

The experience with defined contribution schemes in Latin America

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International Seminar on Pension
System of China and Latin America
CASS - BBVA

Beijing

July 13th 2010

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I. The introduction of social policies in Latin America

Public PAYG pension schemes were introduced very early in the 20th century in Latam.

Demographic changes, actuarial unbalances, unrealistic social outcomes, political interests, inadequate management, lack of transparency and economic crises (especially in the 70s and 80s) shaped a very weak system at the end.

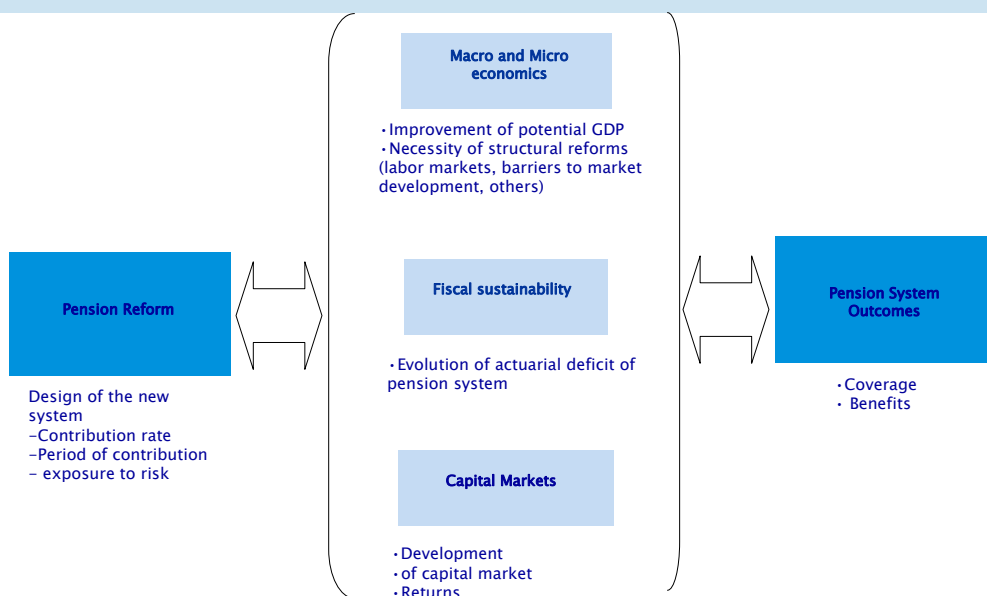
- Many benefits with generous payments
- No relation between contributions and pensions
- Unpaid contributions by private and government employers
- Pensions were given in generous amounts without taking into account fiscal sustainability
- Pension parameters such as retirement age, years of contribution, contribution rate and others were not adjusted on time for economic and demographic changes
- Low and negative returns
- Pension funds were used for other activities such as infrastructure, health programs and current government expenses.
- High administrative costs
- Fiscal and political pressure
- Actuarial and financial imbalance

II. Defined Contribution schemes in Latin America

Pension Reform in Latam = Parametric Changes + Structural Changes (Introduction of DC)

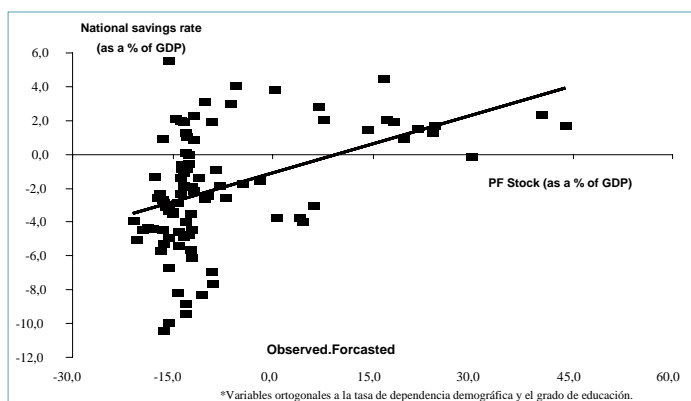
	Social component	Mandatory DB	Mandatory DC	Voluntary DC
Objectives	Social	Redistribution + insurance	Saving + insurance	Saving + insurance
Administration	Government	Government	Private sector	Private sector
Financing regime	National Budget	PAYG	Individual capitalization	Individual capitalization
Benefit	Basic pension	Minimum pension	Pension as a function of saving	Pension as a function of saving
Financing	Government	Contributions + Government	Fully-funded	Fully-funded

III. Goals and outcomes: a new pension system and the interaction with other factors



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Macro and microeconomics



A 10 percent increase in the size of the pension funds has an impact of one tenth in aggregated savings.

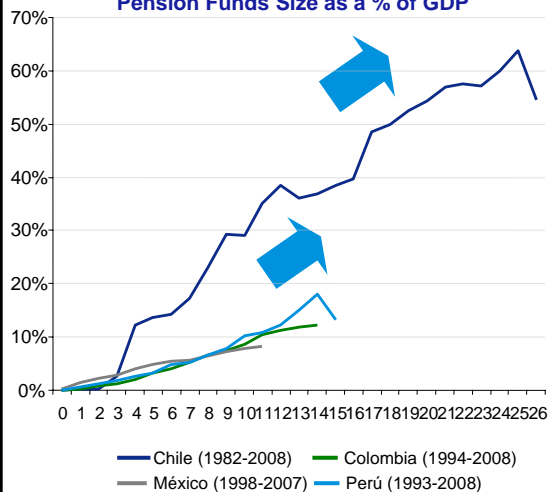
Corbo y Schmidt-Hebbel (2003) found that a one percent point increase in pension funds, relative to GDP, has an impact between 1 and 5 points of GDP in savings.

Growth is a fundamental factor behind savings and financial market development

III. Goals and outcomes: a new pension system and the interaction with other factors

Capital Markets

Pension Funds Size as a % of GDP

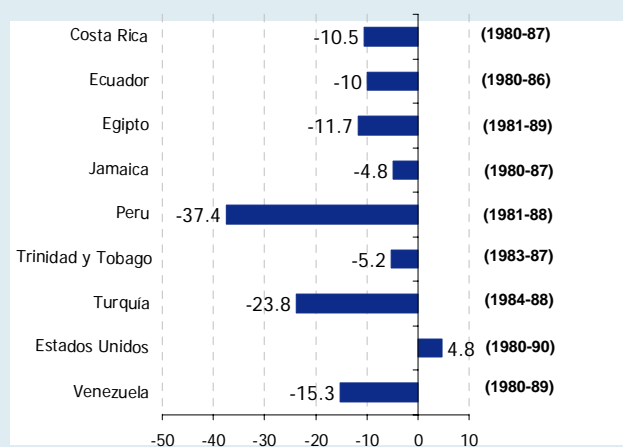


Country	Average return %		
	The first 10 years	From the beginning of the system	2009
Chile (1986)	10,4	9,1	13,4
Colombia (1994)	11,5	10,1	9,3
México (1998)	7,2	7,2	2,5
Perú (1993)	7,2	9,0	12,7

III. Social policies in Latin America: the introduction of PAYG schemes

Capital Markets

Real return of PAYG schemes in the 80s



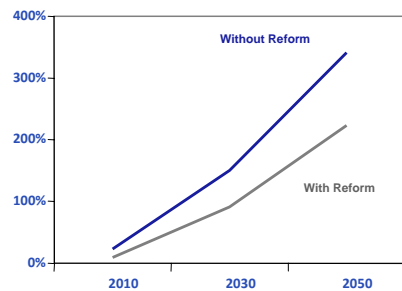
Source: World Bank. 1994: "Envejecimiento sin Crisis"

III. Goals and outcomes: a new pension system and the interaction with other factors

Fiscal sustainability

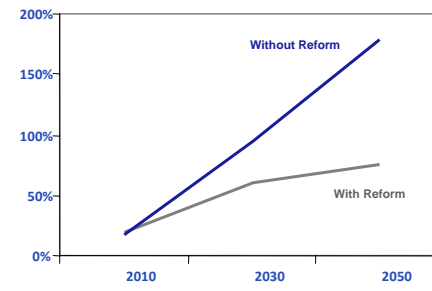
Estimated pension deficit with and without reform, as a % of GDP

Colombia



Source: Zviniene & Packard 2004

Chile



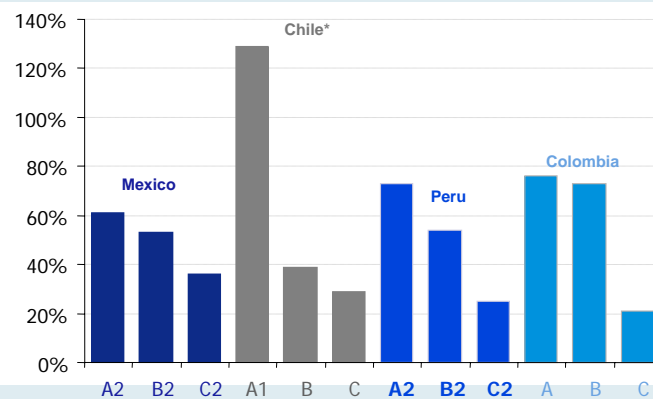
Source: Zviniene & Packard 2004

The reforms significantly reduced the pension deficit in several countries. The amount depends on the models used and on other reforms.

III. Goals and outcomes: a new pension system and the interaction with other factors

Replacement Rates

Replacement Rates

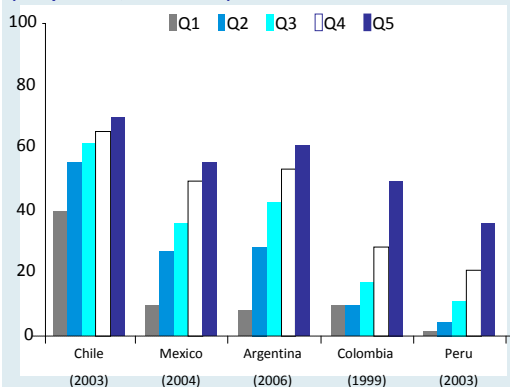


* Men

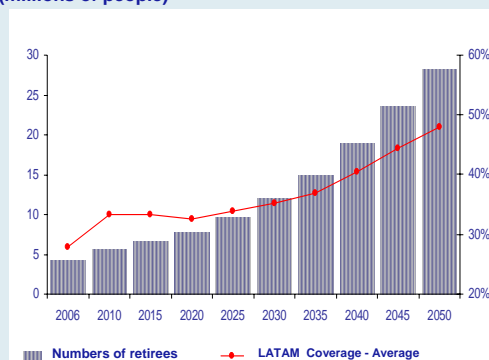
Goals and outcomes: a new pension system and the interaction with other factors

Pension Coverage

EPA coverage by quintiles
(Q1=poorest, Q5=richest)



Latam Average
(millions of people)

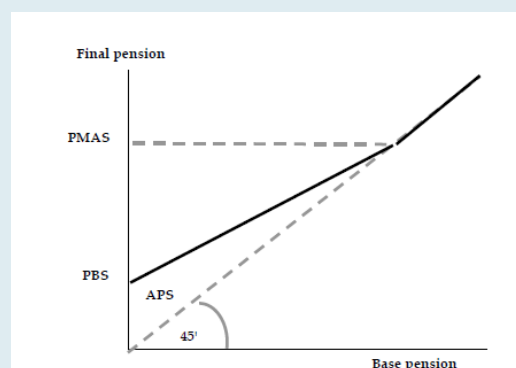


The problem of informality in Latin America

Goals and outcomes: a new pension system and the interaction with other factors

The pursuit of a universal scheme

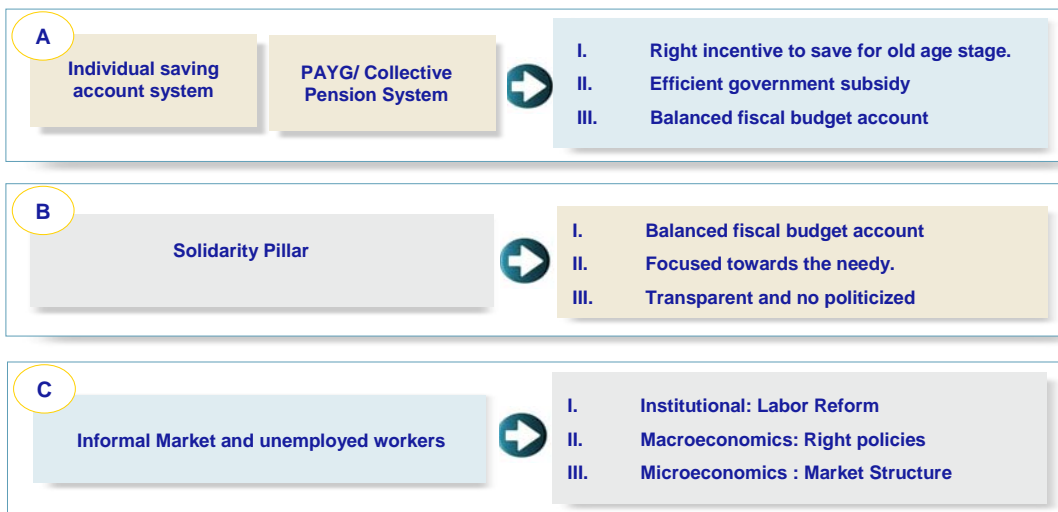
Reformed old age pension system in Chile 2008



Fiscal sustainability is a pre requisite for success

IV. Lessons from the Latin American experience

Important aspects to take into account



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