



The Icelandic Pension System

November 2017



LANDSSAMTÖK
LÍFEYRISSJÓÐA

The pension system



The Icelandic pension system is based on three pillars:

1. Tax-financed and income-tested **public pension**
2. Mandatory membership in occupational **pension funds**
3. Voluntary **individual pension savings**

The importance of Pension Funds



Three pillar system

Public
• minimal pensions

Pension funds
• wage related pensions

A free pension saving
• with participation of employer

Pension funds are foundation

Mandatory saving

Fully funded system

Old age pensions
Disability, spouse- and child pensions

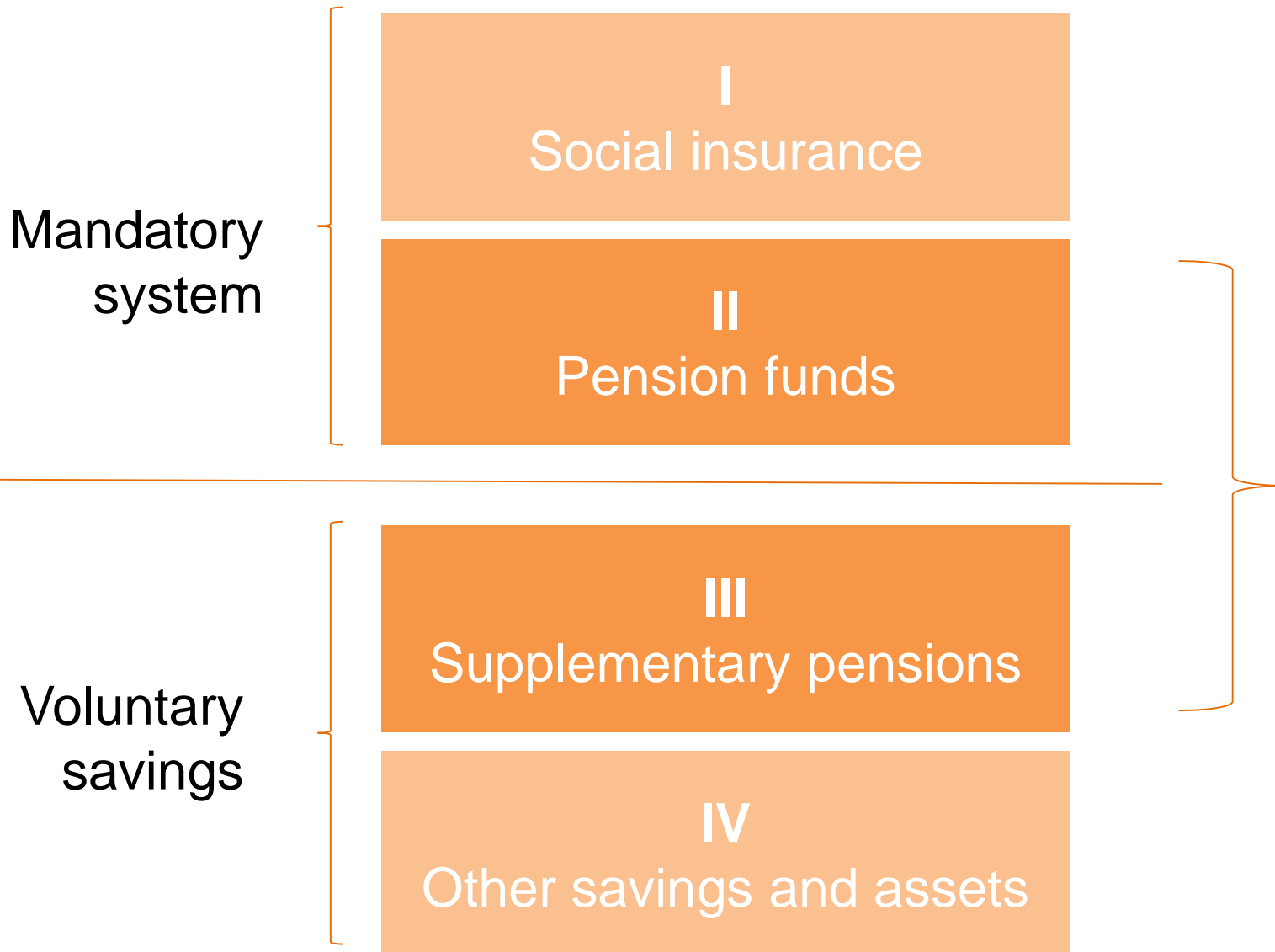
The Icelandic pension system is based on three pillars. The first pillar is based on a tax-financed public pension (social security benefits).

The second pillar consists of mandatory occupational pension funds which are the dominant feature of the system.

The third pillar is based on voluntary individual pension savings with tax incentives.

The main characteristic of the Icelandic pension system is the operation of mandatory occupational pension funds and a fully funded system.

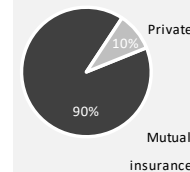
Retirement income



Pensions funds at year end 2016



No.	Pension fund	Net assts		Accrued	Growth 2016	Mutual	Private
		B.ISK	%			B.ISK	B.ISK
1.	Lífeyrissjóður starfsmanna ríkisins	720	20,4%	20%	23,6%	706	14
2.	Lífeyrissjóður verslunarmanna	602	17,0%	37%	3,2%	591	11
3.	Gildi lífeyrissjóður	472	13,3%	51%	3,7%	468	4
4.	Birta lífeyrissjóður	320	9,1%	60%	2,6%	307	13
5.	Stapi lífeyrissjóður	187	5,3%	65%	4,1%	182	5
6.	Frjálsi lífeyrissjóðurinn	186	5,3%	70%	6,7%	55	130
7.	Almennir lífeyrissjóðurinn	185	5,2%	76%	6,2%	88	97
8.	Söfnunarsjóður lífeyrisréttinda	143	4,0%	80%	2,3%	141	2
9.	Brú - Lífeyrissjóður starfsmanna sveitarfélaga	128	3,6%	83%	12,3%	128	
10.	Festa lífeyrissjóður	119	3,4%	87%	6,3%	119	0
11.	Lífeyrissjóður starfsmanna Reykjavíkurborgar	74	2,1%	89%	2,5%	74	
12.	Lífsverk lífeyrissjóður	73	2,1%	91%	10,0%	63	10
13.	Lífeyrissjóður bankamanna	71	2,0%	93%	5,1%	71	
14.	Íslenski lífeyrissjóðurinn	61	1,7%	95%	11,6%	12	49
15.	Lífeyrissjóður Vestmannaeyja	46	1,3%	96%	0,7%	45	0
16.	Eftirlaunasjóður FÍA	32	0,9%	97%	6,1%	32	
17.	Lífeyrissjóður bænda	31	0,9%	98%	2,8%	31	
18.	Lífeyrissjóður hjúkrunarfræðinga	26	0,7%	98%	-4,6%	26	
19.	Lífeyrissjóður starfsmanna Búnaðarbanka Íslands hf.	22	0,6%	99%	4,5%	22	
20.	Lífeyrissjóður starfsmanna Akureyrarbæjar	10	0,3%	99%	0,9%	10	
21.	Lífeyrissjóður Rangæinga	10	0,3%	100%	8,3%	10	
22.	Lífeyrissjóður Tannlæknafélags Íslands	5	0,1%	100%	7,0%	1	4
23.	Lífeyrissjóður starfsmanna Kópavogsbæjar	4	0,1%	100%	4,8%	4	
24.	Eftirlaunasjóður Reykjanesbæjar	4	0,1%	100%	1,8%	4	
25.	Eftirlaunasjóður starfsmanna Útvegsbanka Íslands	0	0,0%	100%	14,7%	0	
		3.533	100%			3.194	340



At the beginning of 2017 there were 25 funds operating (96 funds in 1980)

10 largest funds: 87% of the system
5 largest funds: 65% of the system

Majority of assets, or about 90%, are mutual insurance funds that pay lifelong old-age and disability pensions

Most pension funds offer members to pay supplementary pension savings into private accounts

Organization of old age protection



- Pension system
 - Three pillars (pillar 1, pillar 2, pillar 3)
 - Pillar 1: On basis of residence, income-tested
 - Pillars 2 and 3: On basis of contributions
- Social assistance of the elderly
 - Municipalities: On basis of need (means-test)

The first pension pillar



- Emphasis on those with low or no 2nd pillar pension
- Organized by government
- Basic structure:
 - Each year of residence 1/40th of entitlement, minimum 3 years residence
 - Inflation protected (CPI or better)
 - After 40 year residence: Full basic amount (income-tested)

The first pension pillar contd.



- Basic amounts eff. 2017:
 - Person, living alone: 281.050 ISK (€ 2.280)
 - Person, sharing: 228.734 ISK (€ 1.855)
 - Christmas supplement ISK 51.750 ISK (€ 420)
 - Vacation supplement ISK 34.500 ISK (€ 280)
- All amounts income-tested
 - First 25.000 ISK per month exempt (€ 203)
 - All other income: 1st pillar pension reduced by 45% of income

The second pension pillar



- Mandatory contributions at age 16-70
- Mainly industry-wide pension funds, membership governed by labour contracts
- Managers, specialists, self-employed are free to choose pension funds; several „free“ pension funds focus on them
- Regulated and fiscally stimulated by government
 - Contributions tax-exempt up to a limit (% of wages)

The second pension pillar contd.



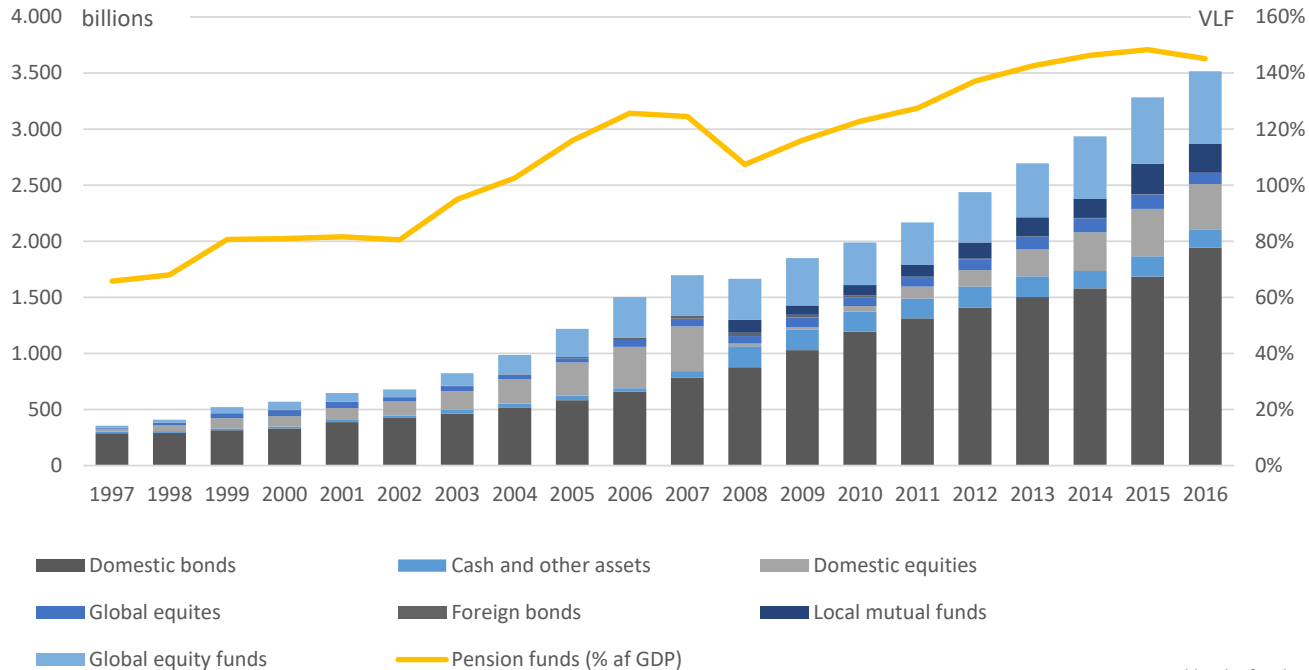
- Everyone has access; full coverage of working population
- Minimum contribution 12% by law (4%+8%); effective contribution 15.5% by mid-2018
- Distribution of 2nd pillar pensions reflects average lifetime wages (contributions)
- Pensions inflation-protected (CPI)

The third pension pillar



- Government-approved savings products
- Managed by 2nd pillar pension funds, banks, insurance companies
- Fiscally stimulated by government (tax-exempt contributions up to a limit)
- Individual decides if to participate; approx. 60% participation

Assets



Assets have grown from 450 to 3.500 billions from 1998

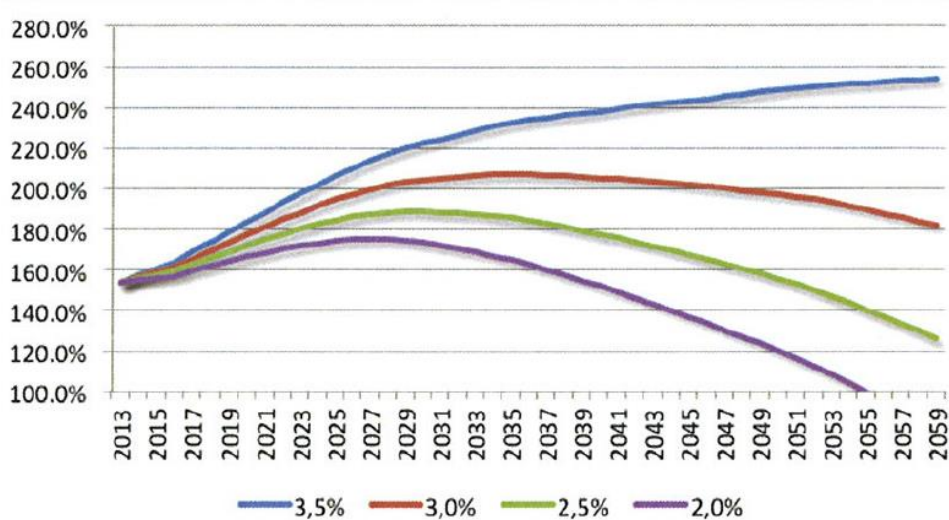
Domestic bonds is the biggest asset class or approx. 60% of assets

Source: Central bank of Iceland

Expected growth



Assets as % of GDP



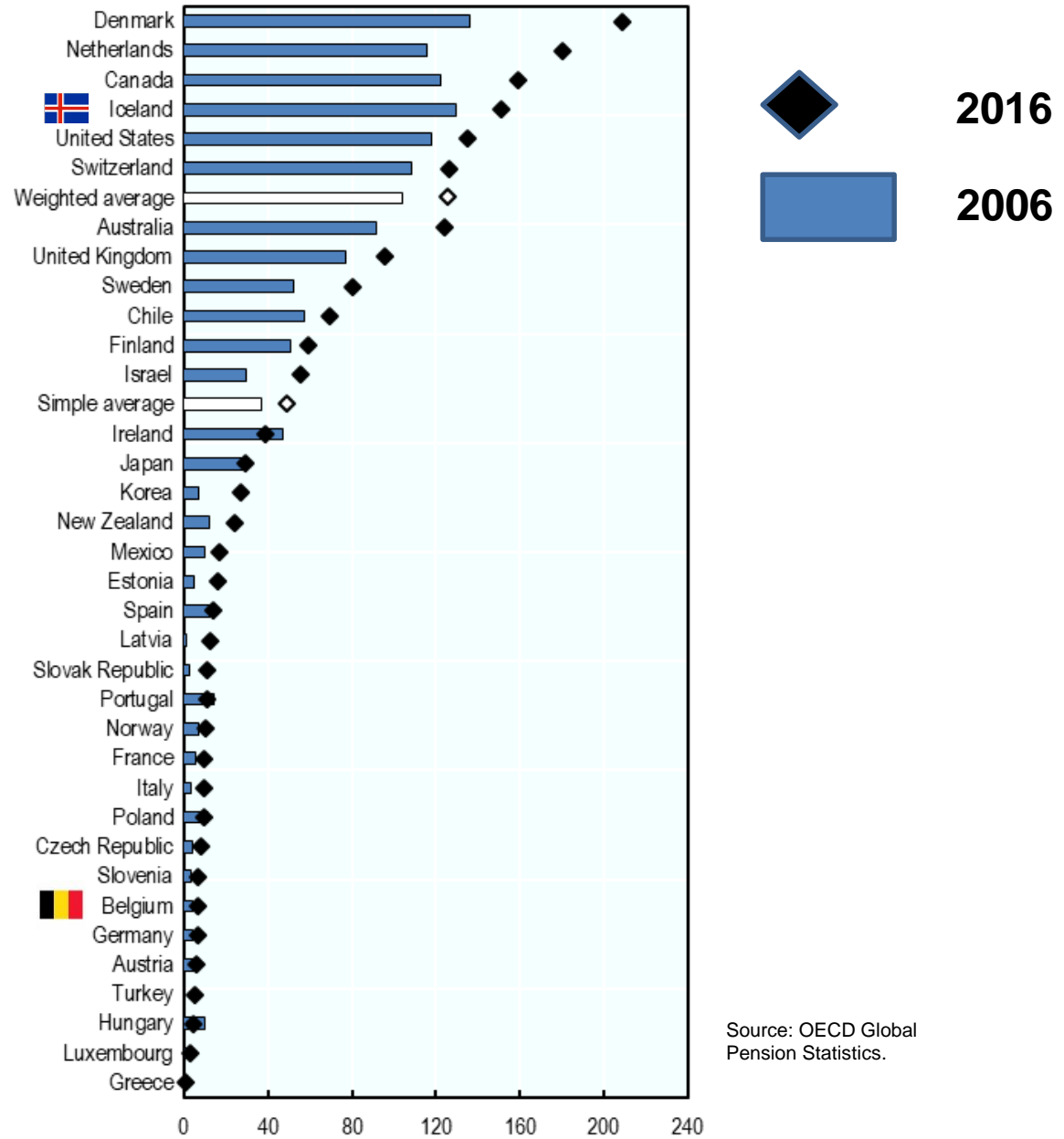
Pension funds are expected to continue to grow.

It is likely that assets will grow to be between 2x and 3x GDP in the future.



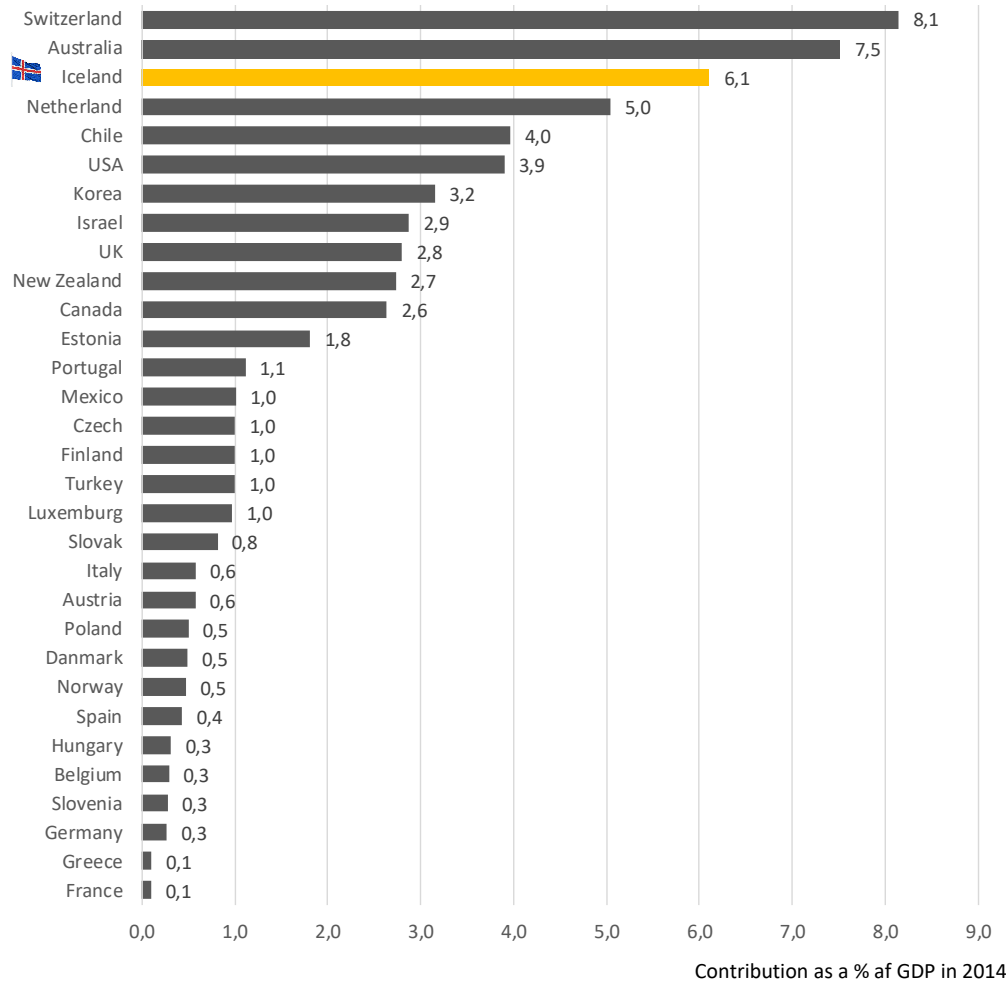
Pension assets to GDP

Four OECD countries achieved asset-to-GDP ratios above 150% in 2016: Denmark (209%), Netherlands (180%), Canada (159%), and Iceland (150%)



Source: OECD Global Pension Statistics.

Contributions in pension funds in selected OECD and non-OECD countries 2014



Iceland is among nations with highest contributions

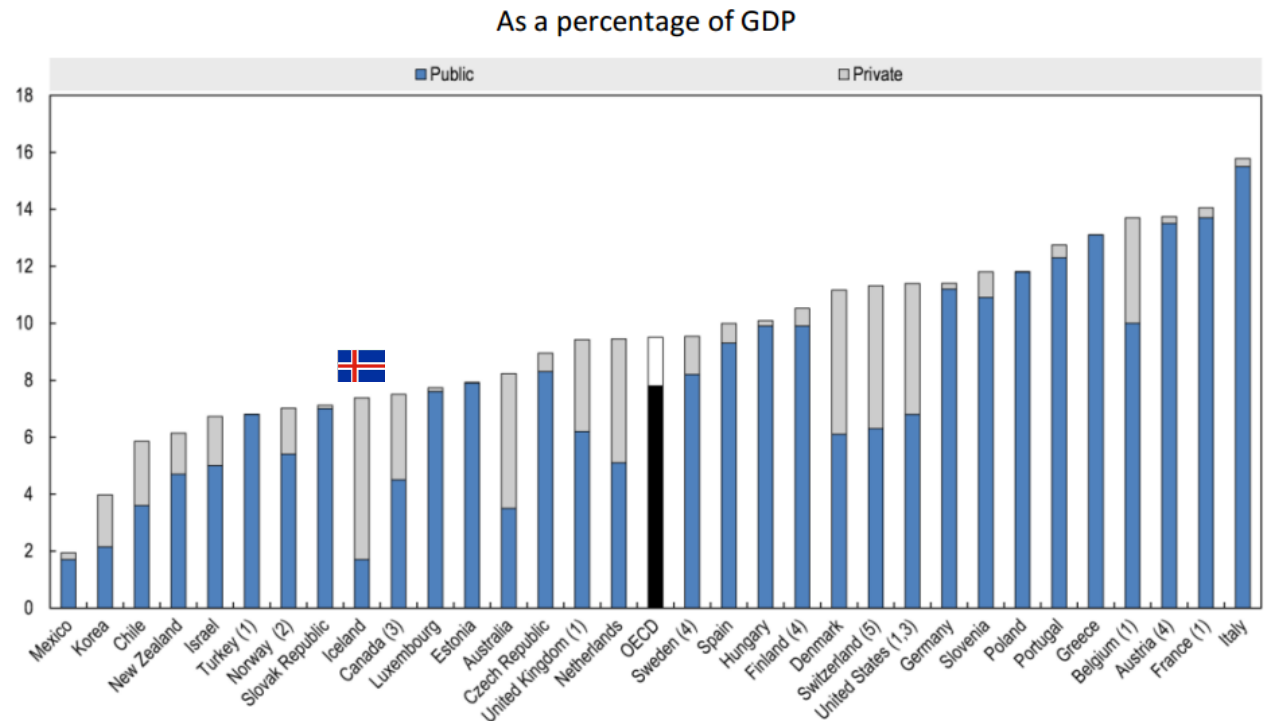
Will probably move up this list in the future

Public vs private pensions



Private pension benefits were greater than public expenditure in two countries: Australia and Iceland

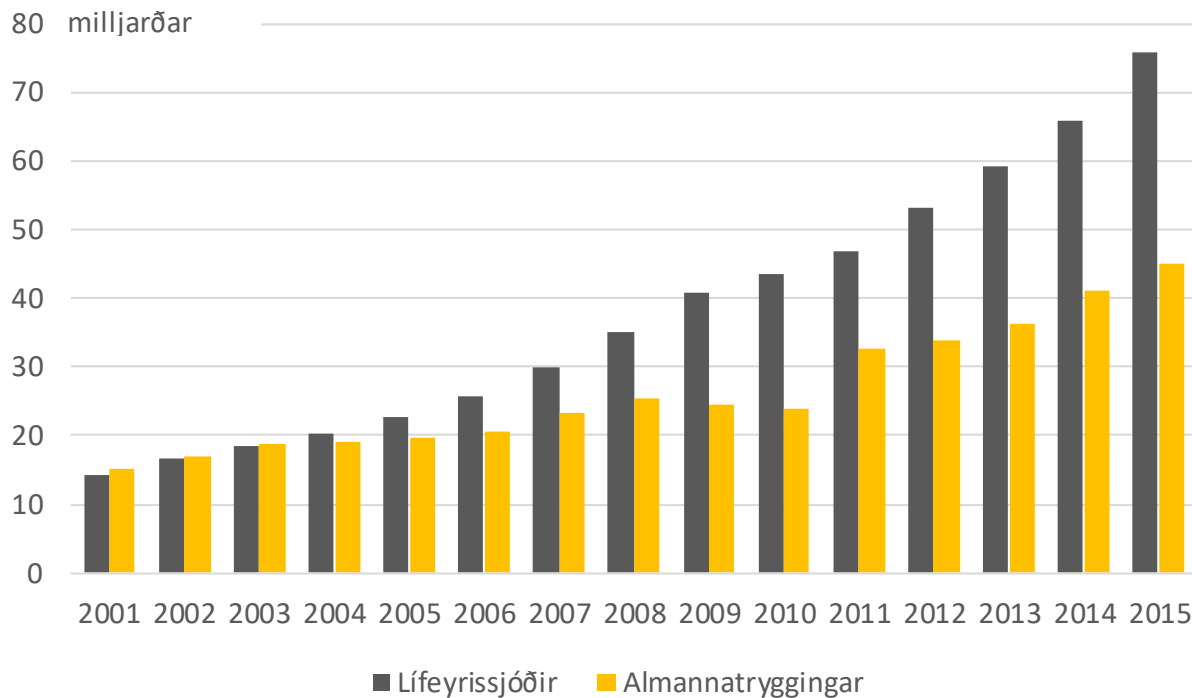
Figure 15. Public and private expenditure on pensions in selected OECD countries, 2012 (or latest year available)



Note: For methodological notes see page 52 onwards.

Source: OECD Global Pension Statistics.

Old age pensions



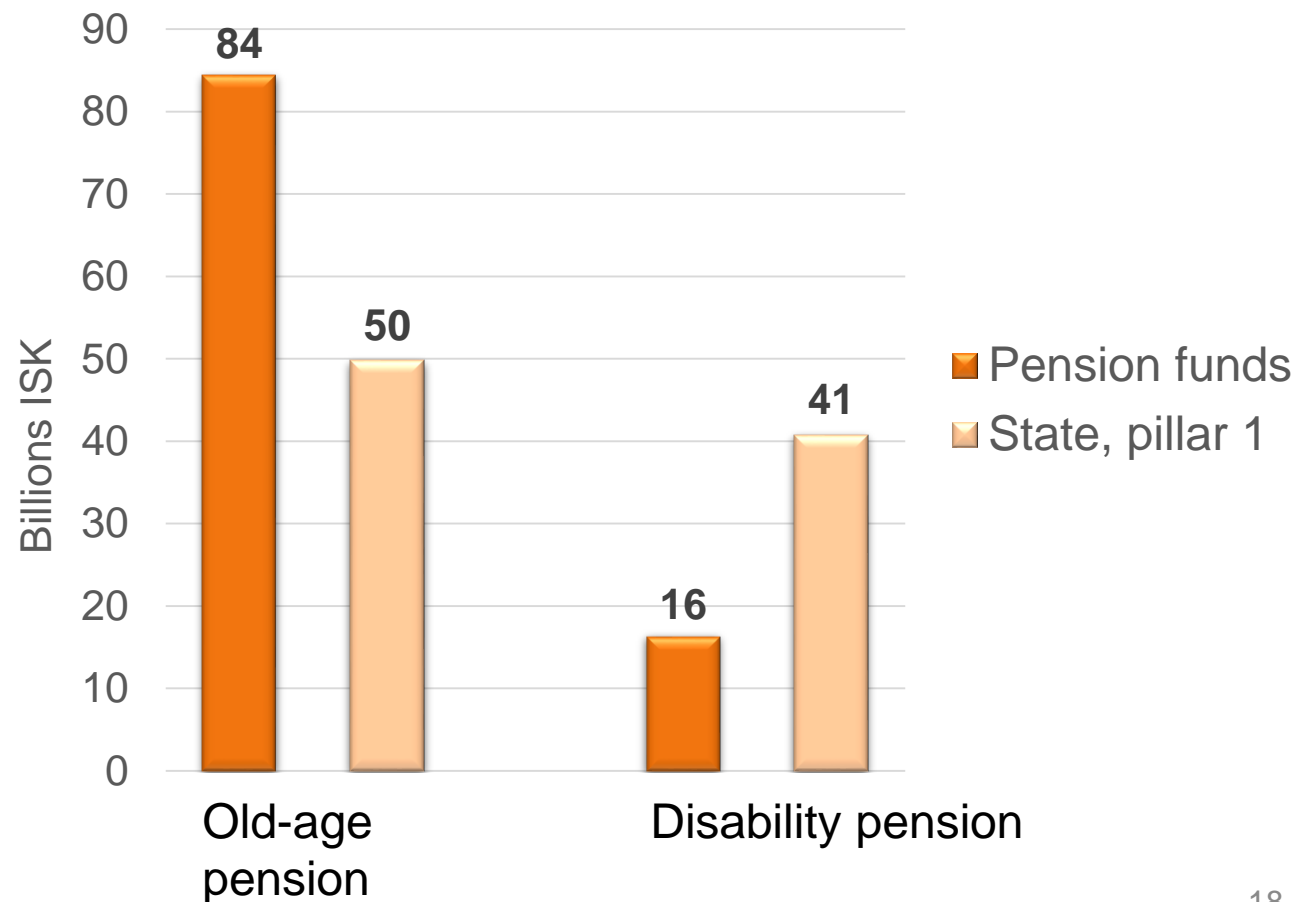
Pension funds have paid majority of old age pensions since 2004

The gap is expected to rise in the future

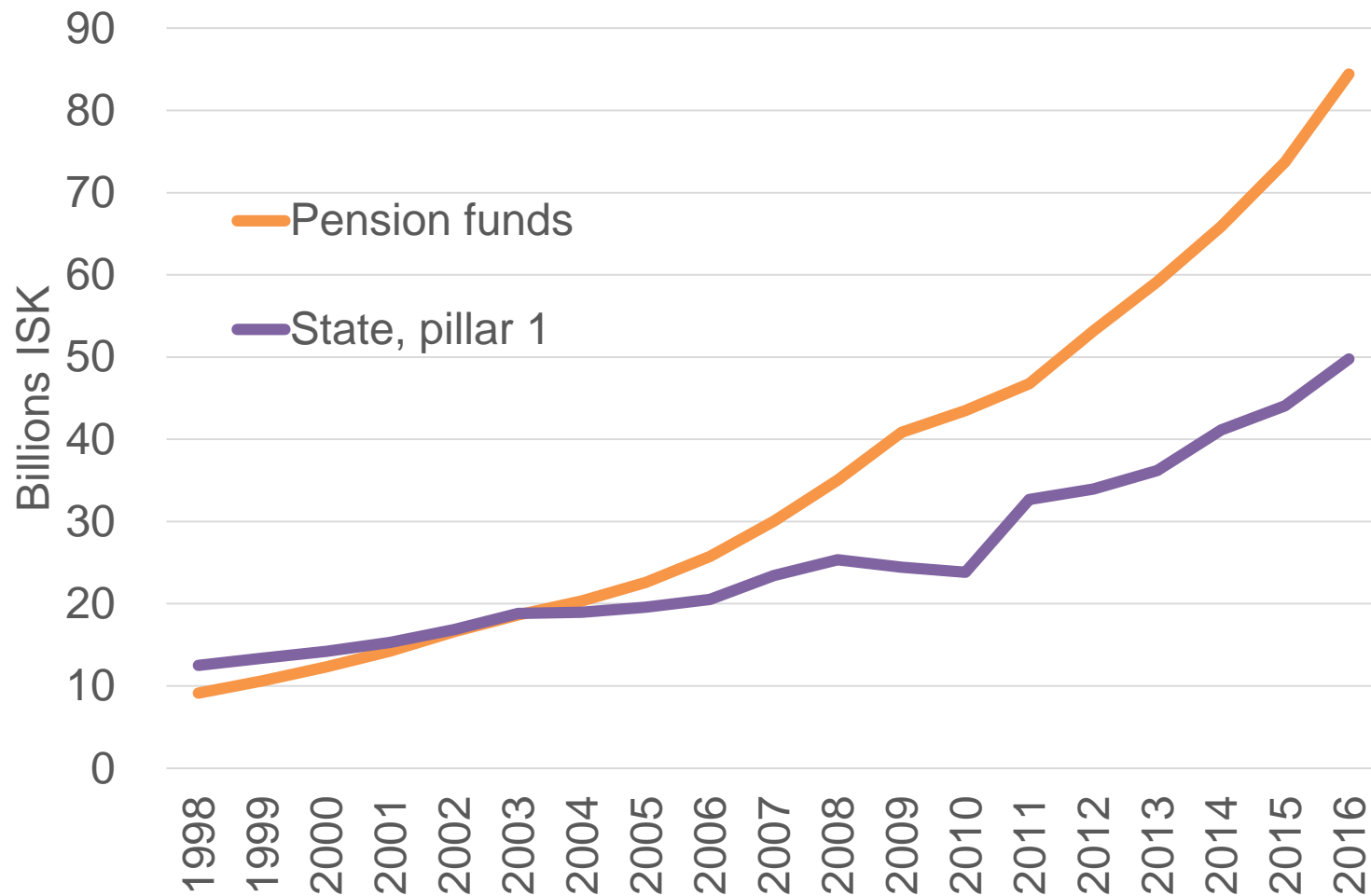


Old-age pension and disability pension 2016

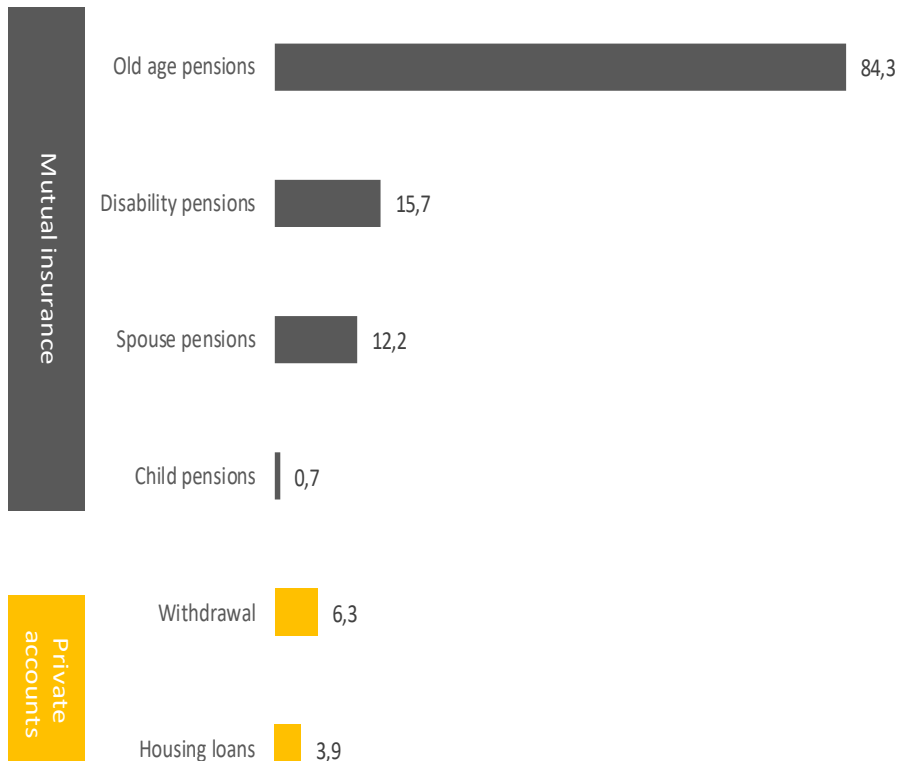
In 2016 pension funds paid 84 Billion ISK in old-age pension. Social insurance paid 50 Billion ISK



Pension funds are the main income provider in retirement



Pensions and withdrawals 2016



Total payments to members were 123 billions ISK in 2016

Mutual insurance funds paid 113 billions ISK. Pension payments are linked to CPI and change monthly

Members received 10 billions from private accounts, where of 3,9 billion were paid into housing loans

Source: Financial supervisory Iceland.

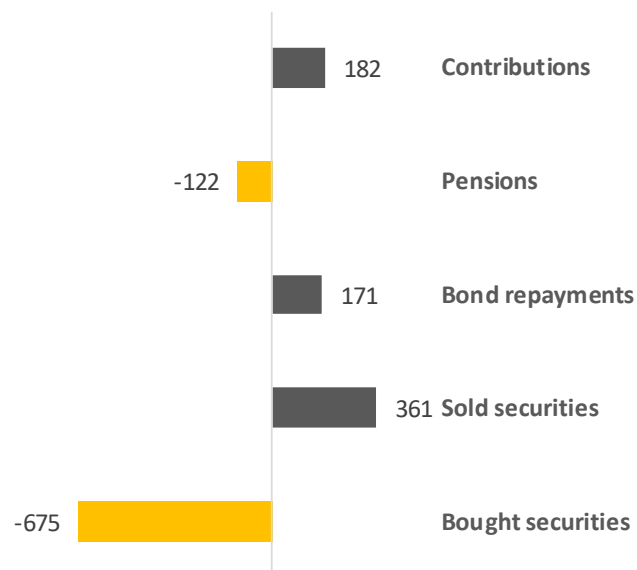
Cash flow 2016



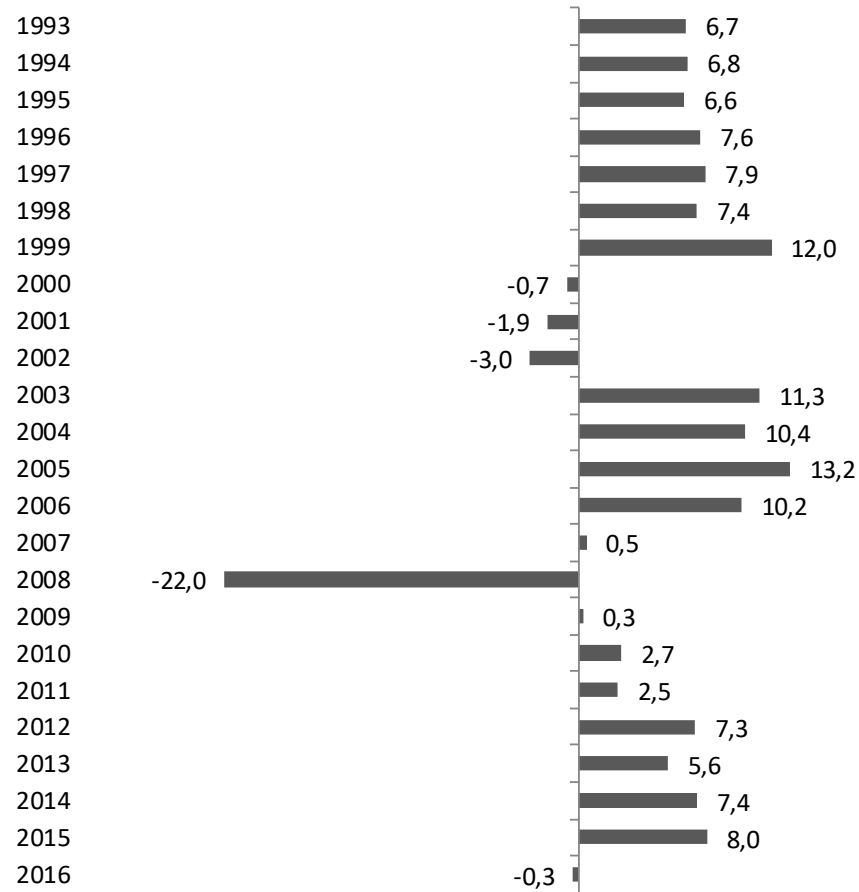
Pensions funds, annual accounts 2016

Pension funds, total	B.ISK
Inflow	795
Contributions	182
Bond repayments	171
Dividends	39
Sold securities	361
Other	42
Outflow	-809
Pensions	-122
Equities and funds	-317
Bonds	-358
Operating cost	-7
Other	-5
Change in cash	-14
Cash at the beginning of year	98
Cash year end	83

Key figures



Real return



Average real return 1993-2016 is 4,2%

Long term real return since 1981 is 4,5%

2014 study on Pensions Adequacy



- Iceland participated in multinational OECD study with grant from European Union
- <https://www.lifeyrismal.is/static/files/Skyrslur/final-report-rsa-iceland.pdf>
- **STRENGTHS:**
- Projected net replacement rate from Pillars I-III totalled 103% over all subgroups.
- Total pension income: Pillar II 67%, Pillars I 23% and Pillar III 10%
 - Housing wealth projected to add 18 percentage points to the total replacement ratio of the three pension pillars.
- Public service DB pension funds much more generous in pensions than the DC funds for the private sector.

2014 study on Pensions Adequacy



- WEAKNESSES:
- Nearly one-third of pensioners will receive less than a 56% replacement ratio from Pillar 2 funds, most of them in private-sector funds. This is mainly due to gaps in contribution years and features of the accrual tables.
- Groups at risk: First-generation immigrants, late entrants to workplace, e.g. after long university studies
- Males receiving 24% higher income on average than females.
- Note: Pillar I social security compensates for low pension income and municipalities are last resource

2017 comparison of country systems

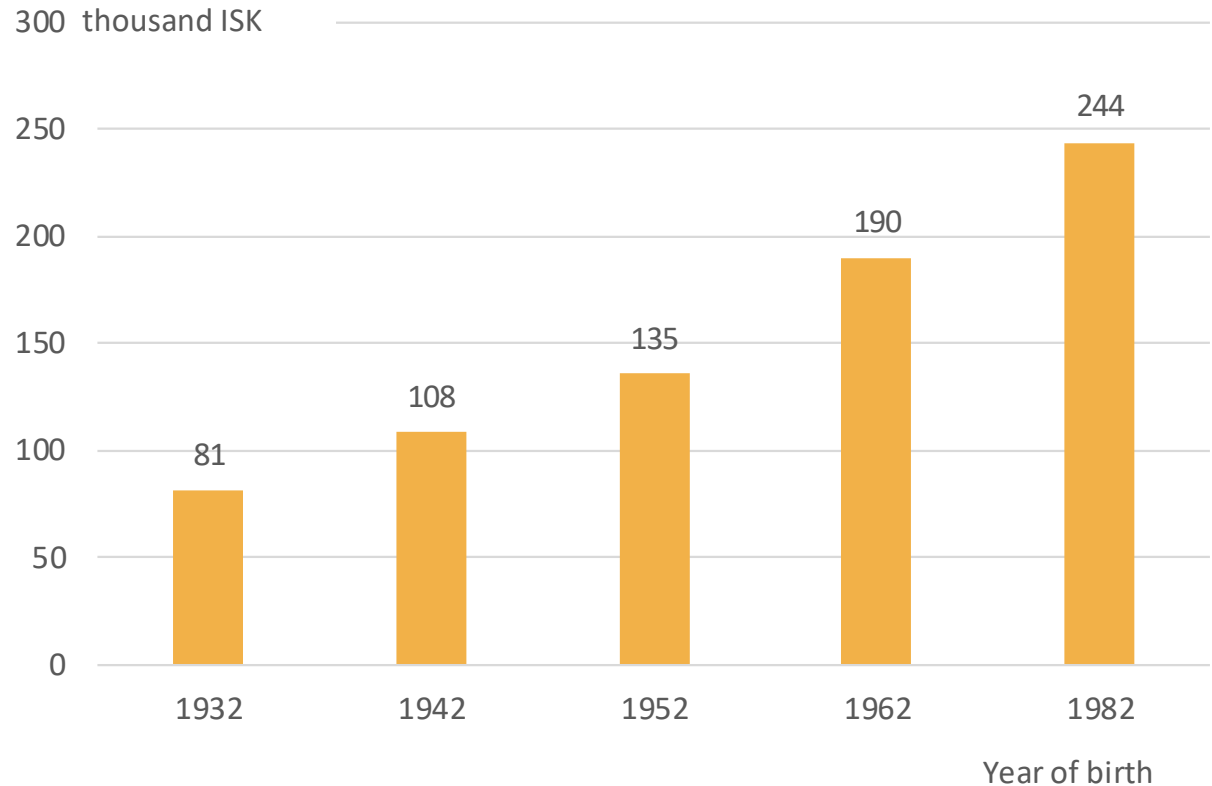


- Pension systems of Iceland, Denmark, Netherlands, Sweden and United Kingdom
 - Report issued March 2017; English summary available
- Iceland compares favorably in most categories:
 - Second highest replacement ratios
 - Highest disposable income of seniors, low relative poverty and lowest income distribution coefficient
- This despite lowest total contributions as % of wages and GDP
 - Public expenditure for old age pensions very low
- Significant factors: High work participation of seniors and high effective retirement age
 - Seniors receive pensions on average 4 fewer years than in the other countries in the comparison

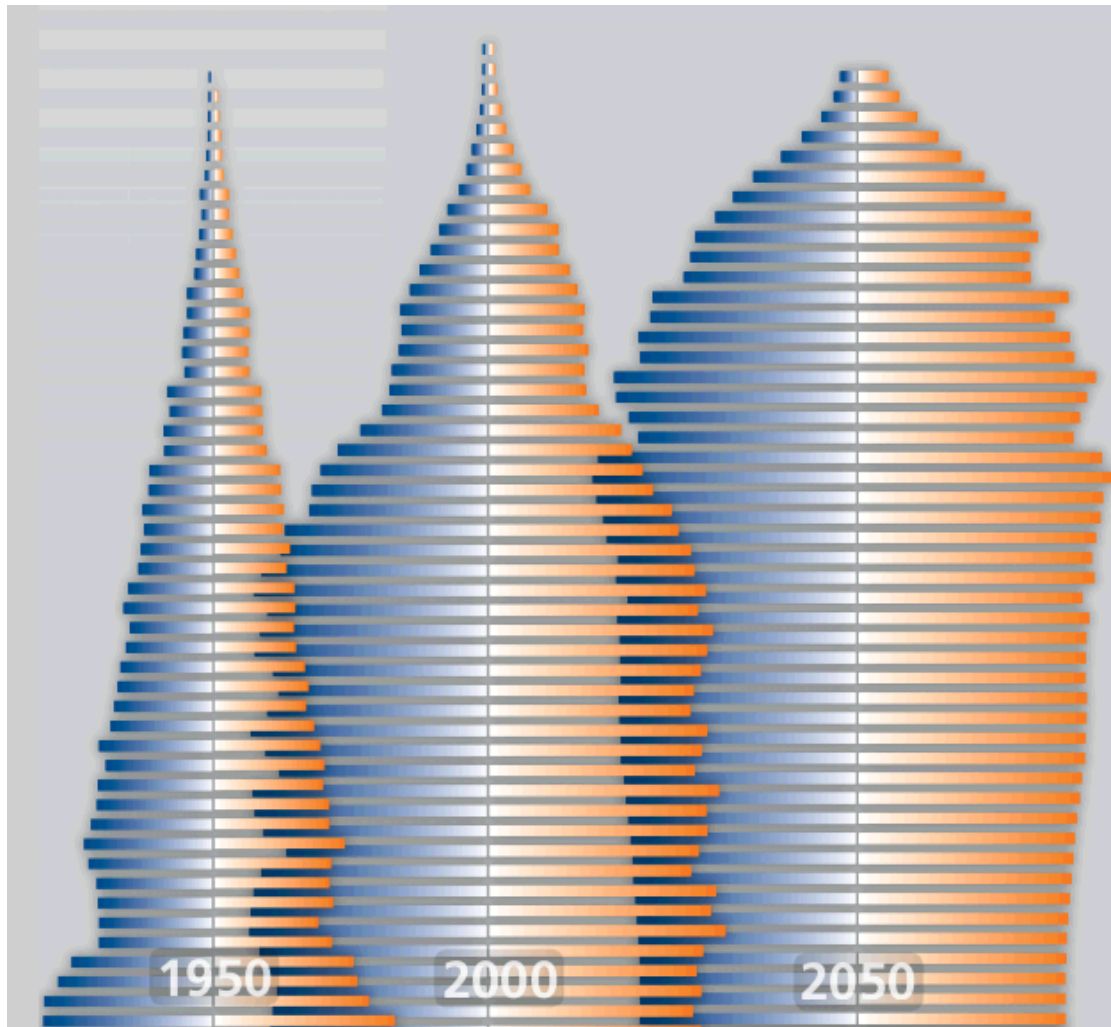
Average pension payments by year of birth



It is estimated that average pensions will rise from 81 K ISK, for citizens born in 1932, to 244 K ISK for those born in 1982



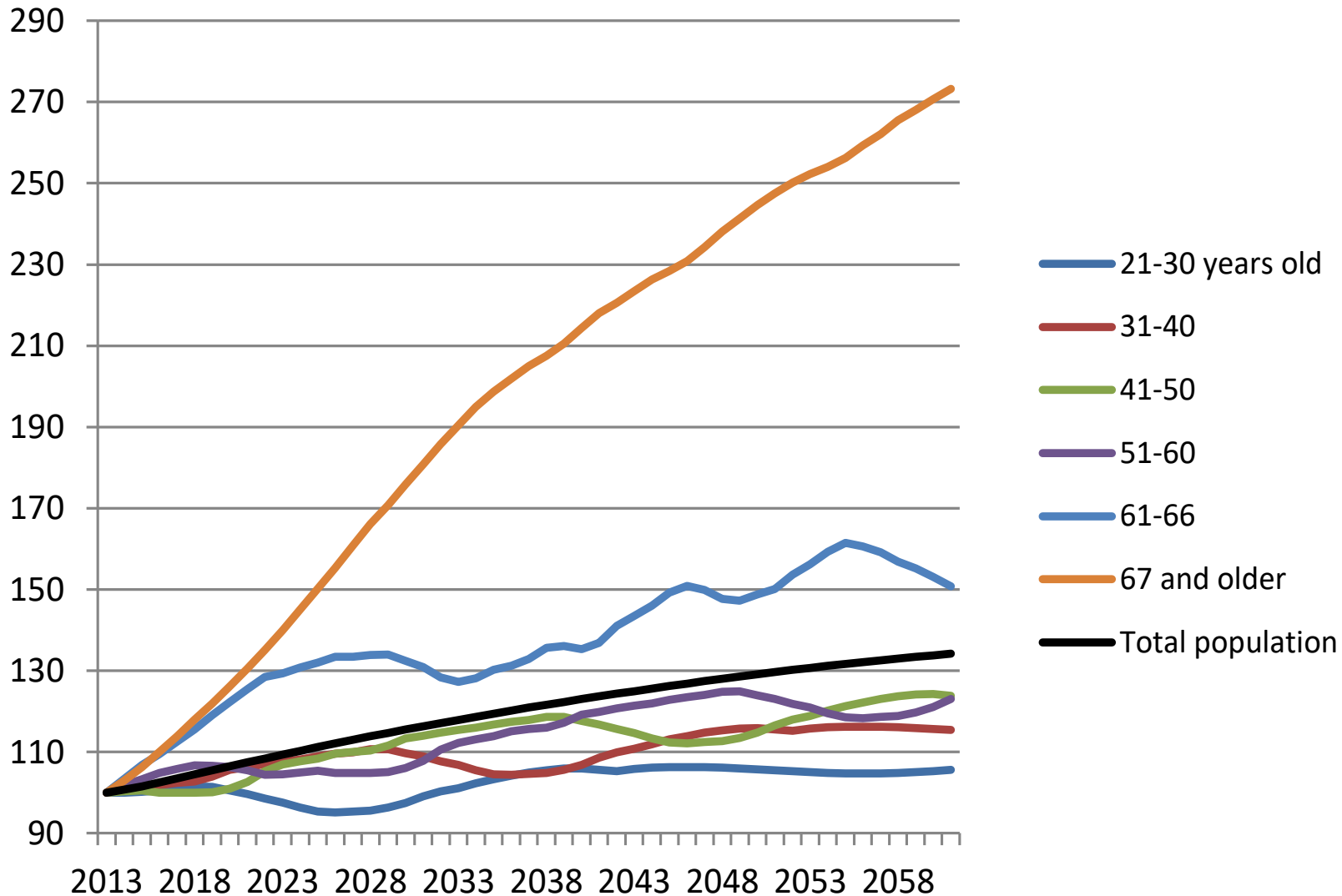
The age pyramid is changing



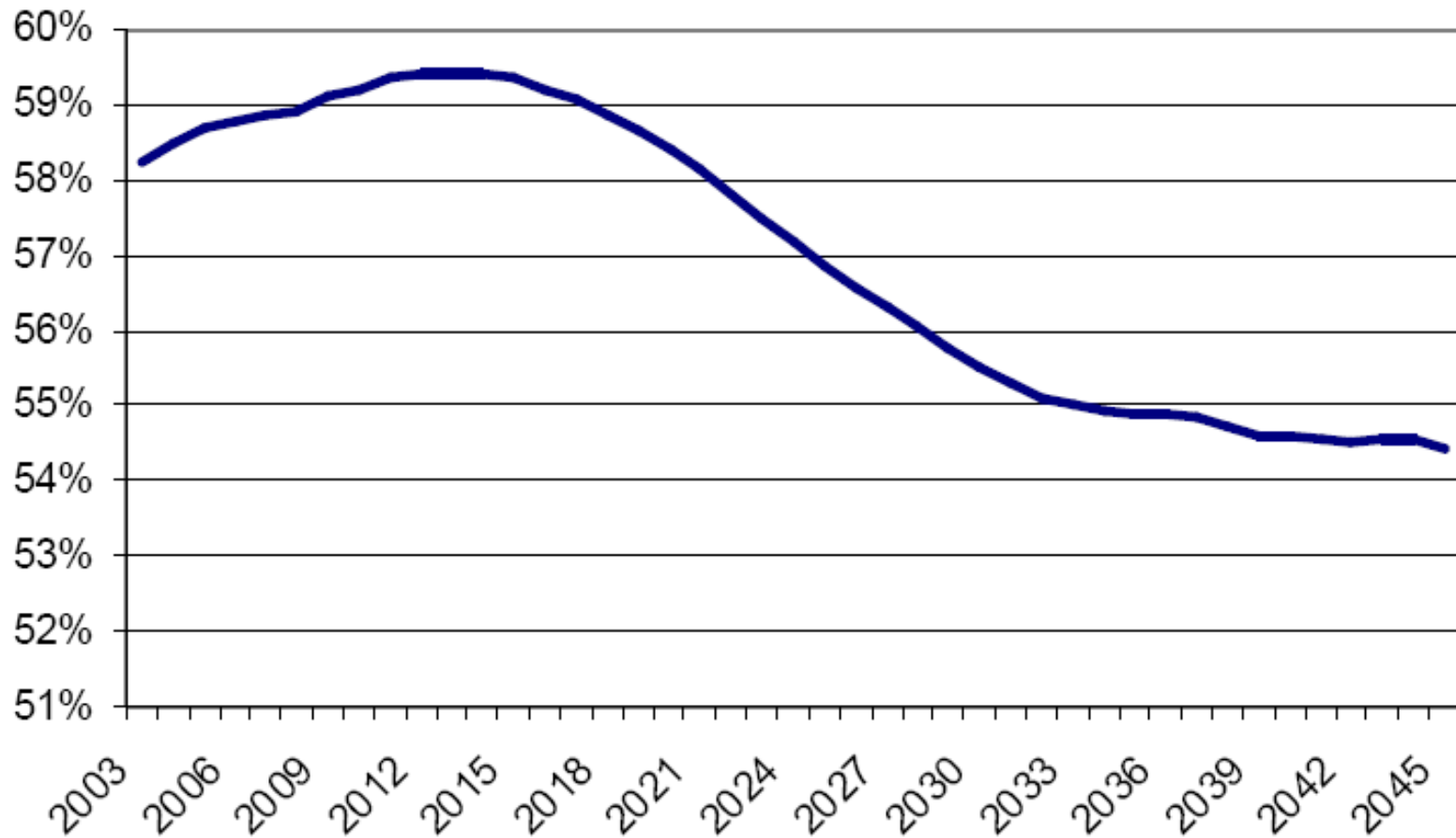
Statistics
Iceland
forecast of
future change
in the age
pyramid

Fully funded
pension funds
are essential
to cope with
the change

Population and age group growth



Workforce ratio will decline



Facts and figures



- Total assets of Pension Funds = 33 billion USD
- Population in the end of 2016: ~338.000
- Assets per inhabitant ~ 10,4 m. ISK ca. 99.000 USD
- Number of pension funds 25

- Mandatory contribution to pension fund is 12% of total salaries (law)
- General workforce pays currently 14% (employee 4%, employer 10%)
 - will be 15,5% from July 1st, 2018
- State employers pay 15,5% (employee 4%, employer 11,5%)

- Individuals can save up to 4% of total salaries into voluntary pension savings schemes
- Employer matches 2% against 2% from employee



- Overall, Iceland has a good and sustainable pension system
- The core: Mandatory occupational pension funds with 100% coverage
 - Generally fully-funded for the general labour market
 - Partially funded for public servants
- Total assets ~150% of GDP at year end 2016
- Good safety net provided by Pillar I social insurance
- Iceland is therefore better prepared than most countries for the „old age crisis“
- More information: www.ll.is



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