

# How can we defend Public Pensions

The role of public pensions in advancing the principles of Social Security enshrined in ILO Standards

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## ▶ Setting the Stage

- ▶ Public pensions are under scrutiny — demographic and fiscal pressures dominate the debate
- ▶ Defending public pensions is about more than numbers — it's about values and rights
- ▶ This presentation links ILO's social security principles with the role of public pensions in achieving social justice.

## ► Over a century of commitment

- Since 1919, the ILO has promoted the right to social security
- ILO Declaration of Philadelphia (1944) on the aim and purposes of the ILO: *“the extension of social security measures to provide a basic income to all in need of such protection and comprehensive medical care”*
- Social security is a fundamental human right (Universal Declaration, 1948)
- ILO Convention on Social Security (Minimum Standards) (1952)
- Social protection is part of the ILO’s Decent Work Agenda
- Last week: Second World Summit for Social Development

## ▶ ILO Social Security Standards as Guidance

- ▶ **Social Security (Minimum Standards) Convention, 1952 (No. 102)**: Sets minimum standards, adequacy and financing principles; requires periodical payments, corresponding to at least 40% of the reference wage. The rates of relevant benefits must be revised following substantial changes in the general level of earnings and /or the cost of living
- ▶ **Invalidity, Old-Age and Survivors' Benefits Convention, 1967 (No.128)**: Sets higher standards for invalidity, old-age & survivors' benefits, adequacy and financing principles; requires periodical payments, corresponding to at least 45% of the reference wage. The rates of relevant benefits must be revised following substantial changes in the general level of earnings and /or the cost of living
- ▶ **Social Protection Floors Recommendation, 2012 (No. 202)**: Complements C102 and C128, and ensures a basic income in old age

## 9 Principles enshrined in these ILO Standards



### Responsibility of the State

The State ensures delivery, administration, and sustainability



### Universality

Social security is a human right for all



### Social Solidarity and Solidarity in Financing

Shared responsibility and equitable contributions



### Predictability of Benefits Defined by Law

Benefits are guaranteed and formula-based



### Adequacy

Benefits must ensure dignity and sufficient income



### Non-discrimination

Equal treatment and gender-sensitive systems



### Transparency in management

Accountable and sound governance



### Financial, Fiscal and Economic Sustainability

With Due Regard to Social Justice and Equity:  
Long-term stability with fairness and solidarity



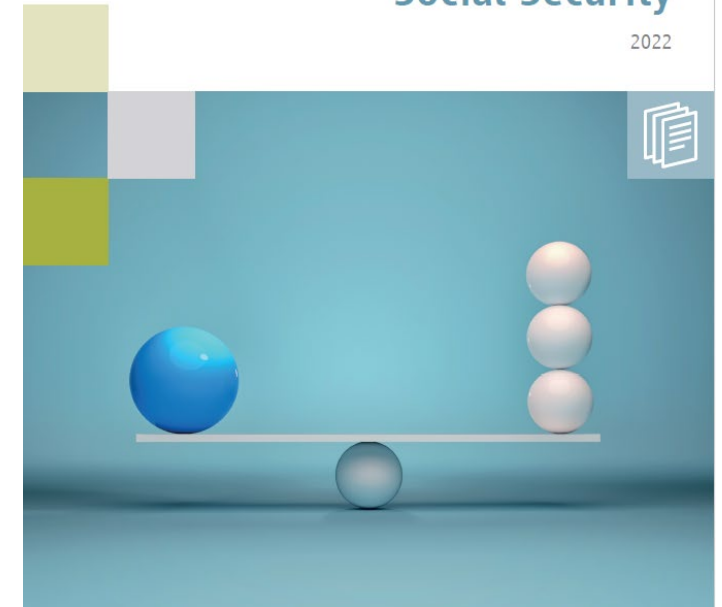
### Social Partners' Participation

Workers and employers engage in governance

Guidelines

## Actuarial Work for Social Security

2022



Guidelines on Actuarial Work for Social Security

**Guideline 42. Social security principles and minimum benchmarks established by ILO standards on social security**

## Cost of Old Age pension is a function of demographic and replacement ratios

Cost of Old-Age Pension in % of  
Insurable earnings  
Pay-As-You-Go (PAYG) rate

$$= \frac{\text{Total pension expenditure}}{\text{Total Insurable Earnings}}$$

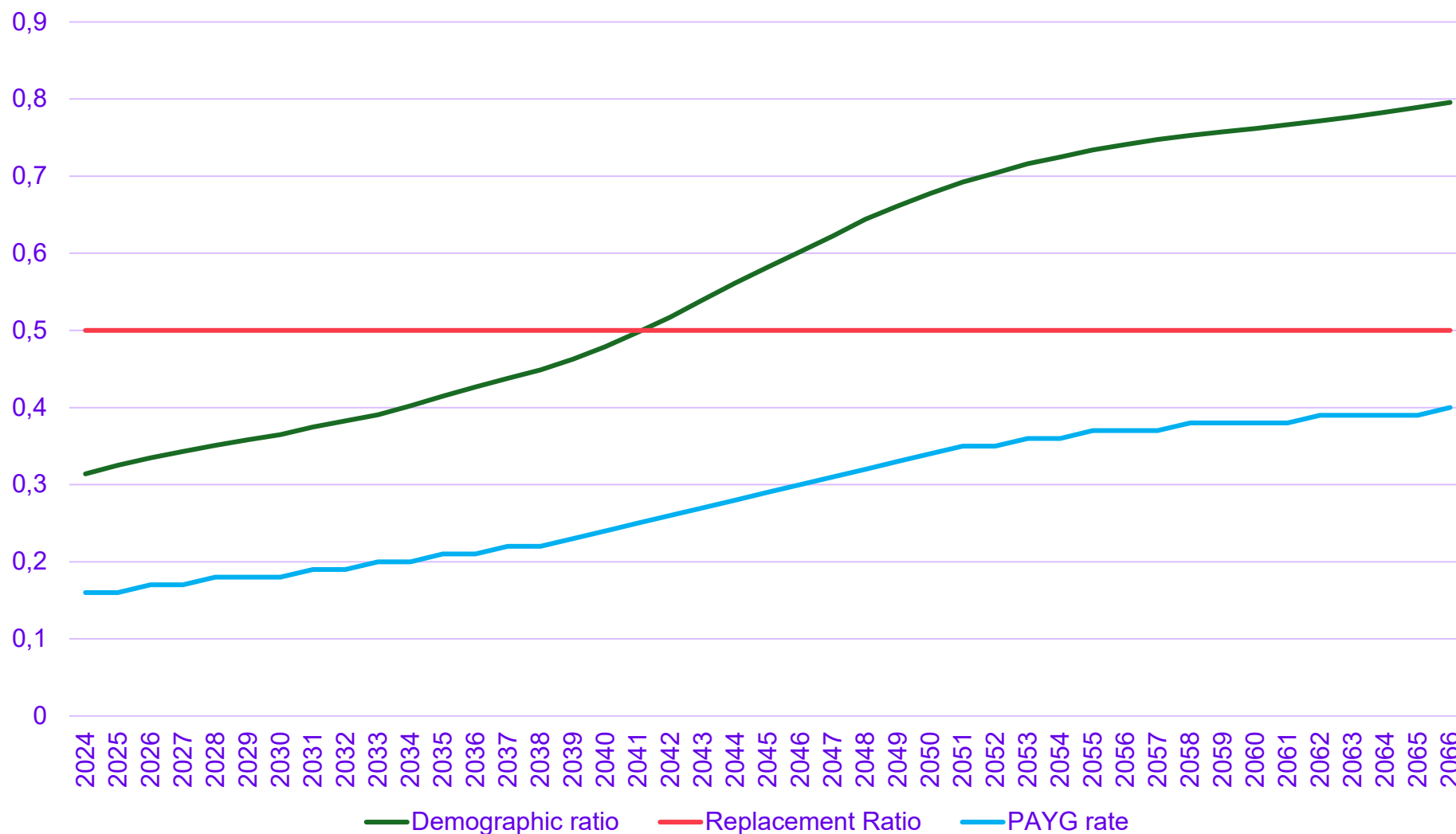
$$= \frac{\text{Nb Pensioners X Average Pension}}{\text{Nb Contributors X Average Insurable Earnings}}$$

$$= \frac{\text{Nb Pensioners}}{\text{Nb Contributors}} \times \frac{\text{Average Pension}}{\text{Average Insurable Earnings}}$$

$$= \text{Demographic Ratio} \times \text{Replacement Ratio}$$

# PAYG rate = Demographic ratio x Replacement ratio

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## 4 levers to reduce cost, i.e. the PAYG rate

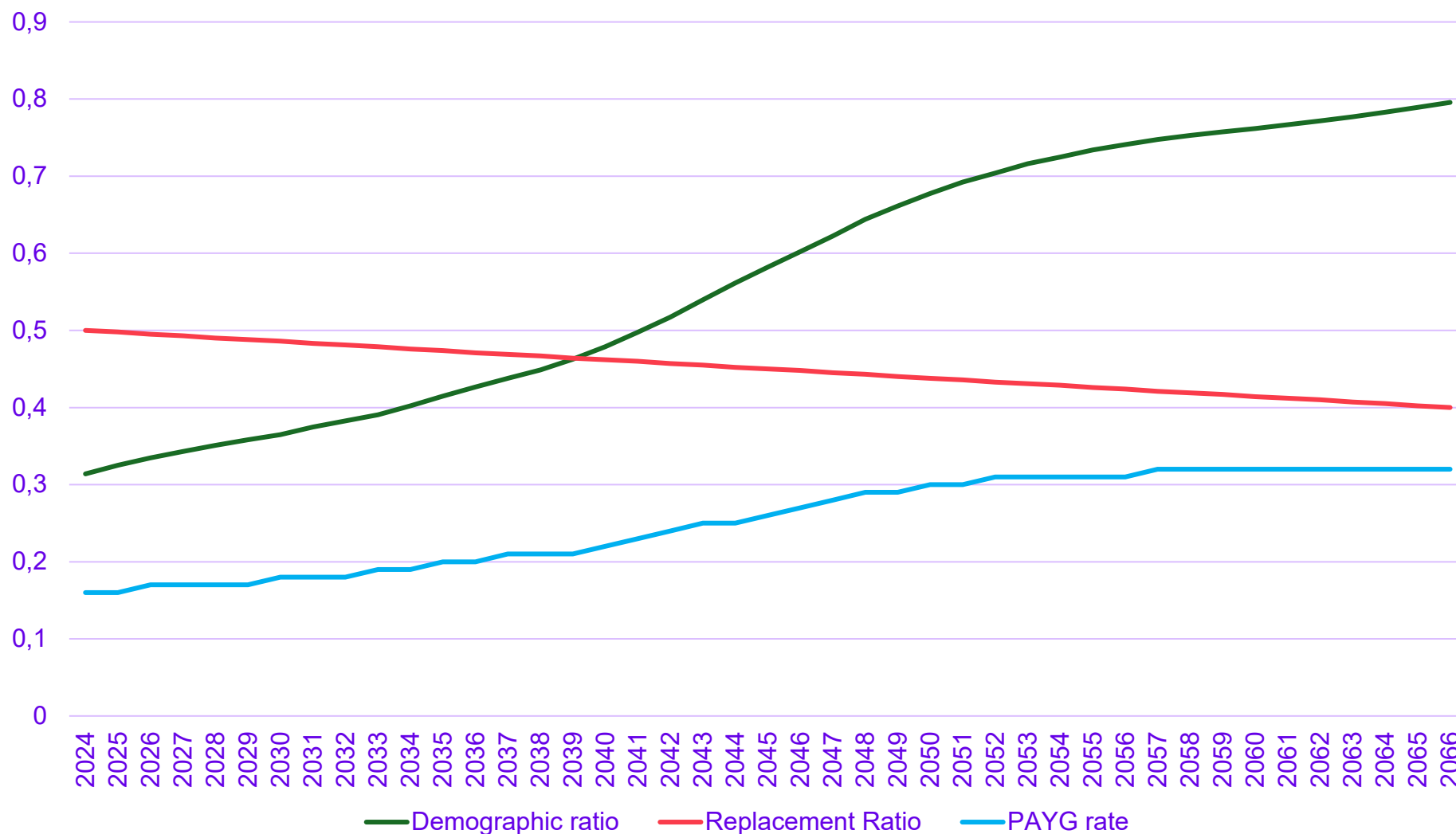
$$\begin{array}{ccc} \downarrow \text{Demographic Ratio} & \text{and/or} & \downarrow \text{Replacement Ratio} \\ \frac{\overset{1 \downarrow}{\text{Nb Pensioners}}}{\underset{2 \uparrow}{\text{Nb Contributors}}} & \times & \frac{\overset{3 \downarrow}{\text{Average Pension}}}{\underset{4 \uparrow}{\text{Average Insurable Earnings}}} \end{array}$$

- ▶ Increase retirement age: Will have an impact on both Number of pensioners and contributors
- ▶ Reduce accrual rates, reduce indexation (lower of inflation and wage index): Impact on average pension
- ▶ Increase coverage rate: Impact on number of contributors
- ▶ Real wage increase in line with economic growth: Impact on Average Insurable earnings

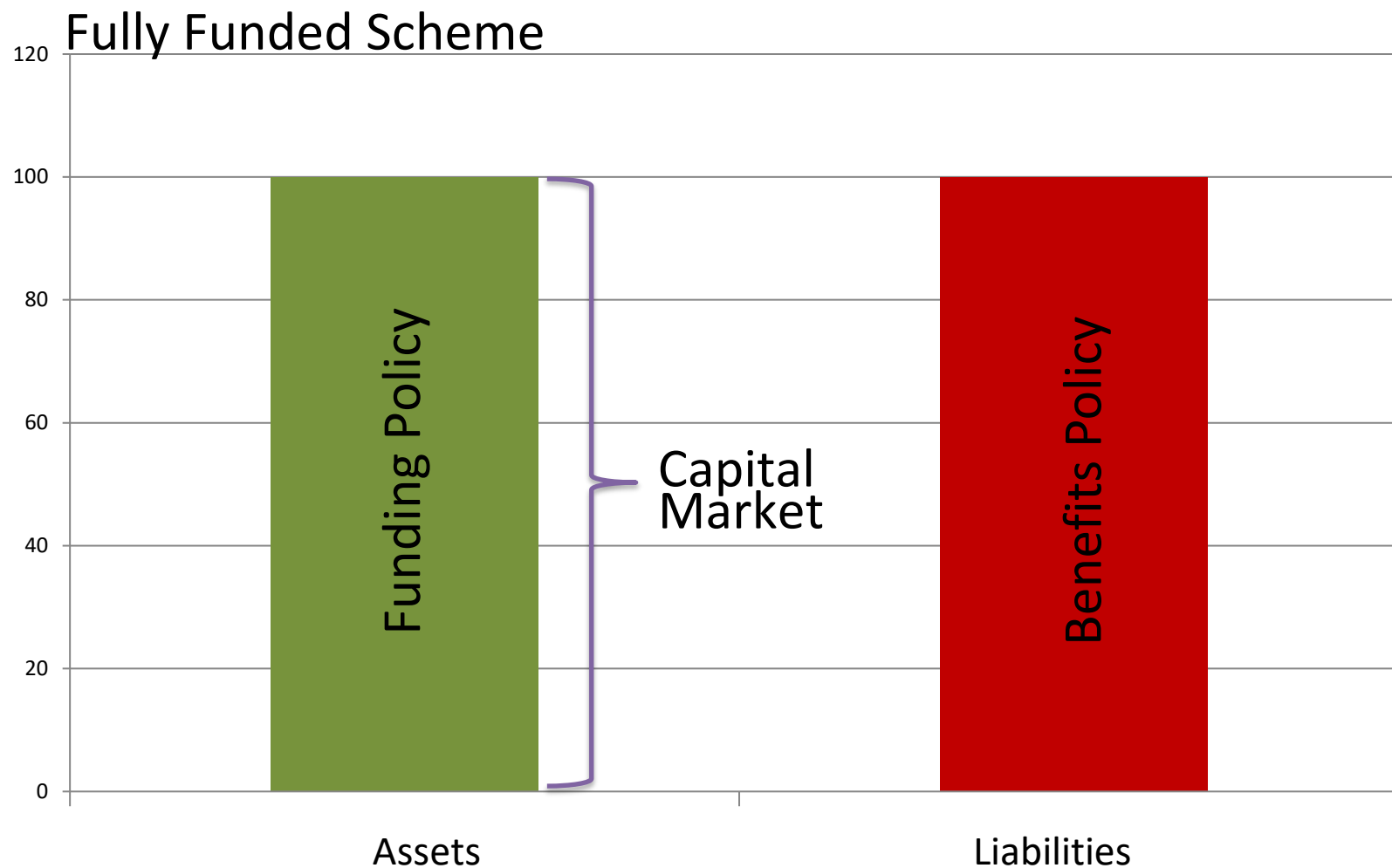


# PAYG rate = Demographic ratio x Replacement ratio

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# Financing of Pension Schemes



# Financing of Pension Schemes

## Sources of income from the Capital market



Equities



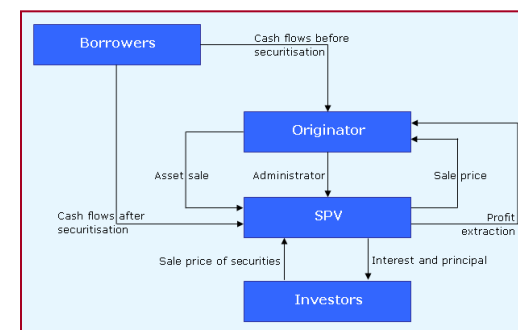
Bonds



Real estate

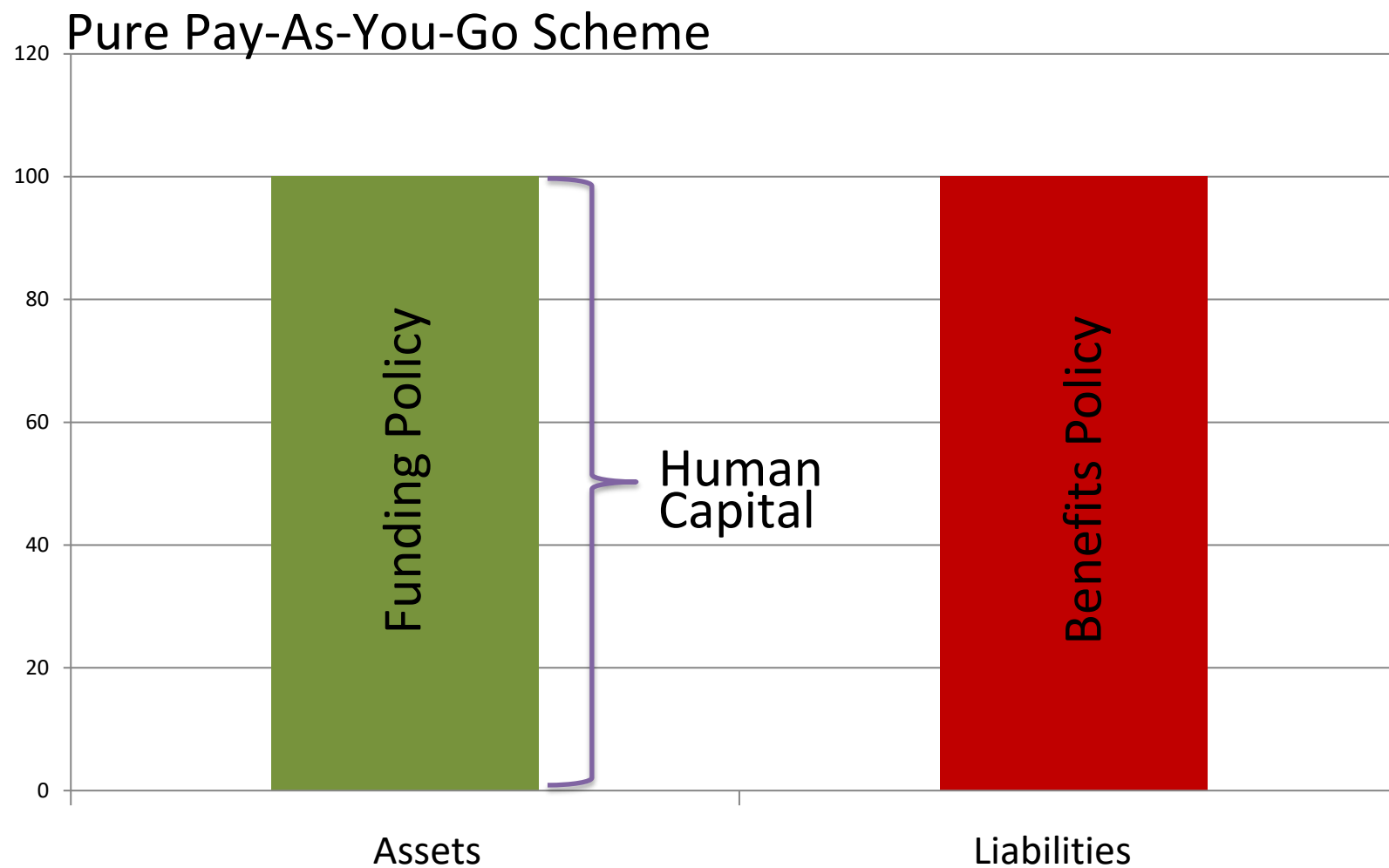


Non traditional investments



Complex products

# Financing of Pension Schemes

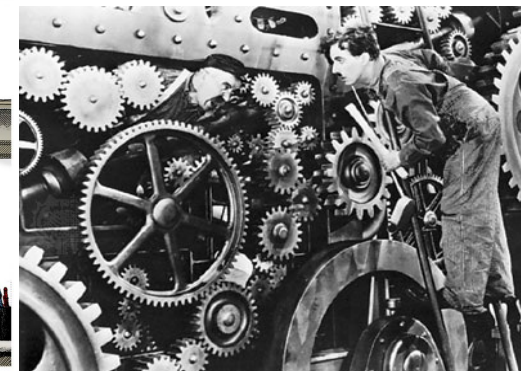
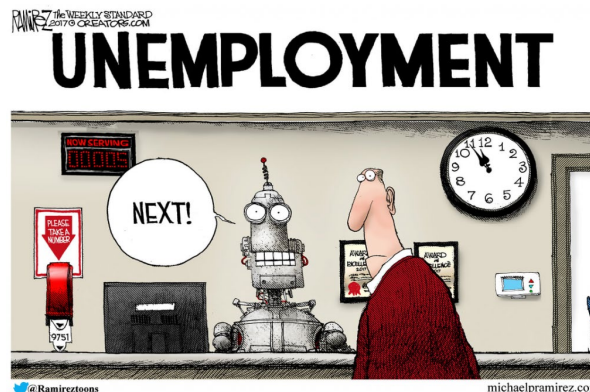


# Financing of Pension Schemes

## Sources of income from the Human Capital



Births



Number of workers

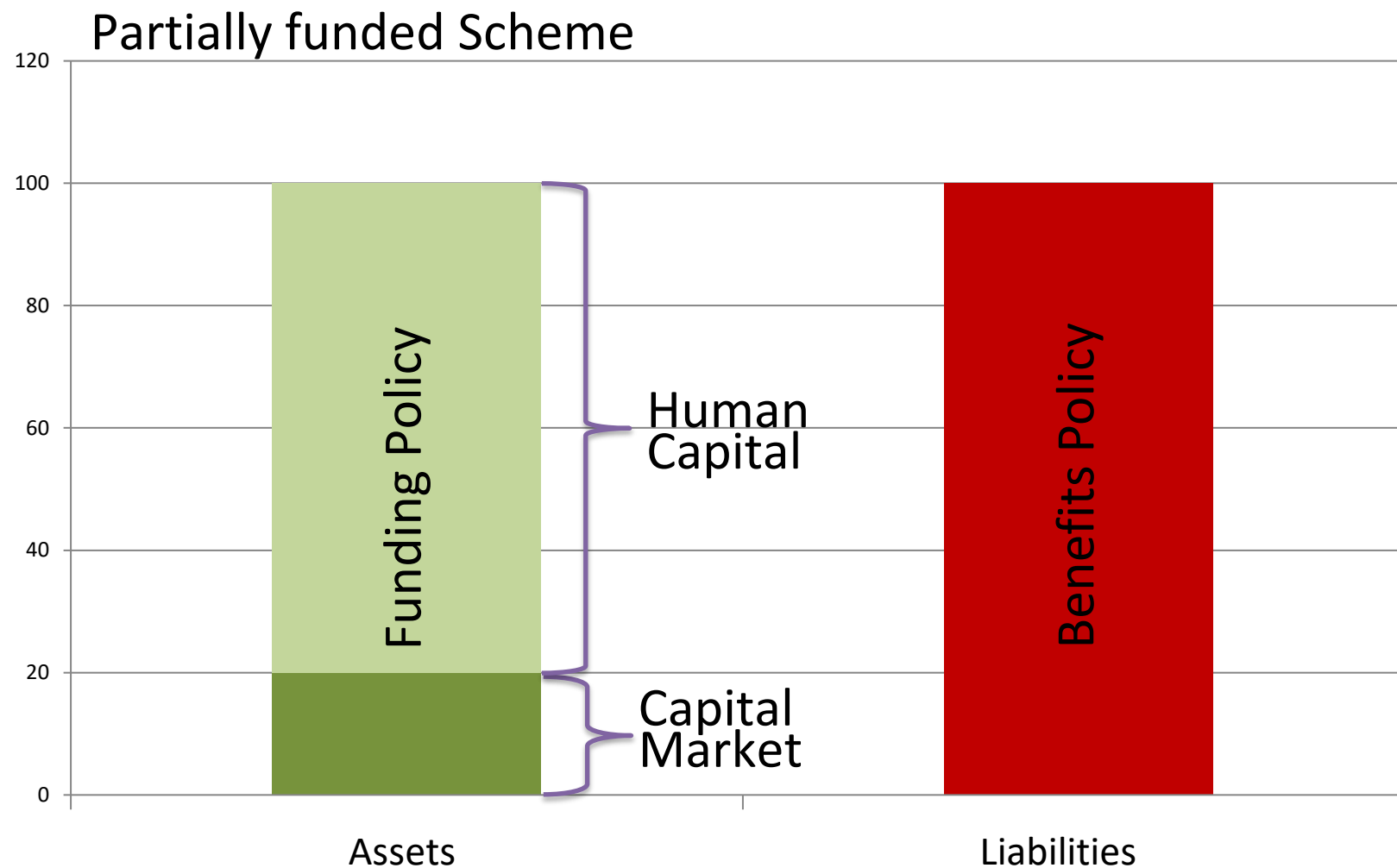


Migration



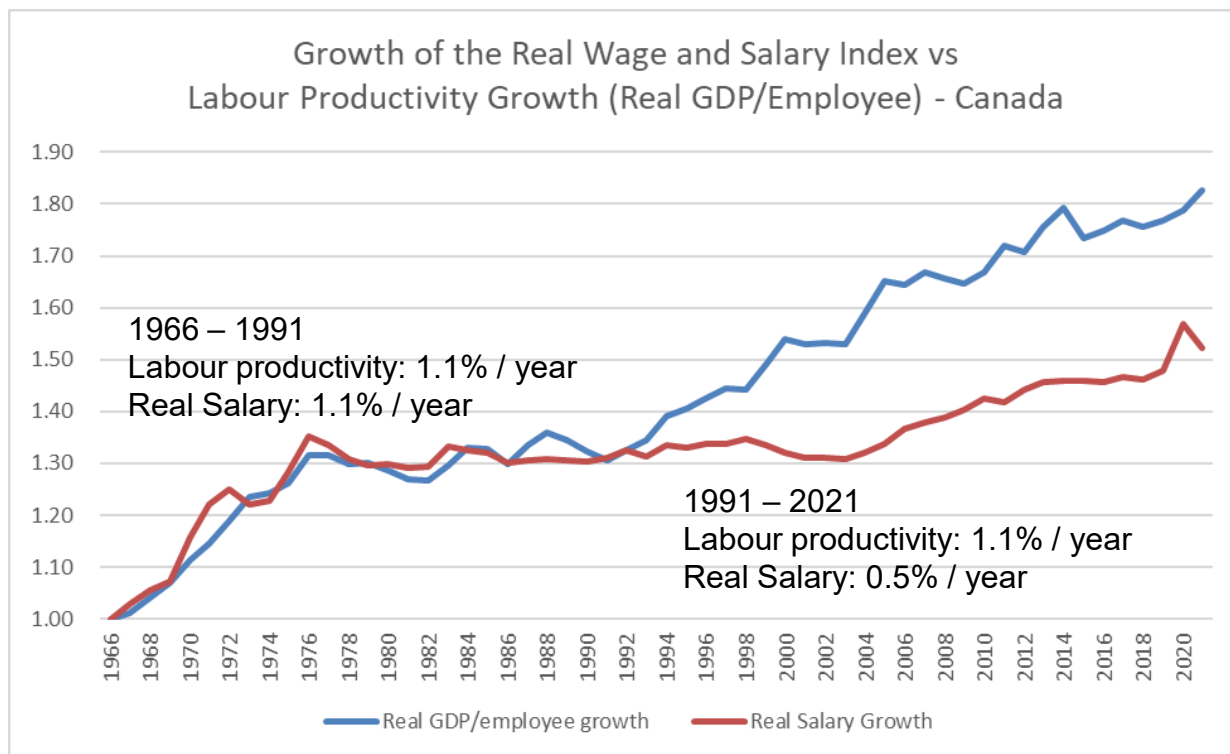
Productivity

# Financing of Pension Schemes

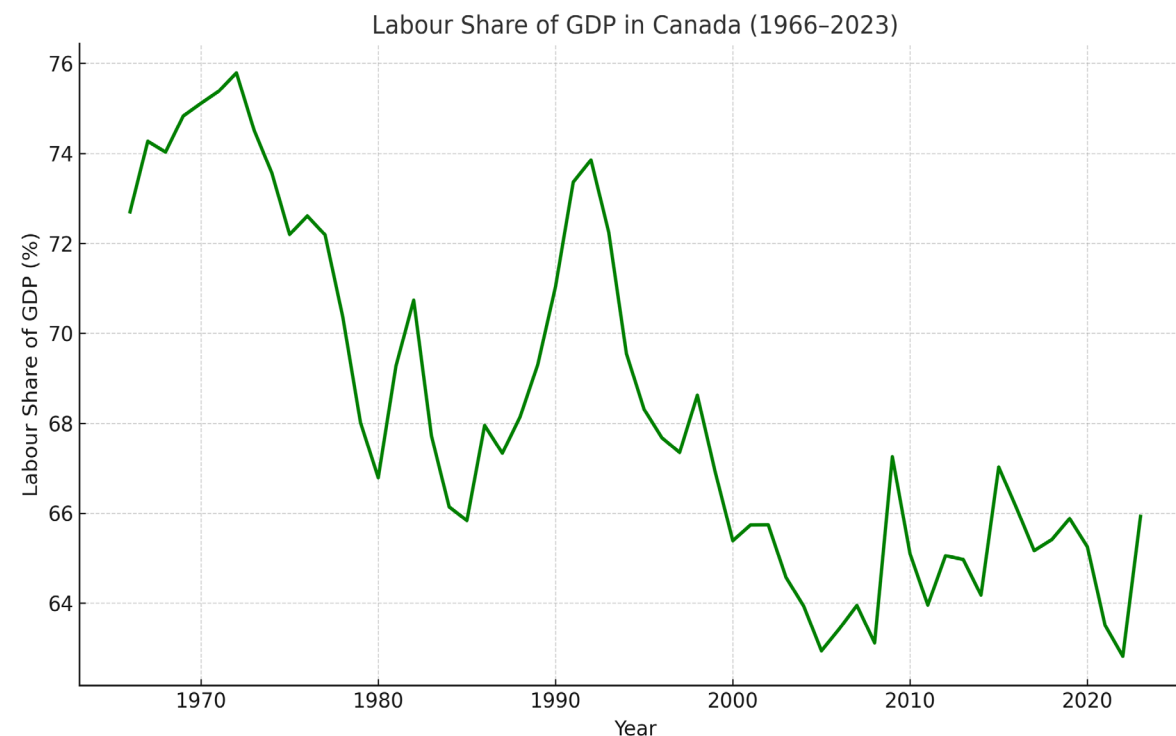


# 2 challenges for PAYG or Partially Funded schemes

## 1- Salary growth does not follow productivity growth anymore



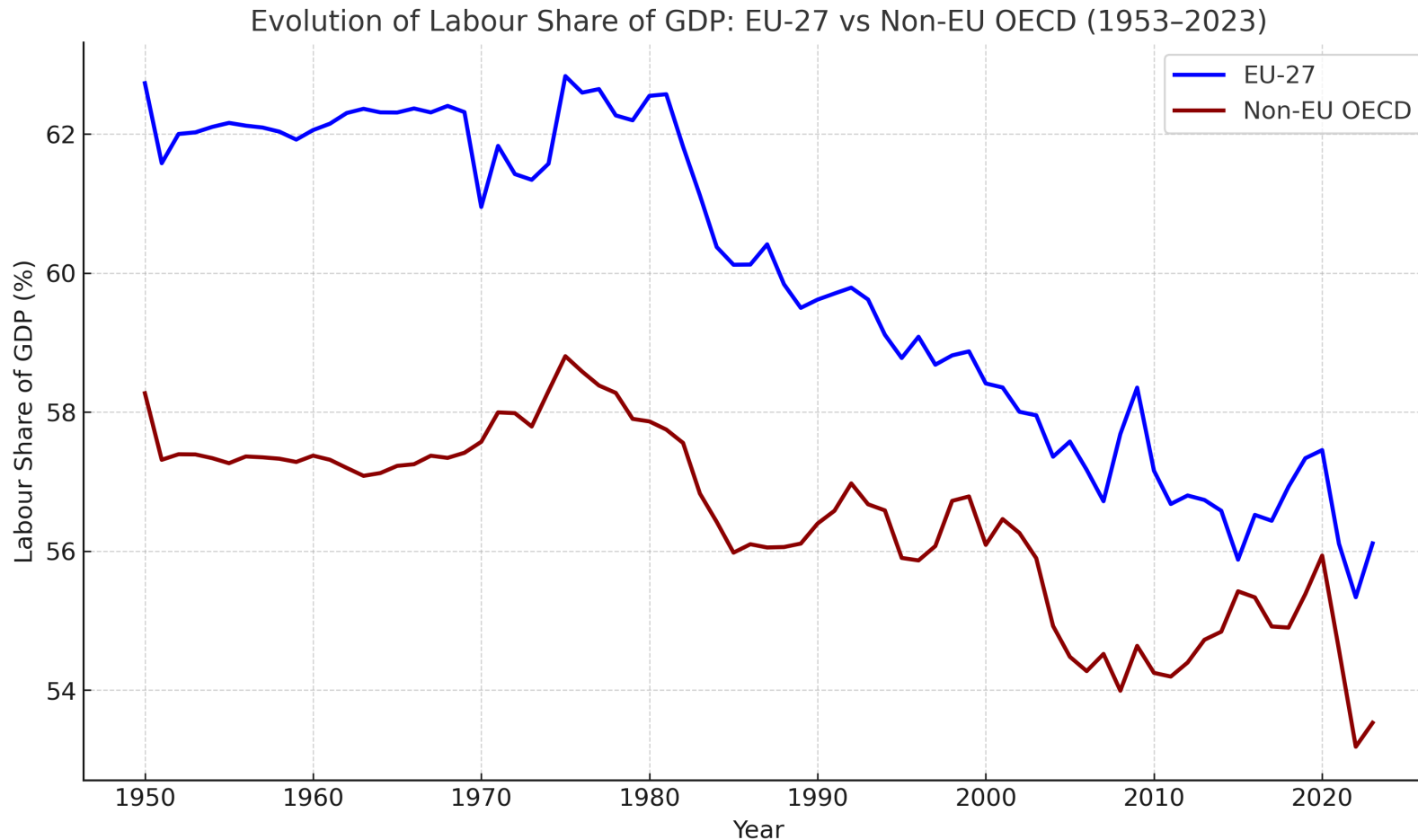
Source: CIA – Report on Canadian Economic Statistics 1924-2021, Table 1B



Source: Penn World Table (PWT 10.0), variable 'labsh' – Share of labour compensation in GDP at current national prices; calculations by author for EU-27 and Non-EU OECD averages.

# 2 challenges for PAYG or Partially Funded schemes

## 1- Salary growth does not follow productivity growth anymore





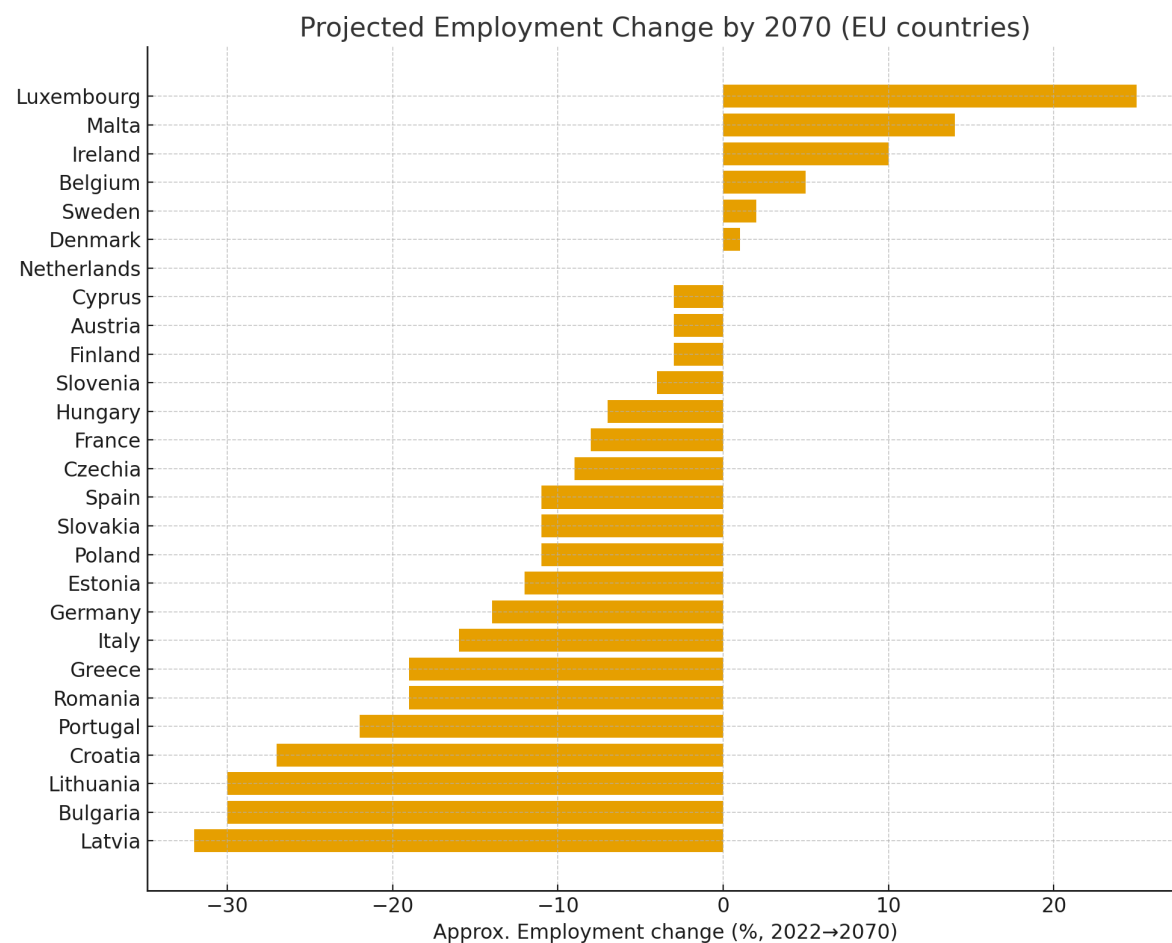
## ► 2- In EU-27, employment is projected to decrease in most countries

### Based on EU Ageing Report 2024's projections and author's calculations

- The EU-27 employment rate (20–64) is projected to rise from about 75% in 2022 to 79% in 2070
- Despite higher participation and employment rates, the working-age population declines by around 12%
- Total employment is projected to fall by about 8–10% by 2070
- Employment may grow in Ireland, Luxembourg, Malta, and Sweden, but decline sharply in Eastern and Southern Europe

# 2 challenges for PAYG or Partially Funded schemes

## 2- In EU-27, employment is projected to decrease in most countries



And these projections do not yet reflect the impact that AI has started to have on employment

What share of productivity gains will be reflected in real wage growth?

## ► In this context, what can be done to achieve the 9 ILO principles

- Intergenerational solidarity: higher contribution rates paid by future generations of workers
- Rely more on multi-pillar system with a reduced pillar 1
- Innovative ways to finance contributory schemes
- Combination of innovative financing and higher pre-funding of Pillar 1: Rely more on capital market than human capital

## ► Intergenerational Solidarity – An application of the scale premium system

What does it mean

- Horizontal redistribution
- Vertical redistribution
- Intergenerational redistribution

The basic principle on which all social security schemes were established is that future generations of workers will be wealthier than current generations, meaning that they will be able to afford to pay higher contribution rates

Assuming real wage increases of 1.5% (wage increases above inflation), in 2070, the average worker's wage will be almost twice, in constant currency, today's average worker's wage (i.e. 1.95 times).

Even if the contribution rate of the workers is doubled from 10% to 20%, the average worker's disposable income (after payment of contribution) would still be 1.74 times today's average worker's disposable income

## ► Intergenerational Solidarity – An application of the scale premium system

Demonstration with a wage of 1,000 in 2025

### ► Today

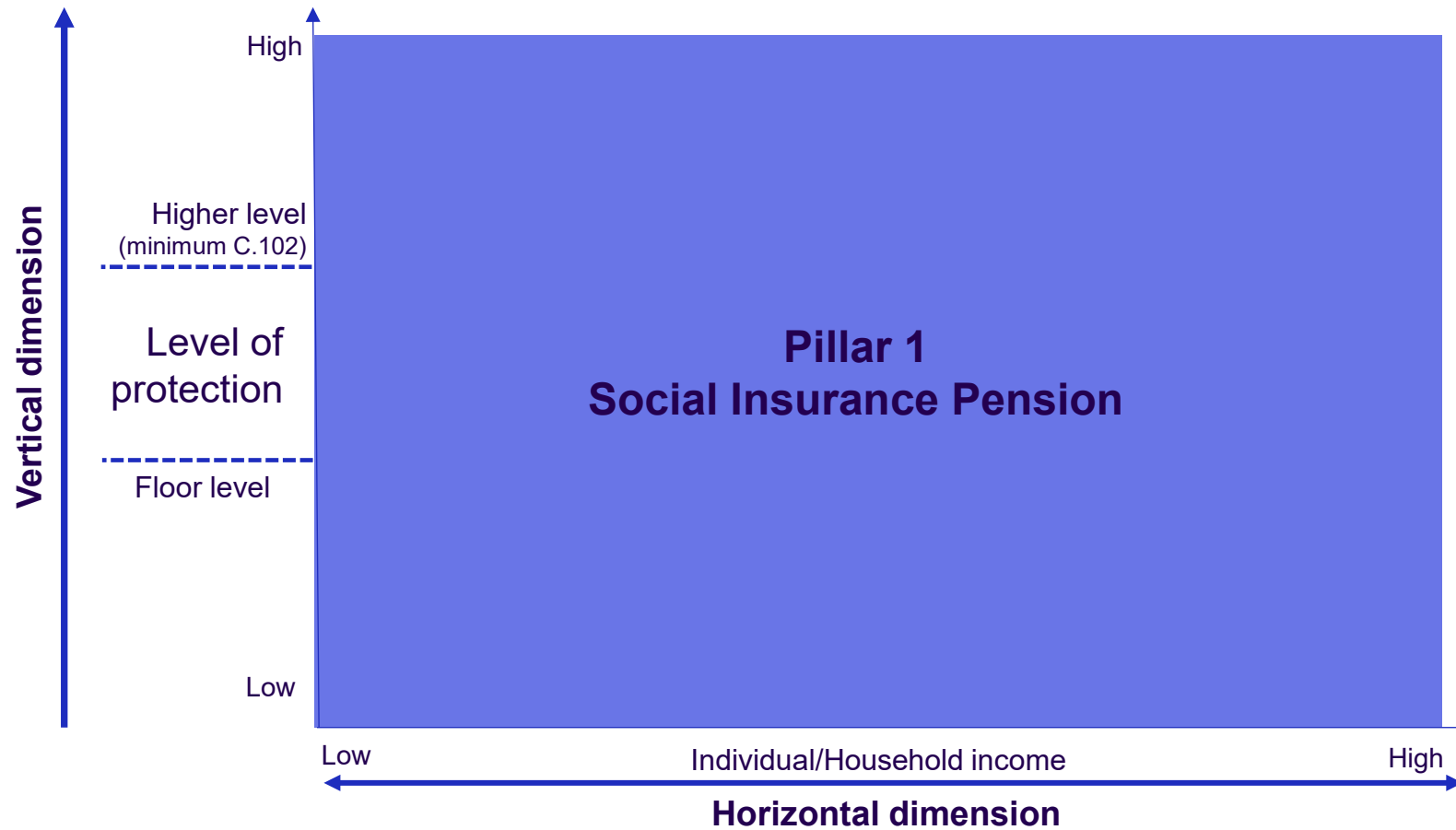
- Contribution:  $10\% \times 1,000 = 100$
- Disposable income:  $900 = 1,000 - 100$

### ► In 2070

- Real wage increase: 1.015
- Wage in constant currency:  $1,954 = 1,000 \times 1.015^{45} = 1.95 \times \text{today's wage}$
- Contribution:  $20\% \times 1,954 = 391$
- Disposable income:  $1,563 = 1,954 - 391 = 1.74 \times \text{today's disposable income}$

**Question is: How much of their productivity gains (i.e. real wages increases) will future generations be willing to give up in the name of intergenerational solidarity?**

## ► Rely more on multi-pillar system with reduced pillar 1

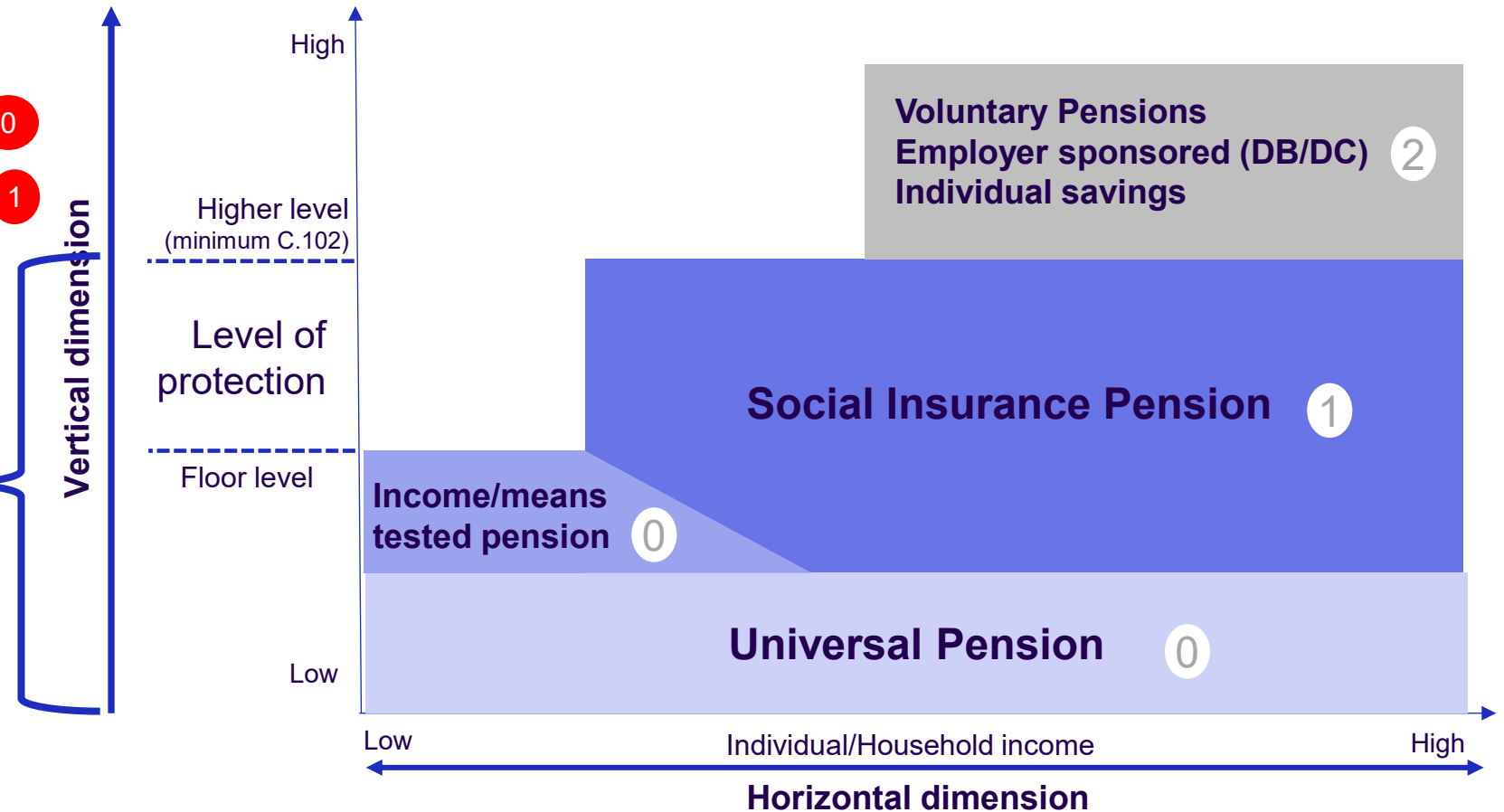


## ► The ILO two-dimensional multi-pillar approach to extension

### Financing:

- Tax finance – Pay-As-You-Go 0
- Contributory – Partially funded 1
- Contributory – Fully funded 2

The essential pillars of  
a national pension system



## ► Innovative ways of financing contributory schemes

### ► Rebalancing Contributions Beyond Wages

- Move away from wage-only financing to capture value from capital, automation, and AI.
- Link employer contributions to capital intensity, profits, sales, or investment in labour-replacing technologies (e.g. 'robot tax')
- Ensures capital-intensive sectors contribute fairly and relieves pressure on labour-intensive firms

### ► Sectoral and Platform-Based Levies

- Portugal: contractors pay contributions for self-employed workers they hire.
- India & Indonesia: levies on construction projects finance insurance for all workers.
- Digital platforms: charges on platform turnover fund social-insurance coverage for gig workers.
- Brazil: unemployment insurance financed by taxes on firms' total revenue, not payroll size



## ► Innovative ways of financing contributory schemes

### ► Complementary Corporate & Fiscal Measures

- Increase corporate-profit taxation or implement a coordinated global minimum tax
- Combine tax-based universal protection with contributory schemes for resilience

### ► Guiding Principles

- Preserve solidarity, fairness, and sustainability between capital and labour.
- Use innovative levies to extend coverage to informal and self-employed workers.
- Reinforce long-term financial sustainability and social justice

## ► Combining innovative and higher pre-funding of Pillar 1 pension schemes

- In the context of shrinking employment and real wage growth that does not follow labour productivity
  - Cost of accrued benefits can hardly be supported only by solidarity of future generation of workers
  - This cost should be financed, at least partly by innovative ways of financing presented in previous slides
- Future benefit accrual, if productivity gains continue to benefit more to the capital market than the human capital
  - Contributory pension schemes (Pillar 1) should be more prefunded to benefit from productivity gains
  - However, this will shift the risk management from human capital risks to capital market risks

# Thank you for your attention!

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