Research Update:

Finland-Based Työllisyysrahasto The Employment Fund Affirmed At 'AA+/A-1+'; Outlook Stable

September 29, 2020

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S&PGR Affirms Finland's Employment Fund At 'AA+/A-1+'

Overview

- We believe Työllisyysrahasto The Employment Fund (EF) plays a 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.
- Moreover, EF has an integral link with the Finnish government, demonstrated by financial support EF received from the government during the pandemic.
- We are therefore affirming our 'AA+/A-1+' ratings on EF.
- The stable outlook reflects that on Finland and our expectation of an almost certain likelihood that the government will provide extraordinary support to EF in the event of financial stress.

Rating Action

On Sept. 29, 2020, S&P Global Ratings affirmed its 'AA+/A-1+' long-term and short-term issuer credit ratings on Finland-based Työllisyysrahasto, The Employment Fund (EF). The outlook is stable.

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 still view EF as a department of the government, reflected in its status as an indirect public administration. As a result, EF is treated as a public authority and must therefore 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 the 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 government to fulfil its statutory tasks through periods of macroeconomic stress. The government's supportive stance toward EF was displayed this year 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 benefits payments administered by EF. These developments prompted swift actions from EF, which thanks to support from the central government, fully executed its statutory responsibilities.

To safeguard liquidity during the pandemic, the Finnish government provided a guarantee for EF's revolving credit facility of €880 million in April 2020. Furthermore, the central government is directly financing the temporary layoff schemes that run from April until the end of 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.

Aside from leaning on central government support, EF has used its own resources to satisfy the heightened demand for unemployment payouts in March and April by divesting about one-third of its investment assets. These liquid assets were subsequently replenished in June when EF placed two bonds totaling €1.2 billion, bringing the value of its investment and financial assets to €2.05 billion at the end of the month. We expect these funds will be used to finance monthly outflows, estimated at €400 million, for the remainder of the year. Overall, EF benefits from strong access to loans and capital market funding, and was accepted by the European Central Bank as an issuer under its Public-Sector Purchase Program in 2015.

EF's financial performance mirrors the economic and employment conditions in Finland. We expect the Finnish economy will contract by 4.5% in 2020, which is modest in a eurozone comparison; this is partly a result of the depth of the Finnish welfare systems and predictability of income-ensuring frameworks that have sustained household consumption despite a highly uncertain labor market. We forecast Finland's unemployment rate will approach 8% in 2020 from 6.7% in 2019, and remain elevated in 2021.

Changes in employment and unemployment rates affect both EF's revenue (premium income base) and expenditure (unemployment payment base). However, because EF has the tools to propose premium levels, differences between actual employment and unemployment rates compared with its forecasts determine its performance, rather than year-to-year changes in those statistics. The unemployment insurance contribution (UIC) for 2020 stood at 1.25% for employees and employers respectively (the total UIC is 2.5%). In light of the pandemic, EF has submitted a proposal to the Ministry of Social Affairs and Health for the total amount of contributions to be increased by 0.32% in 2021.

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.

Because of heightened expenditure pressures in the social security system, we forecast EF's profit and loss position will deteriorate over 2020. Depending on the extent to which furloughed workers return to work or become unemployed, we expect a deficit of about €850 million in 2020 in our base case, compared with a budgeted surplus of €100 million in August 2019. As a consequence, we expect EF's net position to reduce to €850 million from €1.7 billion at year-end 2019.

Outlook

The stable outlook reflects that on Finland since we consider that EF's critical role for and integral link with Finland will endure and prompt 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.

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

Ratings List

Ratings Affirmed	
Tyollisyysrahasto, The Employment Fund	
Sovereign Credit Rating	AA+/Stable/A-1+
Senior Unsecured	AA+

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors,