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EXPERT NOTE

«Problems of Rising Retirement Age in Ukraine»

Introduction

The reasons necessitating the increase in the retirement age in Ukraine are the following: 1) negative demographic trends; 2) economic situation, condition of the budget finances, solvency of the Pension Fund. The reasons and methods to resolve those problems have been similar in many countries, differing only in their specifics.

Statutory retirement age in Ukraine, 55 for women and 60 for men, is lower than in other European countries. It means:

- **decrease** of the national income compared to the potential income;
- **decrease of the GDP share** belonging to the working population;
- **low** level of pensions, in spite of high deductions and the constantly growing **burden** on the working population, as well as **reduction** of their net wages. This serves as a significant incentive for **migration abroad** for those who have such opportunities;
- constantly growing **subsidies** from the State Budget of Ukraine to the Pension Fund of Ukraine. Increased subsidies to the Pension Fund mean reduction of funds available for other public needs: health protection, road construction and maintenance, education, security, legal protection;
- **increase** of deductions and taxes to finance the budget.

The increase in the retirement age would mean:

- a higher national income;
- lower deductions and, consequently, a stronger incentive to work in Ukraine;
- lower subsidies from the budget — more budget money for other purposes, or lower taxes.

The rising retirement age will not have any negative consequences for persons who have already retired, but, contrary, it will produce a positive effect on funding of pensions at present and in the future. Rising retirement age will have immediate positive effects on public finances. It is rather important in current struggle against the consequences of the financial crisis. The number of new pensioners could be cut even by half during next couple of years, whereas number of contributors to pension funds would increase as well as Pension Fund revenues.

Rising Retirement Age in other countries

Negative demographic developments are observed in many countries of the world, and Ukraine is not an exception in this respect. It is the growing numbers of pensioners, along with the decrease in number of working population, have been the reason for the increase in the **retirement age** in many countries (Annex 1). The retirement age was increased in Hungary from 55 years for women and 60 years for men, to 63 years; in Greece – from 58 to 65 years; in Denmark – to 67 years; in Portugal — to 65 years, in the USA — from 65 to 67 years; in Japan — to 65 years; in Turkey — to 65 years (Annex 2)¹.

¹ OECD Data

Demographic Forecast for Ukraine until 2050

Forecasts of the demographic situation until the year 2050 demonstrate that the number of people **in active working age**, that is, 18 to 59 years, **will decrease by 44%**, and the number of persons older than **60 will grow up by 27%** (Annex 3). It is obvious that the burden of pensioners (those receiving social benefits) on the working population who make social deductions will grow. As of today, it equals **1:0.98**, and in **2050** it will reach **1:1.39** (Annex 4). This means that in the future one working persons will have to earn their own labour compensation, pension of one pensioner and almost 40% of another pensioner's pension. This will entail either an increase of social deductions, which in its turn will reduce the net wages of the working generation, or reduction of pensions, which are not very high as they are.

Life Expectancy at Birth or at the Time of Retirement?

Life expectancy **at birth** in Ukraine, 62 for men and 73 for women, is not very high. This is used as argument against reform of the retirement age. This argument, however, is not adequate for assessment of the retirement age reform. One should consider here life expectancy **at the time of retirement**, since this is what shows the duration of pension period. Thus, life expectancy for Ukrainian **women at the age of 55 is 25 years, which is more than in many other countries of the world** (the UK – 23 years, Italy – 24.9, Germany— 20.9, Poland – 22, Slovakia - 18, the USA — 17.7, Hungary - 20, France — 26, the Czech Republic — 19.2, Sweden – 20, Japan - 23). **That means that women in Ukraine work for a shorter period of time than women in other countries, and stay on pension longer** (Annex 5). Life expectancy for men at the age of **60 is 14 years** (the UK – 15.7 years, Italy — 16.9, Germany- 16.8, Poland – 14, Slovakia - 15, the USA — 15.2, Hungary - 16, France - 20, the Czech Republic — 15.9, Sweden – 17.4).

Comparison of Periods on Pension and Periods of Labor Activity

The ratio of pension period to the labor activity period in Ukraine is **3.5** years for each 10 years of work **for men** (in the UK – 3.5, Hungary - 3.8, Germany – 3.7, Italy - 3.8, Poland - 3.1, Slovakia – 3.6, the USA – 3.2, the Czech Republic – 3.7, Sweden – 3.9, Japan - 4), and **for women - 7.1 years for each 10 years of work, which is more than in any other country** (in the UK – 5.8, Hungary - 4.9, Germany – 4.6, Italy - 6.2, Poland - 5.5, Slovakia – 4.3, the USA – 3.8, the Czech Republic – 4.5, Sweden – 4.4, Japan – 5.1) (Annex 6).

The Number of Women Aged 55 to 60

Life expectancy at the age of **60** years for the Ukrainian women is **19** years, which is comparable to the same value in other countries. Therefore, all demographic arguments confirm the idea about the necessity to rise the retirement age for the Ukrainian women. By the population structure in 2007, the number of women aged **55 to 60 accounted to 1.7 million**, which makes up **13%** of the total number of old-age pensioners in 2007 (Annex 7). This equals at least UAH **12 billion** in the expenditure part of the Ukrainian Pension Fund in 2007 (in the expenditures of the Pension Fund in 2008 that amount would reach at least UAH 19 billion). The budget deficit could be

reduced or budget subsidies to the Pension Fund could be channelled to other purposes, or taxes could be reduced by that amount.

Pension Deductions in Ukraine and in other countries

In Ukraine, pension deductions have reached 31 to 34% over the recent years, which greatly exceeds the level of deductions in other European countries (in Hungary - 26.5, France - 24%, the Czech Republic - 28%, Sweden - 18.9%) (Annex 8). Even deductions so high, however, are insufficient to cover pension expenditures, and for that reason the State Budget allocations to the Pension Fund of Ukraine have constantly grown every year. At the same time, the Ukrainian Pension Fund budget does not ensure sufficiently high pensions, and that is why a large share of the population continues to work even after retirement, in order to increase their household incomes. Taking into account negative trends in the economy of the country (decrease of GDP, unemployment), deficits in the Pension Fund of Ukraine and the State Budget will continue to grow, and problems with the pension provision will aggravate.

Significance of Duration of Contribution Time under the Accumulating Account Pension System (Defined Financial Contributions)

A new pension system is planned to be introduced in Ukraine, in which size of pension will depend on contributions accumulated on individual pension accounts. Without an increase of the retirement age, however, the new pension system will not function properly, since workers will not be able to save, over their active employment period, an amount sufficient for at least a minimal pension. This is especially noticeable for women who live on pension for many years compared to the period at work. In that situation, incentives to increase contributions to individual pension account would not work, because pension level will in any case be still lower than guaranteed minimum. In order to secure minimal pension, budget subsidy would be necessary. This should not happen. Under the financial defined contributions, the minimal guaranteed pension is envisaged for exceptional cases, when the size of savings is too small to provide for the pension at the minimal guaranteed level. Providing of the minimal pension must be an exception rather than the rule. **Lack of incentives to save more** would neutralize the advantages of the new reformed system for many of its participants.

Gradual Retirement Age Increase for Women in Ukraine

Therefore, **the** parametric measure of the reform – **rising retirement age** (at least for women) — is the simplest and justified way to resolve the problem of pension provision now. We recommend to rise the retirement age **gradually** – adding 1 year to the retirement age every second year. For example, in 2012, women born in 1956 will retire at the age of 56; in 2014 – women born in 1957 at the age of 57, and so on; in 2020 - women born in 1960 will retire at the age of 60 (Annex 9).

Consequences of Population Aging and Retirement Age Decrease

Duration of Pension Periods in the OECD Countries (average)

1970

- Men – 11 years
- Women - 14 years

2004

- Men -18 years
- Women - 23 years



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Raising Retirement Age in Some OECD Countries *

Country	Raising Retirement Age
Hungary	Gradual, from 55 for women and 60 for men to 63 years
Greece	From 58 to 65 years
Denmark	Gradual, from 65 to 67 years
Portugal	To 65 years
Slovakia	To 62 years
USA	From 65 to 67 years
Turkey	To 65 years
Japan	From 60 to 65 years

* OECD Data

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Demographic Forecast for Ukraine Until 2050*

- Reduction of population aged 18 to 59:

2007 - 28.5 million persons

2050 – 16.1 million persons

-44%



- Increase of population older than 60

2007 - 9.5 million persons

2050 – 12.0 million persons

+27%



*According to data by the NASU Institute of Demography and Social Studies, 2007

Forecast for Systemic Dependency Ratio in 2050

1.39 : 1

- Ratio between pensioners and payers of social contributions*
- Structure of working person wage
 - ✓ remuneration his/her labour
 - ✓ contribution for pension of the 1st pensioner
 - ✓ contribution for 39% of pension of the 2nd pensioner

* Includes all types of pensions

Life Expectancy At Official Retirement Age

Countries	Retirement Age		Life Expectancy	
	Men	Women	Men	Women
UK	65	60	15.7	23
Hungary	62	61	16	20
Germany	65	65	16.8	20.9
Italy	65	60	16.9	24.9
Poland	65	60	14	22
Slovakia	62	62	15	18
USA	67	67	15.2	17.7
Ukraine	60	55	14/12**	25/19*/16**
France	60	60	20	26
Czech Rep.	63	63	15.9	19.2
Sweden	65	65	17.4	20
Japan	65	65	18.2	23

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* - Life expectancy at the age of 60, ** - Life expectancy at the age of 65.

Ratio of Labor Activity to Period on Pension

Countries	Start of Labor Activities, years	Retirement Age		Labor Activity in years		Period on Pension in years		Number of years on pension as ratio to 10 years of labor activity	
		M	F	M	F	M	F	M	F
UK	20	65	60	45	40	15.7	23	3.5	5.8
Hungary	20	62	61	42	41	16	20	3.8	4.9
Germany	20	65	65	45	45	16.8	20.9	3.7	4.6
Italy	20	65	60	45	40	16.9	24.9	3.8	6.2
Poland	20	65	60	45	40	14	22	3.1	5.5
Slovakia	20	62	62	42	42	15	18	3.6	4.3
USA	20	67	67	47	47	15.2	17.7	3.2	3.8
Ukraine	20	60	55	40	35	14	25	3.5	7.1
France	20	60	60	40	40	20	26	5.0	6.5
Czech Rep.	20	63	63	43	43	15.9	19.2	3.7	4.5
Sweden	20	65	65	45	45	17.4	20	3.9	4.4
Japan	20	65	65	45	45	18.2	23	4.0	5.1

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Number of Pensioners in Various Groups Aged 55 to 65, 2007

Groups	Age, years	Number of persons in groups, million.
1	Women - 55-60	~ 1.7
2	Men – 60-65 Women - 55-60	~ 2.4
3	Men – 60-65 Women - 55-65	~ 3.5

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Size of Pension Contributions (employee + employer), %*

Country	1994	1999	2004
Hungary	30.5	30.0	26.5
Italy	28.3	32.7	32.7
USA	12.4	12.4	12.4
Turkey	20.0	20.0	20.0
Ukraine	33.6	33.0	33.0-34.0
France	21.5	24.0	24.0
Czech Rep.	26.9	26.0	28.0
Sweden	19.1	15.1	18.9
Japan	16.5	17.4	13.9

* OECD data

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Retirement Age Increase by 5 Years for Women

Year of Birth	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
1955	55										
1956			56								
1957					57						
1958							58				
1959									59		
1960											60