.1: Total age-related expenditure projections

Table 1 sets out the projected increase in age-related expenditure over the period 2019-2070. As outlined in section 1, the demographic projections underpinning these projections do not take into account any impact from the Covid-19 pandemic, while the macroeconomic projections assume a V-shaped recovery with a fall in GDP of 8.0 per cent in 2020 and GDP growth of 6.0 per cent in 2021.<sup>12</sup>

As outlined in the previous section, Ireland currently has a favourable demographic structure. Despite this, age-related expenditure still amounted to 21 per cent of GNI\* in 2019. Furthermore, this cost is expected to increase by an average of nearly 0.3 percentage points of GNI\* or €650 million each year in the short-term. As a result, by 2030, age-related expenditure is expected to cost an additional 3.3 percentage points of GNI\* a year compared to 2019, the equivalent of an extra €7 billion a year, in today's terms.<sup>13</sup>

Over the long-term, as the population ages significantly, total age-related expenditure is projected to increase by 6.3 percentage points of GDP, or 10.2 percentage points of GNI\* from 2019, to 31.6 per cent of GNI\* in 2070.

**Table 1: total age-related expenditure projections 2019-2070, per cent of GNI\*<sup>14</sup>**

	2019	2030	2040	2050	2060	2070	Δ2009-2018
Pension	7.4	9.6	11.2	12.1	12.2	12.3	+4.9
Health care	6.6	7.2	7.8	8.3	8.7	8.9	+2.3
Long-term care	2.0	2.7	3.2	3.9	4.6	5.2	+3.2
Education	5.3	5.3	5.0	5.2	5.2	5.1	-0.2
Total age-related	21.4	24.7	27.2	29.5	30.7	31.6	+10.2

Based on Ageing Report framework. Source: 2021 Ageing Report, European Commission and Department of Finance.

<sup>11</sup> As part of the Ageing Report framework, individual member states are responsible for the provision of the pension expenditure projections while the European Commission provide the health, long-term care and education expenditure projections with input from member states.

<sup>12</sup> Short term macroeconomic projections based on the European Commission's Spring 2020 forecasts.

<sup>13</sup> Based on estimates of GNI\* in the CSO's 2019 National Income and Expenditure publication.

<sup>14</sup> Statistical distortions to GDP, that overstate the size of the Irish economy, mean expenditure projections scaled by GDP can paint an overly benign picture. GNI\* is also used as a denominator in an attempt to better capture the repayment capacity of the economy.

### 3.2: Pension expenditure projections

In line with the focus of the Commission on Pension's work, this section focuses on the pension expenditure component of the total age-related projections. These projections, compiled by the Department of Finance, have been endorsed by the European Commission and members of the AWG following an extensive peer review process. In line with the *Social Welfare Bill 2020*,<sup>15</sup> passed in December 2020, the no-policy framework under which these projections were produced, the baseline assumes the State Pension Age (SPA) stays constant at 66 years of age throughout the entire period.

The pension expenditure projections submitted to the European Ageing Working Group include the State (Social Welfare) Pension and the Public Sector Pension.<sup>16</sup> As requested, the Department of Finance provided the Commission on Pensions with the below table, that focuses solely on the expenditure related to the State (Social Welfare) Pension for recipients aged above the SPA of 66.<sup>17</sup>

Under this disaggregation, highlighted below, expenditure related to those aged below the SPA is projected to increase by 5.5 percentage points of GNI\* from 3.8 per in 2019 to 9.2 by the end of the projection period.

**Table 2: disaggregated pension expenditure, as per cent of GNI\***

	2019	2030	2040	2050	2060	2070
Social Welfare Pension (a)	5.8	7.2	8.5	9.9	10.7	11.3
Public Sector Pension (b)	1.6	2.4	2.7	2.3	1.5	1.1
(a+b) Total Pension (c)	7.4	9.6	11.2	12.1	12.2	12.3
Total below SPA (d)	2.0	2.1	2.1	2.0	2.0	2.0
<b>(e) Social Welfare Pension excluding expenditure below SPA (a-d)</b>	<b>3.8</b>	<b>5.0</b>	<b>6.4</b>	<b>7.9</b>	<b>8.7</b>	<b>9.2</b>
(f) Total Pension excluding expenditure below SPA (c-d)	5.4	7.5	9.1	10.1	10.2	10.3

Rounding may affect totals. Source: Department of Finance.

<sup>15</sup> Social Welfare Bill 2020 repeals the previous legislated plans to increase the State Pension Age to 67 in 2021 and 68 in 2028.

<sup>16</sup> Under the Ageing Report classification, State (Social Welfare) Pension expenditure is made up of the following components: *Old Age* (including flat component and minimum, i.e. State Contributory and Non-Contributory Pension), *Survivors'* (including Widows'/Widowers'/Surviving Civil Partners' Pension), *Disability* (including Invalidity Pension, Disability Pension, Blind Pension) and *Other* (including Illness Benefit, Deserted Wife's Allowance and Benefit, Carer's Allowance and Benefit).

<sup>17</sup> This disaggregates pension expenditure to include just expenditure related to recipients aged at or above the State Pension Age in the *Old Age* and *Other* categories outlined above.

## Section 4: Impact of ageing on key fiscal indicators

The previous section sets out the projected cost of ageing in the context of national income (GDP and GNI\*). Statistical distortions to GDP, that overstate the size of the Irish economy, mean expenditure projections scaled by GDP can paint an overly benign picture. GNI\* is also used as a denominator in an attempt to better capture the repayment capacity of the economy. That being said, additional analysis is needed to examine the sustainability of the public finances in relation to the expected shift in the demographic structure of the population over the coming decades.

For illustrative purposes, the analysis in this section highlights the potential impact of population ageing on the budget balance and public debt in the event that budgetary policy did not adjust to the challenges posed by population ageing.

### 4.1: Impact on the general government balance and debt-to-income ratio

In this no-policy-change scenario, non-age related expenditure as a share of GNI\* is assumed to remain unchanged over the forecast horizon while total revenue is assumed to move in line with nominal GDP/GNI\*. <sup>18</sup> In this simplified scenario, deficit and debt dynamics are driven solely by the age-related expenditure projections.

The starting point for this exercise is outturn fiscal data from 2019. While the macroeconomic projections underpinning this analysis envisages a sharp decline in output in 2020, it does not capture the significant increase in expenditure related to the support measures implemented by the Irish Government during the Covid-19 pandemic. As such, the deficit in this exercise in the short-term may be understated.

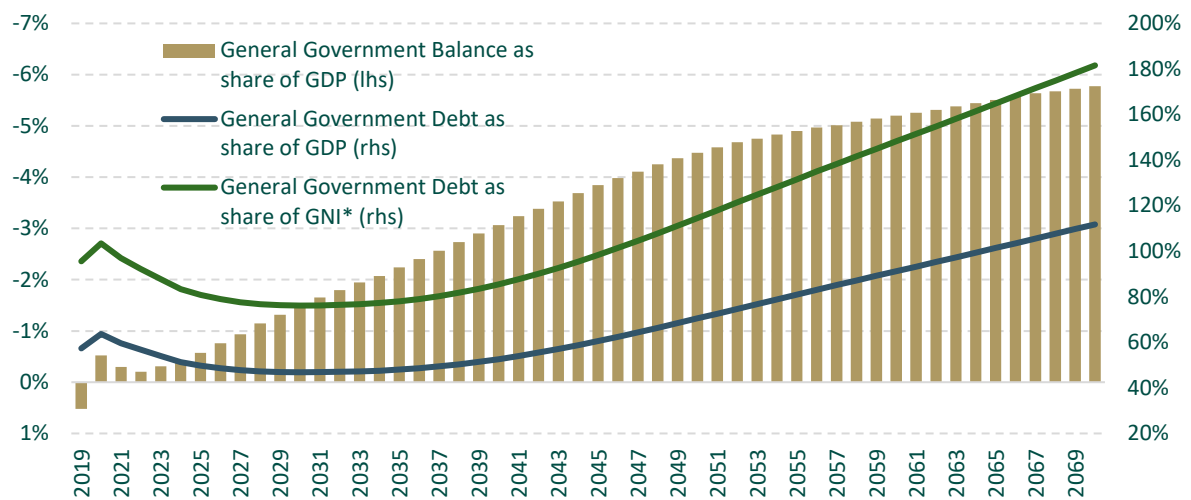
Despite this significantly more positive starting point, age-related increases in public expenditure and a slower pace of revenue growth lead to the emergence of a significant deficit by the end of the next decade, reaching just below 3 per cent of GDP (-4.7 per cent of GNI\*). The deficit is projected to continue to increase sharply thereafter, reaching just below 6 per cent of GDP (-9.4 per cent of GNI\*) by 2070, without policy intervention. As a result of these developments, the debt-to-income ratio is projected to increase by 54 percentage points of GDP, or 86 percentage points of GNI\* to reach 112 per cent of GDP, 182 per cent of GNI\*, by 2070.

It is important to note that the simulations do not take into account second round effects or non-linearities. For instance, continuing to run deficits of this magnitude would, almost certainly, result in a significant risk premium, with adverse implications for sovereign borrowing costs and the interest bill. Increases in interest rates with such elevated levels of debt would put significant pressure on the public finances.

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<sup>18</sup> Potential GDP/GNI\* growth is assumed to in parallel over the projection period.

**Figure 7: evolution of key fiscal ratios on a no-policy change basis, per cent ^**



^ does not capture impact of Covid-19 pandemic and related support measures. Source: Department of Finance.

This is of course a highly stylised scenario, however, it illustrates the impact of population ageing on the public finances and the need for policy intervention to ensure the sustainability of the public finances.

### Box 1: supplementary pension coverage

While pensions may be considered an issue with a medium to long-term horizon, changing demographic and work arrangements imply that various policy responses merit consideration. Data from the CSO illustrates the persistence of low supplementary pension coverage, with only around half of those in work actively contributing to a pension.<sup>19</sup> When adjusted for the public sector, where occupational pensions are largely mandatory, the remaining private sector pension coverage stands at about a third of those in employment. Inertia and affordability are cited as significant factors in explaining these low rates, with about 60 per cent of workers with no supplementary pension indicating they will rely upon the State for pension provision. From a fiscal sustainability perspective, such an outcome would clearly place a significant future strain on Exchequer resources.

Accordingly, such data underscores that part of the appropriate response should be to encourage citizens to save adequately for their retirement. As such, a strengthening of the ‘multi-pillar’ pension system is in-line with international best practice as recommended by organisations such as the OECD, World Bank & International Labour Organisation. This approach is complementary to other sources of pension income; reduces sustainability risk; and improves total retirement income. Furthermore, from the view of the public finances, a strengthening of the supplementary pension pillars provides a larger taxable income stream at the decumulation phase, which in turn can help meet the cost of ageing as demographics trends deteriorate.

From the perspective of the Department of Finance, the Interdepartmental Pensions Reform and Taxation Group (IDPRTG) reviewed areas of the Government’s Roadmap for Pensions Reform 2018-2023.<sup>20</sup> The IDPRTG Report, published in 2020, makes a number of practical, focussed recommendations on reform and simplification of the existing supplementary pension’s landscape. These include the phasing-out of certain products and the enhancement of others. This work represents a significant building block for a piece of long-term structural reform in the area of supplementary pension provision. It is also of note that the current Programme for Government separately reaffirms the commitment to introduce a pension automatic enrolment system.

These complementary initiatives should help expand pension coverage; enhance market competitiveness; drive product efficiencies and in turn lead to better retirement outcomes for pension savers. An increased focus on policy development within the supplementary pension landscape has the potential to play an important role in helping to alleviate the expected significant pressures of demographic change on public expenditure.

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<sup>19</sup> CSO Pensions Survey, *Pension Coverage 2020*.

<sup>20</sup> Available at: <https://www.gov.ie/en/publication/98d7f-report-of-the-interdepartmental-pensions-reform-and-taxation-group/>

## Section 5: Policy scenarios – changes in the State Pension Age

The Department of Finance's pension expenditure model allows a number of different scenarios regarding the State Pension Age (SPA) to be run. This section will highlight two such scenarios, linked to policy considerations.

### 5.1: Impact of restoring the previously legislated increases in the SPA

Up until late 2020, and the passing of the Social Welfare Bill 2020, the SPA was legislated to increase to 67 in 2021 and 68 in 2028. The Department of Finance has undertaken analysis on the projected long-term cost of this change in legislation, based on the SPA remaining at 66 years of age for the projection period.

Table 3 below outlines the difference from the baseline scenario, which assumes the SPA remains at 66, and a scenario in which the SPA increases as previously legislated for. As can be seen, the model suggests keeping the SPA unchanged will result in significant increases in annual expenditure on pensions. While the choice of discount rate is important, the estimated cumulative cost of this policy decision is projected to amount to €50 billion by 2070.<sup>21</sup>

**Table 3: pension expenditure projections, per cent of GNI\***

	2019	2030	2040	2050	2060	2070
Constant SPA	7.4	9.6	11.2	12.1	12.2	12.3
Previously legislated increases in SPA	7.4	9.0	10.5	11.3	11.4	11.5
<b>Difference</b>	<b>0.0</b>	<b>0.6</b>	<b>0.7</b>	<b>0.8</b>	<b>0.8</b>	<b>0.9</b>

Rounding may affect totals. Source: Department of Finance.

When analysed in tandem with the no-policy change scenario in the previous section, the choice to keep the SPA at 66 accounts for nearly 20 percentage points of the increase in the debt-to-GNI\* ratio of 86 percentage points to 182 per cent of GNI\*.

### 5.2: Impact of linking the SPA to life expectancy

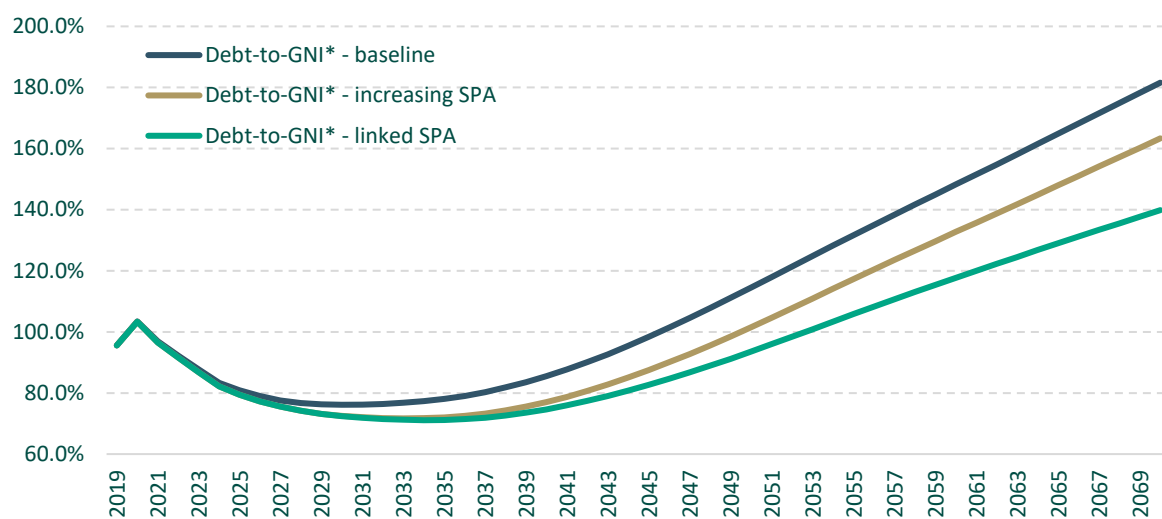
A further policy scenario analysed by the Department of Finance involves linking the SPA to increases in life expectancy. Considering that an increase of one year in life expectancy may not result in one additional healthy year of life, this framework assumes that for every additional year in life expectancy, the SPA increases by  $\frac{3}{4}$  of a year.<sup>22</sup> As can be seen in figure 8, under this scenario, the debt-to-GNI\* is projected to grow at a much lower rate, eventually finishing at more than 40 percentage points of GNI\* lower than the projected ratio under the scenario keeping the SPA at 66.

<sup>21</sup> Assuming discount rate of 4 per cent per annum.

<sup>22</sup> This scenario assumes the SPA increases in 2021 and 2028 as previously legislated for and is linked to life expectancy from 2029.



**Figure 8: evolution of debt ratio of different policy scenarios, per cent of GNI\***



Source: Department of Finance.

## Section 6: Conclusion

It is indisputable that, firstly, people are living longer and, secondly, the population is ageing. Indeed, the **demographic profile of the Irish population is set to change significantly** in the coming decades, as Ireland transitions from having one of the youngest populations in the EU towards one characterised by a similar population structure.

From an economic and fiscal perspective, this creates two issues. Firstly, as the pace of growth of the working age population slows, the **rate of economic growth will moderate**, as additional labour supply becomes more scarce. Fiscal revenues will, accordingly, evolve at a slower rate.

Secondly, this 'greying' of the population will put **significant upward pressure on demographically-sensitive public expenditure**, with increases of approximately 8 percentage points of GNI\* in prospect by the mid-part of this century.

In summary, both the revenue and expenditure side of the fiscal accounts will be adversely affected.

**Structural changes are, therefore, absolutely necessary to meet the fiscal costs associated with population ageing**; without these, it is possible that the debt ratio will move onto an unsustainable path.

The most **important reform involves better aligning the State Pension Age with increased life-expectancy**.

In addition, the Covid-19 pandemic has seen public indebtedness increase significantly over the past year. While the exact impact of the pandemic on the public finances is beyond the scope of this submission, **it is clear the pandemic has worsened the starting position**.

Ireland is fortunate to have the opportunity to undertake the necessary policy changes to ensure the sustainability of the public pension system before the budgetary implications of population ageing begin to impact. That said, the **window of opportunity is rapidly closing and any delay in implementing the necessary policy interventions will inevitably raise the cost** of the ageing of the population.



**Tithe an Rialtas, Sráid Mhuirfean Uacht,  
Baile Átha Cliath 2, D02 R583, Éire**  
Government Buildings, Upper Merrion Street,  
Dublin 2, D02 R583, Ireland

T:+353 1 676 7571  
@IRLDeptFinance  
[www.gov.ie/finance](http://www.gov.ie/finance)