

Factors Determining Enrollment in Contributory Pension Programs: Evidence from Latin America



World Bank-Hitotsubashi-MOF Workshop on
Closing the Coverage Gap
The Role of Social Pensions
MITA Kaigisho, Tokyo

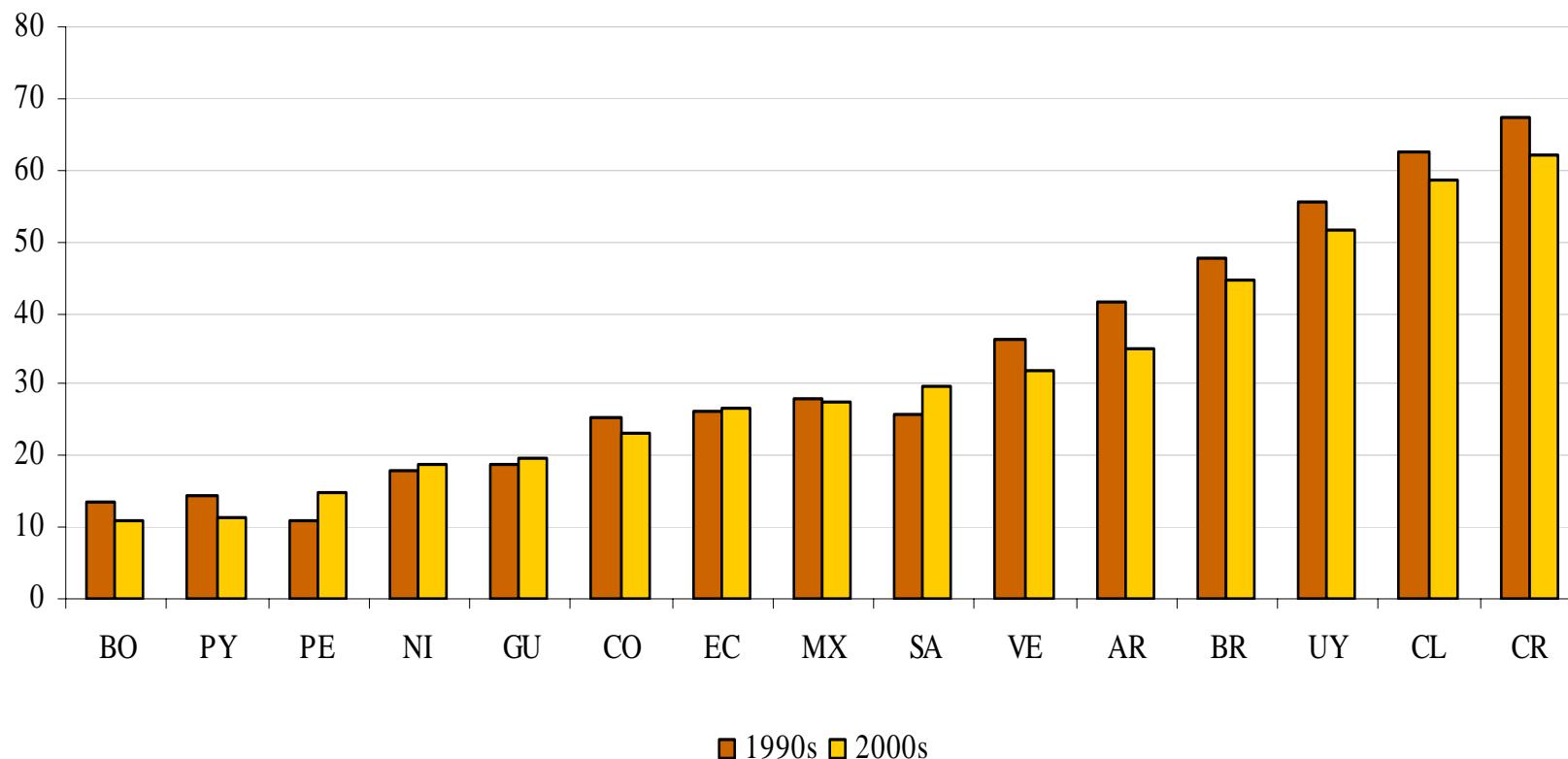
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The World Bank
February 22, 2008

Presentation Outline

- Context – Low Pension Coverage in Latin America
- Individual Determinants of Pension Program Participation
 - The Correlates of Pension Program Participation
 - Self-Reported Reasons for *Not* Participating
- Labor Market Determinants
 - Labor Informality in Latin America: “Exclusion” and “Exit”
 - Unintended Effects of Policy and Program Design
- Finding the Way Forward

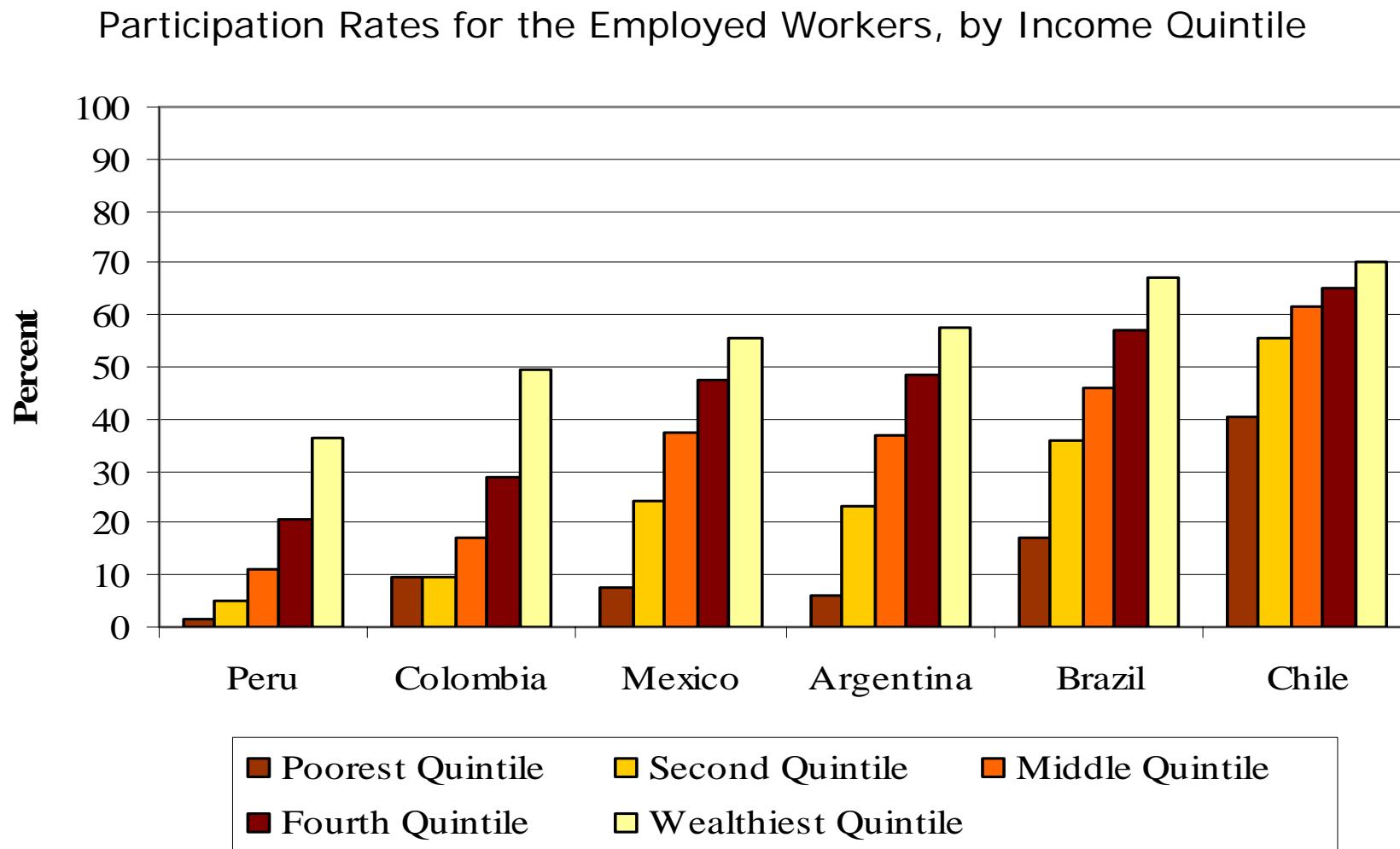
Participation in contributory pension programs remains low in Latin America

Participation Rates among the Economically Active Population,
1990s and 2000s



Source: Rofman and Luccetti (2006)

The working poor have significantly less access than the non-poor



Source: Adapted from Rofman and Luccetti (2006)

Correlates of Pension Program Participation: Argentina, Bolivia, Colombia, Dominican Republic

□ Individual-level

- Education + (AR, BO, CO, DR)
- Age + (AR, CO, DR)
- Male + (AR, CO) - (DR)
- Income[#] + (CO)
- Urban[#] + (CO)
- Ethnic Minority - (CO)

□ Job-level

- Self-employment - (AR, BO, CO, DR)
- Job Tenure (< 1 yr) - (AR, BO, DR)

□ Firm-level

- Firm size + (AR, BO, CO, DR)

□ Sector-level*

- Construction - (AR, CO, DR)
- Agriculture - (BO, CO, DR)
- Trade - (AR, DR)
- Transport/Comm. - (DR)
- Finance - (AR)
- Manufacturing - (CO)
- Public Admin. + (AR, BO)

Analyzed only in CO

* Omitted category manufacturing in AR, DR, industry in BO, and "other" in CO

The Main Reasons Informal Workers Say They Do Not Contribute to Pensions

| | Argentina | | Bolivia | | Colombia | | Dominican Republic | |
|-----------------------------------|-----------|------|----------|------|----------|------|--------------------|------|
| Reason | Salaried | S-E | Salaried | S-E | Salaried | S-E | Salaried | S-E |
| Cannot afford it | -- | 76.0 | 25.4 | 26.0 | 55.8 | 74.8 | 22.9 | 51.2 |
| Unaware of right/how system works | n/a | n/a | 42.1 | 55.3 | n/a | n/a | 5.2 | 19.4 |
| Employer only offered this job | 95.5 | -- | 23.7 | -- | 11.8 | 0.6 | 21.0 | -- |
| Employer does not require it | n/a | n/a | n/a | n/a | 13.4 | 1.3 | n/a | n/a |
| Most jobs are like this | n/a | n/a | n/a | n/a | 4.6 | 1.8 | 15.7 | -- |
| Lack of trust in system | -- | 4.3 | 6.9 | 15.4 | 2.0 | 6.2 | 2.4 | 5.6 |
| Prefers higher earnings | 4.5 | 1.7 | n/a | n/a | 1.7 | 1.3 | 11.8 | 1.8 |
| Children/spouse will look after | n/a | n/a | n/a | n/a | 0.3 | 2.1 | 0.6 | 10.1 |
| Too young | n/a | n/a | n/a | n/a | 3.8 | 2.4 | 5.0 | 3.4 |
| Prefers own savings | n/a | n/a | n/a | n/a | 0.8 | 2.5 | 4.3 | 2.3 |
| Not worth it | -- | 3.0 | n/a | n/a | n/a | n/a | 2.9 | 1.9 |
| Other | -- | 15.0 | 1.9 | 3.3 | 5.8 | 6.9 | 8.3 | 4.5 |

Source: Adapted from Perry et al (2007)

More Reasons for Not Contributing: Focus Group Findings from Bogotá, Colombia

- Low- and middle-income workers highlight the issue of *affordability*, their inability to make regular pension contributions given the levels – and variability – of their incomes
- Many indicated that, even if they were able to save, they would rather use the money for *more immediate needs*, e.g., investment in their own enterprise, housing, children's schooling, etc.
- Several highlighted a *preference for more flexible (voluntary) savings instruments* that could be used for either short- or longer-term needs
- Several respondents noted
 - A *lack of confidence* in the Government and skepticism that they would ever see their contributions (if made) in the future
 - *Concerns about fairness*, specifically that informal workers don't get matching contributions while formal employees do
 - A *lack of information and understanding* of how the pension system works and how to contribute

Informality in Latin America: “Exclusion” but also “Exit”

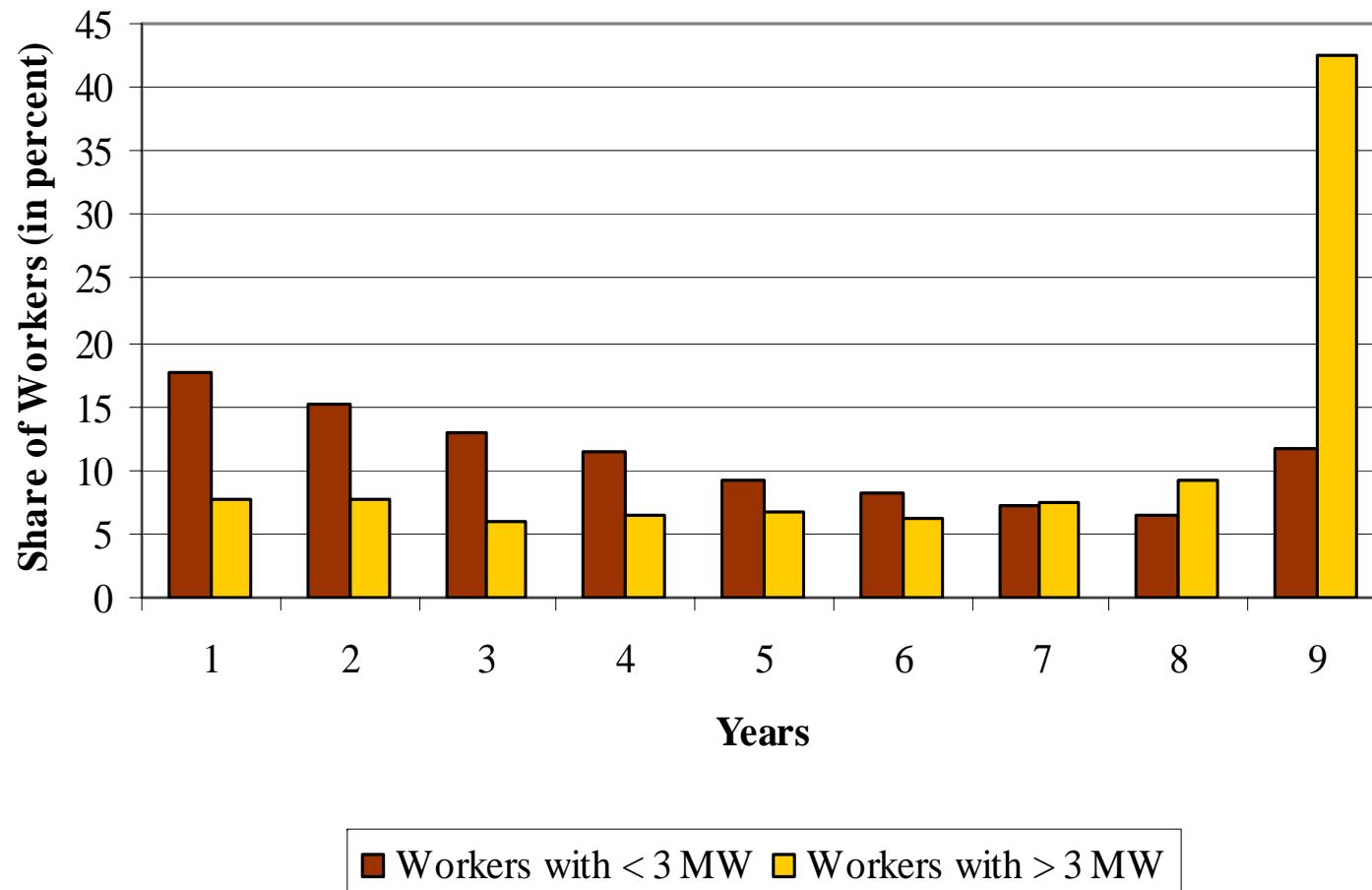
- In addition to understanding the individual factors, it is critical to understand the nature of labor informality if one is to understand why so many workers do *not* participate in contributory pension programs
- There is evidence supporting the traditional view that *some informal workers are excluded* from formal sector jobs (and, hence, largely from contributory pension programs) ...
- ... but the evidence also highlights that *many informal sector workers and firms “opt into” informality* (Perry et al 2007)
- Both “Exclusion” and “Exit” are *shaped by policy- and program-related factors* (e.g., labor regulations, the design of social security programs, etc.)

Unintended Effects of Policy and Program Design

- *Labor market policies* can induce informality, making pension access more difficult
 - High minimum wages (e.g., Colombia, Costa Rica)
 - High costs of payroll taxes (e.g., Colombia, Mexico)
- *Design features of social security* can raise the perceived costs and lower the perceived benefits of participation, e.g.:
 - Excessive “bundling” of benefits (not only pensions, health insurance and disability, but also childcare, housing benefits, training, sports and recreation facilities, etc.)
 - Rigid “one-size-fits-all” schemes (same rules for young and old, despite different preferences)
 - Lack of accounting for labor mobility in and out of the formal sector (onerous vesting periods)

Pension design is not consistent with patterns of labor mobility in-and-out of the formal sector (I)

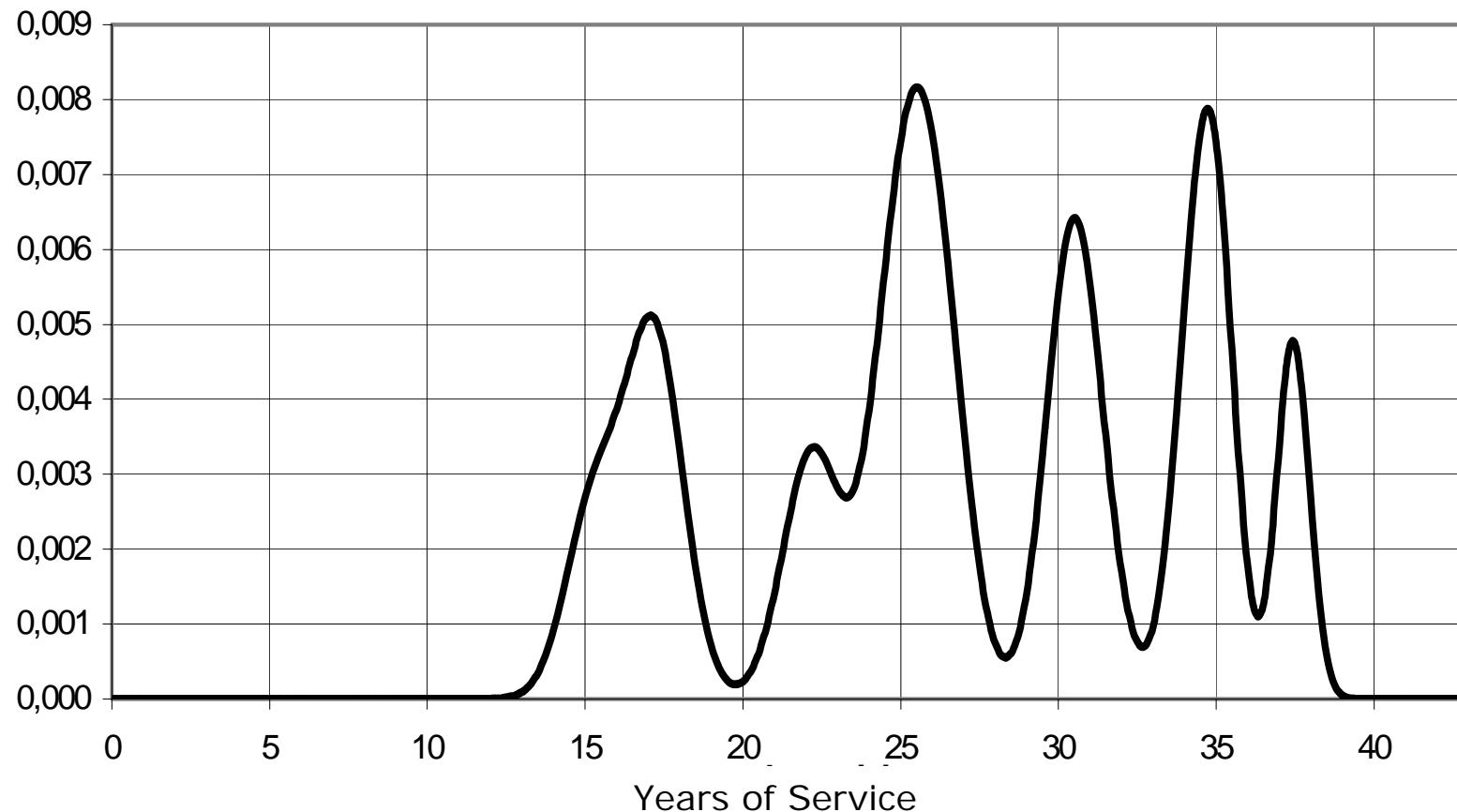
Distribution of Workers' Years Insured by IMSS, Mexico, 1997-2005



Source: Adapted from Razu (2006) as presented in Levy (2006)

Pension design is not consistent with patterns of labor mobility in-and-out of the formal sector (II)

Density function for years of formal sector work among 60-year olds in Uruguay
(accumulated from age 18 to 60)



Source: Bucheli et al (2006)

Finding the Way Forward

- Increasing pension coverage in Latin America, including among the poor, will require *a multi-faceted approach* that includes, but also looks beyond, the strengthening of contributory pension schemes
- Making progress will require *addressing the underlying causes of informality*, taking into account both forces of "exclusion" and "exit", e.g.:
 - Improving the labor market regulatory environment (e.g., high payroll tax burdens, minimum wages)
 - Addressing the program design issues that affect workers' (and firms' assessment of the relative costs and benefits of being formal (e.g., bundling and quality of benefits, rigid program rules, etc.)
- It will also require *confronting the critical barriers to pension participation faced by poor workers* – i.e., lack of ability to save, lack of knowledge about pensions, the need/desire for flexibility, etc.

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