Alberto Arenas de Mesa and Claudia Robles, *Non-Contributory Pension Systems in Latin America and the Caribbean: Towards solidarity with sustainability*

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Central arguments of the book

• The authors’ arguments
  • Non-contributory pensions are an effective public policy in reducing old-age poverty and inequalities, particularly gender inequalities
  • Thus non-contributory pensions have an important place within the pension system on their own merits
  • They suggest that initially non-contributory pensions should cover the poorest 40% of the elderly population

• My argument: the advantages of non-contributory pensions are no accident. The design is
  • Good economics
  • Good social policy
  • Good politics
Message 1: Non-contributory pensions work (reprise)

- Coverage of non-contributory pensions in LAC (Arenas de Mesa and Robles, 2024)
  - 2000: 1 million people, 3.4% of elderly LAC population
  - 2022: 20 million people, 31%
  - 2023: 28 of the 33 countries in LAC has some sort of non-contributory pension

- Poverty relief: in Chile
  - The solidarity pension system reduced elderly poverty from 23.5% to 14.8% between 2006 and 2009 (Vila and Yanes, 2024)
  - In 2020, the non-contributory pension system reduced elderly poverty by 5.7% (Arenas de Mesa, Espíndola and Vila, 2024)

- Spending on non-contributory pensions, %GDP
  - 2000: 0.15%
  - 2021: 0.42%
  - Target: 2035: 1.1%
Social and economic advantages

• Social policy: important advantages in terms of adequacy, coverage and gender equity (more below)

• Ministry of Finance: multiple levers to maintain sustainability (more below)

• ‘The case for social pensions’, Jobs and Development Blog, World Bank, 9 December 2013
Advantages in terms of gender

• The Bravo Commission found that women in Chile face a quadruple disadvantage
  • On average their annual earnings are lower
  • On average they have fewer years of paid employment: 71 per cent of men aged 15 or more are part of the formal labour force, only 48 per cent of women
  • The age at which pension contributions cease to be mandatory is lower for women than for men; men retire from the labour market at an average age of 68.1 years, women at an average age of 62.4 years
  • Annuities are based on separate life tables for men and women

• Non-contributory pensions are a powerful way to reduce the gender pensions gradient
Wider advantages (reprise)

• A study of Brazil and South Africa, the countries with the largest non-contributory pension plans, found that

  • ‘...the poverty headcount and the poverty gap would be appreciably higher for households with older people. The impact on the poverty gap is much larger for the poorer households. The programmes significantly reduce the probability that individuals in households with a pension recipient will be in poverty’

• Family poverty relief via Grandma

  • In South Africa, Duflo (2012), ‘finds that girls who live with a grandmother who receives the pension are heavier than those who live with a grandmother who is not quite old enough to receive the pension.... In contrast, no such effect is found when the pension is received by a man’
Message 2: That success is no accident

• Successful policy rests on a tripod of skills
  • Strategic policy design
  • Political implementation
  • Technical implementation

• All three hold of non-contributory pensions
  – Strategic policy design: non-contributory pensions
    • Fill gaps because in the face of informality contributory benefits do not work well (the world has changed)
    • Are well targeted (more below)
  – Political: popular across the political spectrum (more below)
  – Technical: easier to implement than contributory plans: need to establish a person’s age and residence but not their employment history
Ways of targeting benefits

Poverty relief should aim to assist

• *All* the poor, i.e. avoid gaps in coverage (horizontal efficiency)
• *Only* (or mainly) the poor, i.e. avoid unnecessary spending (vertical efficiency)

• Different mechanisms
  • Income testing
  • Indicator targeting

• A common but mistaken argument is that unless a benefit is income tested it is badly targeted

• The mistake is sufficiently important that it is worth explaining carefully
Income testing

• Method: identify poor people via their income
• Advantages: can target tightly
• Disadvantages
  – Adverse incentives to labour supply and/or saving
  – Incomplete coverage: low take-up because of
    • High compliance costs for applicants
    • Stigma through receipt of benefits or through application process
  – Administratively demanding and costly
• BIG mistake to think that income testing is the only way to target well
Indicator targeting

• Method: identify poor people via indicators other than income

• Example: assume that
  • Only redheads are poor
  • All redheads are poor
  • There is no hair-dyeing technology

• Thus a redhead benefit will
  • Eliminate poverty by covering all the poor, i.e. no gaps
  • Pay benefits only to the poor, i.e. no leakages
  • Do so administratively cheaply since the colour of someone’s hair is easy to see; and
  • Avoid adverse incentives (no hair-dyeing technology)
Properties of the ideal indicator

• Highly correlated with poverty, to avoid gaps and leakages
• Outside the individual’s control, to avoid adverse incentives
• Easily observable and easily measurable for operational reasons
Conclusion
Good economics

• Adequacy and coverage
  – Age (old, young) is
    • Highly correlated with poverty
    • Outside the individual’s control
    • Easily measurable
  – Thus non-contributory pensions and child benefit
    • Are well (though not perfectly) targeted
    • Can be designed to fit different budget envelopes

• Sustainability: multiple levers
  • The level of the monthly benefit
  • The age at which the benefit starts
  • Whether there is an income or affluence test
Good social policy

• Non-contributory pensions
  • Strengthen poverty relief in terms of coverage and adequacy
  • Help to reduce inequality
  • Provide insurance against shocks
  • Lead to a considerable gain in gender equity
  • Broader social benefits, e.g. family poverty relief via Grandma
  • Share risk with taxpayers and hence via government borrowing intergenerationally

• Coverage
  • 2000: 1 million people, 3.4% of elderly LAC population
  • 2022: 20 million people, 31%
  • 2023: 28 of the 33 countries in LAC has some sort of non-contributory pension

• Poverty relief: multiple examples of success, including Chile, Brazil, South Africa
Good politics

• The strong and widespread political support for non-contributory pensions is not surprising
• The benefit has the economic and social advantages just outlined
• In addition non-contributory pensions and child benefit (i.e. a form of Universal Basic Income for the old and young) has support
  • From the political ‘right’, as reducing what they see as the stranglehold of in-kind benefits under the welfare state
  • From the political ‘left’ as giving people some income as a right of citizenship
References

Barr, Nicholas (2013), ‘The case for social pensions’, Jobs and Development Blog, World Bank, 9 December
Addenda
What’s the problem

• Structural shortcomings of contributory systems
  • Limited coverage, in large part because of informality leading to incomplete contribution records
  • Impact of bad DB design, e.g. regressive (more below)

• A changing world: declining coverage of contributory plans based on a worker’s employment status
  • Increased diversity of labour market relations, both LMICs and OECD countries
  • Implications: convergence between OECD countries and LMICs; contributions via a person’s employment status no longer generates the coverage it once did