

What to do about Coverage—and how Gender Fits In?

by

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Part I: How to Increase Coverage

Why low coverage and low contribution density?

- We make old age schemes mandatory because many people may not save enough for old age
- Financed by contributions linked to benefits in hope they will not be viewed as tax, may not compete with other public goods
- But difficult to enforce contributions in low and middle income countries:
 - many self-employed, small firms, informal sector
 - limited government capacity
- So high correlation between stage of development and coverage or density of contributions
- Much concern about this in Latin America (Chile)³

But we should not exaggerate the coverage problem

- Education of younger women is much higher, therefore they participate in labor market, have higher contribution density than their mothers.
- Wives of covered men covered by joint pension
- We need to distinguish between non-contributors who are 1) myopic, 2) poor or 3) save other ways
 - Non-poor who save enough will be OK, may be better off saving some other way (flexible, liquid)
 - Myopic workers--don't save, avoid contributing by self-employment: mandate contributions and collect through income tax or license system
 - Lifetime poor: non-contributory public benefit needed--what form and how much?

Types of public benefits

- Minimum pension guarantee (for contributors only)
- Mean-tested benefits (universal)
- Flat benefit—
 - uniform benefit per contributor (Argentina) or
 - uniform payment per day worked (Mexico) or
 - universal uniform benefit for every old person (OECD)
- Combinations also possible

Minimum pension guarantee (MPG) for contributors

- Common in Latin America and Eastern Europe
- May encourage contributions by setting floor, protecting from financial market volatility
- But doesn't help poor who don't contribute
- Eligibility conditions are crucial policy choice
 - 25 years (Mexico) excludes most women, 10 years (Argentina's flat) is almost universal but costly, 20 years (Chile) discourages marginal work
 - benefit per year worked avoids on-off switch, gives partial protection to those who work few years
- Must be accompanied by some universal benefit to prevent poverty among non-regular contributors

Universal means-tested benefit

- Like MPG but takes all income into account and all old people are eligible
- Examples: UK, India, Australia, Hong Kong, PASIS in Chile, Costa Rica, Canada
- Can keep recipients above poverty line at lower cost than flat benefit, more inclusive than MPG (Very old women are major beneficiaries)
- But harder to administer than flat or MPG
 - mis-targeting, high transactions and bribery costs
 - disincentives to contribute and save
 - difficult to apply in extended family situation

Flat (uniform) benefit based on age

- Examples--Denmark, Bolivia, Kosovo, Mex. City; also New Zealand, Mauritius, Namibia, Botswana
- Designed to increase coverage, reach everyone
- Administration simple, diversifies income sources for all, less distortionary than means-tested benefit
- Higher cost-but reduce by small benefit, claw back from rich, high eligibility age indexed to longevity
- Most recipients aren't poor
 - inefficient anti-poverty method
- Is mandatory contributory pillar still needed?
Yes—otherwise many myopic old people will only have flat benefit--small pension

3 possible patterns for public pillar

- 1) MPG for contributors + smaller means-tested benefit for non-contributors (Chile but MPG proportional and PASIS better funded)
- 2) modest universal flat (OECD, Bolivia, Kosovo) for all (with high eligibility age indexed to longevity, claw-back)—replaces MPG+PASIS
- 3) smaller universal flat + MPG
- Different costs, incentives, protection, so depends on budget constraints and priorities
- As populations age, some countries shift from flat toward means-test or MPG to control costs (Nordics, Canada; UK too much)

Important design choice: Price vs. wage indexation?

- Price indexation--public benefit keeps up with prices; wage indexation--it keeps up with wages (higher due to productivity growth)
- Price index costs less and binds future govts less, but benefits becomes negligible in long run (UK)
- Wage indexation provides more protection to very old women and future cohorts but costs more and reduces discretionary spending of future govts
- Swiss indexation (50-50) a possible compromise
- Important to do long run cost simulations
 - Price indexation is unrealistic in long run but can be used in short run if starting benefit is too high (Sweden)¹⁰

One choice doesn't fit all.

Diagnostic questions:

- How are old people supported now?
 - if family system works, univ. benefit less crucial
- How many old poor compared with young poor?—if young families are poorer, use public budget to help young rather than old
- Is poverty concentrated or widespread?
 - if concentrated, means-test better than flat
- What is long run fiscal cost of each option?
- How does this rate with other fiscal needs?
 - if education and health system are under-funded, they may take priority so spend less on elderly
- Does country have administrative capacity to means test? fiscal capacity for universal flat?

Basic principles that always apply

- Finance public benefit by general revenues, not payroll tax, so doesn't depress employment, wages
- Avoid tax and benefit structure in public pillar that discourages contributions to private pillar
- Careful assessments of long term costs, distributional effects, budget capacity and priorities are essential

II. Gender issues

Why are women different?

- They work less, earn less, contribute less
- They live longer, are younger than husbands, become widows
- Very old women are often pockets of poverty

What is the impact of pension reform on women vs. men?

- Critics argue that close benefit-contribution link in new systems hurts women
- We studied this in Chile, Argentina & Mexico
 - We constructed synthetic work histories of representative men and women using hh surveys
- We applied rules of new and old systems to simulate future benefits for young workers
 - Average vs. 10 year vs. full career women
 - Women in 5 different educational groups
- Compared relative (not absolute) positions of men and women in new and old systems

Major results

- Women gained relative to men in Latin America
- Biggest gainers were:
 - low earners (low education)--public benefit
 - married and career women—joint pension
- Women get much smaller pension than men from contributory account
- But gain a lot from redistributive public benefit and joint pension requirement
 - husbands must leave 60-70% to widow
- Women lose from earlier retirement age. Pension would go up by 50% if ages were equalized at 65

Must take all parts of system into account

Different impact in transition economies (East & C. Europe)

- Wage inequality is growing, so accounts unequal
- Public benefits less targeted toward low earners
- Survivors' benefit reduced to save money
- Policies re joint annuities not yet clear
- Many single and divorced women
- Earlier allowable retirement age hurts women more in new systems than old systems
- Therefore new systems increase gender inequality in pensions in transition economies (also Sweden)
- The devil is in the details

Key design features for women

- Equalize retirement age for men and women—raises pension of women by 50%
- Require or strongly encourage annuitization
- Require joint pension and survivors benefits; let women keep own-pension+joint pension
- Require price indexation of annuities—otherwise very old women will be poor
- Split balance in accounts, upon divorce
- Unisex mortality tables?? Less important in context of joint annuities. (see next slide)
- Eligibility conditions for MPG matter a lot
- Women are major beneficiaries of flat or MT benefit, policies that increase coverage

Should unisex mortality tables be used for annuities?

- Uses same average mortality tables for M and W
 - For individual annuities, raises payouts to W
- Redistributes from men to women (not from rich to poor). Inefficient anti-poverty measure.
- Selection--may lead men not to buy annuities, insurance companies to try not to sell to women.
 - so may not be compatible with voluntary annuitization and competitive insurance markets
- With joint annuities, unisex and gender-specific tables yield similar payouts, selection disappears
- Not feasible with different retirement ages for M&W. Equal retirement age has bigger impact