

Työllisyysrahasto The Employment Fund

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This report does not constitute a rating action.

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Major Rating Factors

Key strengths

- Critical role for Finland's labor market policy as the sole entity responsible for funding the country's earnings-related unemployment insurance scheme and adult education allowance.
- Uncontested link with the Finnish government, demonstrated by financial support received from the government during the pandemic.
- A business-cycle buffer safeguards its solvency and evens out changes in unemployment insurance contributions caused by trend cycles in the national economy.

Key risks

- Although remote, any erosion of its position in the policy architecture of the Finnish welfare state could reduce interconnectedness with the government.

Outlook

S&P Global Ratings' stable outlook on Työllisyysrahasto The Employment Fund (EF) reflects that on Finland since we consider that EF's critical role for and integral link with Finland will endure and prompt the government to secure the entity's solvency and liquidity in all circumstances.

Downside scenario

Downside risks to the ratings would build if we observed an unwinding of EF's role in the execution of key public policy, leading to a lower degree of government involvement and support for EF's activities. We consider this scenario unlikely over our outlook horizon and expect our ratings on EF to move in line with those on Finland.

Upside scenario

We could raise the ratings on EF if we raise our Finland sovereign ratings, all else remaining equal.

Rationale

We equalize our ratings on EF with those on Finland (AA+/Stable/A-1+). This reflects our expectation of an almost certain likelihood that the Finnish government would provide timely and sufficient extraordinary support to EF in the event of financial distress. Given its critical role in the execution of key labor market policy, which is usually conducted by the government directly, we believe that the almost certain likelihood of extraordinary government support for EF will endure and is not subject to transition risk. We, therefore, do not assess EF's creditworthiness on a stand-alone basis.

We view EF as a department of the government, reflected in its status as an indirect public administration. As a result, EF must comply with the same rules as public authorities. This status not only underlines EF's integral link with the government, but also implies that, if it did not exist, a government body would be needed to manage its duties. We note that EF's net financial position is included in Finland's debt position in the European Monetary Union, a testament to EF's public-sector foundation.

In accordance with our approach for rating government-related entities, we base our assessment of an almost certain likelihood of government support on EF's:

- Critical role for Finland, as the sole entity responsible for funding the Finnish earnings-related unemployment insurance scheme and adult education allowance; and
- Integral link with the Finnish government, as indicated by the government's strong supervision and control over EF.

In administering the financing of statutory unemployment allowances, EF plays a central role in managing what is a key pillar of the Finnish social security system. Because of this vital public-policy role, its interaction with the central government is close and EF has enjoyed unwavering support from the government to fulfil its statutory tasks through periods of macroeconomic stress. The government's supportive stance toward EF was displayed recently as the COVID-19 pandemic tested the Finnish social security system. The economic shock from the pandemic led to a significant increase in layoffs that prompted an unprecedented rise in statutory benefit payments administered by EF. These developments prompted swift actions from EF, which, thanks to support from the central government, fully executed its statutory responsibilities.

EF tapped its extensive financial buffers and benefitted from a strong precautionary financial arrangement from the government to navigate the labor market repercussions of the COVID pandemic in 2020-2021. To safeguard liquidity during the pandemic, the Finnish government provided a guarantee for EF's €880 million revolving credit facility in April 2020. Furthermore, the central government directly financed the temporary layoff schemes that ran from April until year-end 2020, saving EF about €300 million in outlays. We consider the central government to be ultimately responsible for the functioning of the Finnish social security system and hence believe that it will stay committed to ensuring EF's solvency and liquidity position at all times.

In accordance with the Act on the Financing of Unemployment Benefits, EF maintains a business-cycle buffer generated from the difference between its income and expenses. The stipulated maximum buffer is tailored to annual benefits paid by EF at an unemployment rate of 6%. This buffer, equivalent to EF's net asset position, is to safeguard EF's solvency and even out changes in unemployment insurance contributions caused by trend cycles in the national economy. EF seeks to ensure the sufficiency of the business-cycle buffer by setting unemployment insurance contribution rates at an appropriate level, using diverse forecasting methods. Aside from leaning on central government support, EF has used its own resources to satisfy the heightened demand for unemployment payouts. EF has tapped its business-cycle buffer extensively over 2020-2021. We expect it to reduce €1.2 billion in total over the two pandemic years to end at €500 million at year-end 2021. For 2022, we anticipate the buffer will remain largely stable at €500 million following EF's budget and our forecast for an improving labor market. EF's financial activities over 2020 also included the placement of two bonds totaling €1.2 billion. Overall, EF benefits from strong access to loans and capital market funding and it was accepted by the European Central Bank as an issuer under its Public-Sector Purchase Program in 2015.

Changes in employment and unemployment rates affect both EF's revenue (premium income base) and expenditure (unemployment payment base). The shock to the Finnish economy as a result of the pandemic resulted in a stark rise in benefit payments for EF, as people became unemployed or entered the temporary unemployment scheme, an existing feature of Finnish labor market legislation.

As a result, the fund's profit-and-loss position deteriorated markedly to a deficit of 23% of turnover in 2020. We expect the profit-and-loss position to improve slightly in 2021, but remain in negative territory, resulting in a deficit of 18% of turnover due to the still-elevated unemployment rate. In light of the pandemic, total contributions increased 0.32% in 2021 to stand at 1.40% for employees and 1.41% for employers (average; the total unemployment insurance contribution is 2.81%). To stabilize its financial position, EF has submitted a proposal to the Ministry of Social Affairs and Health for total contributions to be increased 0.2% in 2022. We expect the government to approve this proposal, which we anticipate will lead EF to break even.

EF's financial performance mirrors the economic and employment conditions in Finland, which have turned a corner in 2021, supported by vaccine rollouts and the return of domestic and external demand. We expect the economy to rebound strongly to 3.2% growth in 2021 and surpass prepandemic levels by year-end on the back of strong recovery in demand, business investment, and international trade. Confidence in the manufacturing sector is expected to rebound strongly in second-half 2021. We believe these robust growth dynamics will continue into 2022, owing to strong exports, private consumption, and investments in machinery and the construction sector. We expect growth will then stabilize at about 1.4% by 2024, converging toward the economy's potential.

Finland's unemployed rate has now recovered to prepandemic levels with industry confidence indicators all in positive territory. In particular, we note that the wage sum has increased meaningfully in 2021, which is important since it correlates with EF's revenue collection. We expect these positive developments to show in EF's financial performance in 2022 as a large part of 2021 has been characterized by elevated allowances for workers temporarily laid off. In addition, the central government has not deployed any direct support to finance temporary layoff schemes in 2021, in contrast to 2020 where it disbursed €333 million to help EF meet requirements.

Related Criteria

- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

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