Executive summary

This review provides a detailed analysis of the different components of the Portuguese pension system, which consists of an old-age safety net, a pay-as-you-go earnings-related public scheme and voluntary private pensions. It assesses the system according to the OECD best practices and guidelines, and draws on international experiences to make recommendations for improvement. It also addresses the effects of recent labour market trends on future retirement benefits and on the pension coverage of workers in non-standard forms of employment.

Portugal is ageing rapidly. The projected decrease of the working-age population until 2050 will be among the largest in the OECD, leading to a substantial fall in the number of contributors to the pension system. Retirement finances will be put under stress as a result. Old-age inequality is high in Portugal but thanks to safety-net provisions, the relative old-age poverty rate is below the OECD average. The labour market has been recovering from the deep and prolonged crisis of 2008-09 in Portugal and employment rates are now close to the OECD average. Yet, for those who were affected the crisis is likely to leave its mark on future pensions. The main recommendations are presented below.

- *Simplify non-contributory benefits to avoid the multiplication of instruments with similar objectives. In particular, merge the old-age social pension, the complement (CES) and the top-up (CSI), and remove the CSI's means testing to descendants' income*. The interaction between numerous non-contributory schemes pursuing similar objectives is unduly complex. Means-testing the CSI not only at the household level but also including descendants' income might cut cost by restricting the number of beneficiaries but makes the pension system complicated. The administrative complexity generates costs and long waiting times, and some people may be discouraged or uncomfortable to have their children's income means-tested.

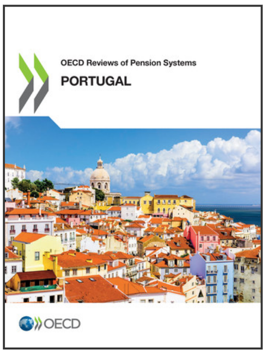
- *Lower the minimum contribution period of 15 years required for the minimum pension, adjust the benefit level accordingly and ensure that each additional year of contribution results in a higher minimum pension benefit*. For those currently entering the labour market there are three levels of minimum pensions available: one for those with 15-20 years of contributions, one for those with 21-30 years of contributions and one for those with 31 years of contributions or more. In Portugal, the minimum pension provides little additional benefit from working longer. Only those with contributory periods just below the thresholds of 15, 21 and 31 years benefit from working longer in terms of the minimum pension.

- *Separate the uprating of the initial minimum pension benefit at retirement from the indexation of minimum pensions in payment*. The uprating of the initial benefit should be closely related to average- or minimum-wage growth to ensure a stable level relative to labour income over time.

- *Duly implement the link between increases in the retirement age and life expectancy gains, and extend that link to the minimum age of early retirement*. The link between the retirement age and life expectancy plays a key role in dealing with challenges raised by population ageing. It should be extended to the minimum age of early retirement, which at 60 years is currently too low.
- *Use the sustainability factor to adjust pension benefits across the board as an ultimate instrument to ensure financial sustainability*. Abolishing the sustainability factor only for retirement at or after the normal retirement age created very large pension penalties for those retiring before the normal retirement age. These differences will grow with life expectancy gains. Once the sustainability factor has been reshaped early retirement could rather be discouraged by raising the current 0.5% penalty per month of early retirement.
- *Eliminate the option for long-term unemployed people to enter retirement very early and without the full penalties applied to other early-retirement entries*. Ensure effective support for active job-search efforts of older workers in particular. Policy measures should ensure that unemployment schemes do not encourage early retirement. Rather than permitting older long-term unemployed to enter retirement very early with lower penalties, the unemployment benefit system should be adapted to offer good protection against unemployment while providing effective active labour market programmes to strengthen job-search efforts and employability before the retirement age.
- *In the benefit calculation, uprate past wages with wage growth rather than a combination of price inflation and wage growth while lowering accrual rates*. For benefit calculation, uprating past wages based mostly on prices makes the financial balances of the pension system and pension replacement rates highly dependent on real-wage growth. This is undesirable because productivity developments are difficult to predict and difficult to influence by policies. With the same objective in terms of financial balances and pension levels, it is preferable to shift to wage uprating and lower accrual rates accordingly – which are currently very high.
- *Index intermediate pensions at least with prices and use lower accrual rates in the contribution phase to finance this more generous indexation*. Medium pension levels (between two and three times the IAS) are currently indexed below prices (inflation minus 0.5 percentage point) when annual real GDP growth is smaller than 2%. Indexation below prices erodes standards of living during retirement and jeopardises pension adequacy.
- *Increase coverage by improving incentives to contribute to voluntary pension schemes and promoting occupational plans*. Increasing incentives could be achieved by: removing the complexity of the pension tax system by applying one set of tax rules to all schemes and contributions; and, introducing non-tax financial incentives (such as fixed nominal subsidies or matching contributions). The government could also promote occupational plans as an effective way to increase coverage.
- *Improve withdrawal settings*. The conditions currently permitting early withdrawals from Retirement Savings Plans (PPRs) are relatively lenient. The government could tighten these conditions and align retirement age rules with the

statutory retirement ages. It could also discourage taking sizeable retirement savings as lump sums.

- *Improve regulation*. The Portuguese government should consider updating the assumptions around the minimum funding ratio calculation and develop Portuguese mortality tables for use in funds' independent funding ratio calculation.



From:

OECD Reviews of Pension Systems: Portugal

Access the complete publication at:

https://doi.org/10.1787/9789264313736-en

Please cite this chapter as:

OECD (2019), “Executive summary”, in *OECD Reviews of Pension Systems: Portugal*, OECD Publishing, Paris.

DOI: https://doi.org/10.1787/eea8cd69-en