Better **Pensions**, Better **Jobs**

Towards Universal Coverage in Latin America and the Caribbean

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Better Pensions, Better Jobs. Towards Universal Coverage in Latin America and the Caribbean

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- Diagnostic of pension coverage in the region
- A conceptual framework
- Study recent policy innovations
- Offer guidance for policy reform
Low pension coverage in LAC: 4 out of 10 among Pop 65+ do not get a pension

Pension Coverage in Latin America and the Caribbean, 2010

Source: Bosch, Melguizo, and Pagés (2013).

(National Household Surveys data)
The labor market at the epicenter of the challenge and the solution

Only 44.7% of workers in LAC contribute to a pension system

Source: Bosch, Melguizo, and Pagés (2013).

(National Household Surveys data)
Pension savings are low for non-wage earners, workers in small firms, or low-income workers ...
... but also for the emerging middle class

Pension savings: Contributors to the pension system in Latin America and the Caribbean by income decile, occupation and firm size, 2010

Source: Bosch, Melguizo, and Pagés (2013).
Pop $65^+$ will more than triple in four decades

Population projection for Latin America and the Caribbean, 2010–50

- Pop 65+ (2010) 38 million (6.8%)
- Pop 65+ (2050) 144 million (19.8%)

Source: Bosch, Melguizo, and Pagés (2013).

(United Nations and Celade projections)
Between 47% and 60% of adults 65\(^+\) (up to 83M) will not have an adequate pension

**Pension coverage gap in 2050**
(Percentage of adults over 65 without an adequate pension)

Source: Bosch, Melguizo and Pagés (2013)
This pension gap will have relevant consequences:

- **Social**: Families will need to devote greater effort to the care of the elderly.

- **Political**: Adults 65+ will make up between 20% and 30% of the potential voters.

- **Economic**: How coverage gaps are closed can have an impact on productivity growth.

- **Fiscal**: Lack of coverage represents (also) an implicit fiscal cost.
Informality is not an incurable disease

It is the outcome of:

- **Designs:** Systems exclude *(de jure or de facto)* non-wage earners.
- **Incentives:** Provided by the state in labor markets (including monitoring).
- **Value:** Placed by workers and firms on social security.

All this can be changed with *adequate policies*.
It’s possible to eradicate poverty in old age and to increase formal employment

**Increase coverage today**
- Social/universal pension
  - Anti-poverty
  - Sustainable
  - Efficient

**Secure coverage in the future**
- Formal jobs subsidies
  - Subsidizing SS contributions
  - Innovating in channels
  - Enforcement, information and financial literacy
Better pensions: Anti-poverty pension

- **Universal**: With age and residence criteria

- **Anti poverty**: 10%-20% of PIB per capita
  (in line with national poverty lines; 2010 poverty 65+: 19.3%)

- **Sustainable**: Inflation adjusted, with sound fiscal institutions and funding sources

- **Integrated**: Compatible with having contributory savings

It could eradicate old-age poverty (19% today)
Better jobs: Subsidizing formal employment

Formality could increase from 45% to 63% (10 p.p. higher than the statu quo scenario)

(State subsidy for all workers/firms equivalent to 50% of total social security contribution of one minimum wage)

Source: Bosch, Melguizo and Pagés (2013)
Better pensions and better jobs would cost annually on average for LAC 1.5% of GDP

Source: Bosch, Melguizo, and Pagés (2013).
Financing choice would depend on current and future tax revenues

Consumption taxes and pension and health contributions in Latin America and the Caribbean, 2012 (Percentage of GDP)

Nota: El dato de cotizaciones sociales incluye todos los aportes a pensiones y salud públicas y privadas de contribución obligatoria.
The time is now: financial and political economy challenges can be overcome

- **Demography**: The region is still young but the window of opportunity will rapidly close.

- **Financing**: Pension reform requires an increase in resources allocated to these policies, preferably from alternative sources (VAT, commodities).

- **Improvement in formal employment and productivity**: Pension reform is central to achieve both.

- **Political economy**: Formal employment is a central aspiration of the middle classes.
Research open questions

• **Savings**: prices vs. **channels**

• **Accounting** pension implicit debt:
  • IPD
  • Pension coverage gap and non-contributory pensions

• **Taxes** and informality: Level and composition (VAT, Commodities), other institutions
Taxing labor in Latin America and the Caribbean

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Cost of formality in selected economies in LAC
(Percentage of wages)

Source: Pagés (2010)

Do non-labor costs (especially taxes) explain informality?
Which is the tax burden faced by diff types of workers?
Taxing labor in Latin America and the Caribbean

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Source of Income

- Employees
- Independent Workers

Household Composition

- Single
- Married with 2 children*

Levels of Income

- Fixed Annual Income
  - US$ 6,000
  - US$ 12,000
  - US$ 60,000
  - US$120,000

- Deciles
  - Third
  - Sixth
  - Ninth

- Minimum Wages
  - ½ Minimum wage
  - 1 Minimum wage
  - 2 Minimum wage
  - 2 > minimum wages

Composition of the Wedge

1. Income Tax; 2. Public and Private Social Security Contributions; 3. Compulsory health schemes; and 4. Regulatory costs (firing costs, holiday costs)

* Under the assumption that only one of the spouses receives income in the household