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