FOCUS · **Tensions in Social Security**

For the past eight years, Spain's Social Security has been in the red. From 2010 to 2016 its budget deficit was financed via the Social Security Reserve Fund, created from budget surpluses in previous years. However, in 2017, with the Social Security Reserve Fund running out, the State Treasury granted a loan to Social Security to finance its budget deficit, something which is also expected to happen this year and which highlights the existence of a structural problem in Social Security funding.

The following data illustrate the problem: while revenue from Social Security contributions, highly sensitive to the economic cycle (and especially employment trends), has risen by just 1.8% compared with 2009, retirement pension expenditure is now 54% higher than in 2009. What is this marked rise in spending on retirement pensions due to?

First, it is due to the rise in the average pension, much more than the rise in the average wage and, to a lesser extent, to the increase in the number of pensioners, boosted by the constant lengthening of life expectancy and increase in early retirement, mainly during the crisis. Regarding the first factor, the average pension received by recent retirees has gradually risen, reaching 70% of the average wage[1] compared with the 60% recorded in 2008. This is currently one of the highest percentages in Europe. However, the reforms carried out in 2011 and 2013, and in particular the Pension Revaluation Index,[2] are likely to contain increases in the average pension during the next few years. On the other hand, the increase in the number of pensioners and consequent rise in the dependency ratio,[3] which has grown by more than 5 pp in the past 10 years to 29%, will continue to push up pension expenditure over the coming years.[4]
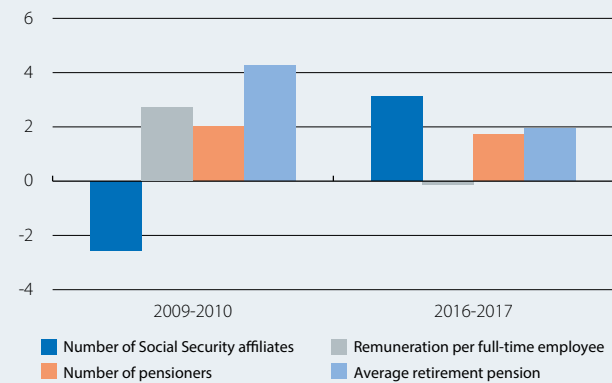
Given this situation, it is vitally important to combine forces and define a new intergenerational social pact. Given the notable increase in life expectancy, as well as in the quality of life for older people, a large part of the debate is focusing on the search for measures aimed at making the pension system more compatible with work

beyond the current retirement age, at least for those people who wish to do so. The impact of such measures on the Social Security accounts would be twofold, as it would boost revenue but also reduce pressure on expenditure.

In this respect, one notable proposal is by Domínguez-Fabián, del Olmo and Herce (2017),[5] of a «two-stage» mixed pension system. The first stage would cover the period from the statutory retirement age up to an age set by Social Security in line with life expectancy and quality of life (called the «grand age» by the authors). During this stage, the income received would come from a pension insurance policy. In the second stage, after this «grand age», there would be a state pension system. However, this proposal aimed at ensuring the system is sustainable fails to clarify, among other questions, how this «grand age» should be defined, an issue which is not inconsequential. Neither does it explain how the current system can be transformed into the new one. Nevertheless, given such a huge problem, any debate and search for solutions are more than welcome.

Key determining factors of the Social Security budget balance
Year-on-year growth (%)

- Number of Social Security affiliates
- Number of pensioners
- Remuneration per full-time employee
- Average retirement pension

Source: CaixaBank Research, based on data from the Ministry of Employment and Social Security.

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1. Data refer to 2016. The average pension is currently EUR 1,070 per month (November 2017). Under some special regimes, such as that for the coal industry, the average pension rises to EUR 2,075 per month, 80% of the average wage of the mining industry employment group, namely EUR 2,612 per month. Data based on the Salary Structure Survey.
2. The revaluation factor pegs the annual increase in pensions to the expected medium-term trend for the Social Security deficit.
3. The dependency ratio is defined as the ratio between the population aged over 64 and the working age population (from 16 to 64).
4. In this respect, the sustainability factor, which modifies the initial pension according to life expectancy, will help to offset the increase in the number of pensions.

5. Domínguez-Fabián, I., del Olmo, F. and Herce, J. A. (2017). «Reinventando la Seguridad Social. Hacia un sistema mixto de pensiones "por etapas"», IAES, Documento de Trabajo 06/17.