

*Background Note for the World Bank 2012–2022 Social Protection and Labor Strategy*

## The World Bank in Pensions

Pensions and social insurance programs that address the risks of death, disability and old age faced by all households are an integral part of any social protection system.<sup>1</sup> The dual objectives of such systems are to provide *protection* against poverty and *prevention* of a sharp decline in income when these life-cycle events take place.

In the World Bank's conceptual framework, *coverage*, *adequacy*, and *sustainability* are the three objectives that take precedence and where the challenge is to achieve what is often a difficult balance. At present, coverage gaps are responsible for a huge proportion of the growing elderly population being unprotected. In low income countries (LIC), roughly one in ten workers contributes to a pension program and more than three-fourths of elderly people do not receive pension income or cash transfers of any kind. This proportion has remained stagnant for decades, despite substantial growth in per capita income.<sup>2</sup> In middle income countries (MIC), coverage expansion has stalled or even declined.

The Bank's safety net agenda is part of the policy response to this gap, with broader social assistance programs covering the elderly and disabled in such countries as Brazil and Mexico. The Bank also is supporting cash transfer programs aimed specifically at the elderly (and often, widows and the disabled) in countries such as Maldives and South Africa. Going forward, further analysis is needed, especially in terms of implementation details and increased coordination between the Pension and Safety Net teams to better understand the intersection of these two important aspects of social protection.

There is much less experience, both within and beyond the Bank, with promoting voluntary pension coverage for workers outside the formal sector. The Bank has been a leader in assembling ideas and actions to

**World Bank Publications and Workshops**

The book entitled *Closing the Coverage Gap* was published by the Bank in 2009; it aimed to bring together the conceptual knowledge and select case studies of approaches to reform measures.

In June 2011, a workshop was held to compile further information on approaches to so-called Matching Defined Contribution Schemes; a volume that summarizes the insights of the workshop will be published in 2012.

respond to this vacuum. Going forward, there is a need for further study of country experiences that are only now unfolding in places such as China, India, and Kenya. The Bank will continue to advise on policy for LICs with regard to the relative emphasis on and coordination between policies to expand sustainable contributory pensions and social assistance programs as part of a long term pension strategy. These two approaches need not be substitutes but can be viewed as complementary elements of a long run strategy. Adequacy of contribution-based pensions is directly related to coverage in that many workers participate in these schemes for only part of their careers resulting in relatively low benefits.

*This note is based on Dorfman, Mark and Robert Palacios. 2012. "The World Bank in Pensions: A Background Paper for the Social Protection Strategy." Social Protection & Labor Discussion Paper No. 1208. World Bank. Washington, D.C.*

<sup>1</sup> In addition, social insurance programs often insure against unemployment, work injury, and illness. Dorfman, Mark and Robert Palacios. 2012. "The World Bank in Pensions: A Background Paper for the Social Protection Strategy." Social Protection & Labor Discussion Paper No. 1208. World Bank. Washington, D.C.

<sup>2</sup> Based on World Bank pension database covering 78 LICs, there were about 100 million contributors from a labor force of almost 900 million or about 11 percent.

This is particularly true for low income workers that shift between the formal and informal sector as well as for women who tend to spend a greater share of their working age period caring for children and the elderly. Adequacy also is an issue when non-contributory pension levels are too low.

Pension policy involves multi-decade commitments and creates long term liabilities. Broadly speaking, the policy variables involved in sustainability are those of benefit design and financing. Benefit parameters can be adjusted, for instance, by linking retirement to life expectancy; and technical assistance and modeling can inform financing by reviewing the impact of different changes on pension system finances, the adequacy of benefits, and the indirect impact on the economy. These ongoing challenges require the improvement and application of existing tools such as APEX and PROST.

In order to achieve these three objectives, good institutions and systems are key. This includes improved administration to track beneficiaries, deliver their benefits, and maintain accurate individual account records. In some cases, it includes addressing duplication and fragmentation of programs. For fully- and partially-funded schemes, it involves effective supervision of private actors and strong fiduciary arrangements for public fund managers. These funds are often very large relative to the economy and to other domestic investors, with implications beyond the pension system. In these areas of fund management and governance, there is a particular need for coordination between the Bank's Social Protection and Financial Sector staff.

Specific areas where further investment in knowledge products and tools is needed include:

- Old-age poverty, informal support, and pension systems in LICs, especially in Sub Saharan Africa.
- Innovative mechanisms to expand voluntary coverage for social insurance programs and voluntary pensions savings arrangements, with closer SP and Health collaborations.
- Approaches to dealing with coverage of migrant workers both internal (often rural–urban as in

### Leveraging the World Bank's Tools

The capacity to provide such assistance can be enhanced through further development and dissemination of the micro-simulation and actuarial projection tools such as the Analysis of Pension Entitlements across Countries (APEX) model and the Pension Reform Options Simulation Toolkit (PROST). The latter already has contributed to Bank operations and technical assistance efforts in dozens of countries.

In addition, the lessons from international experience can be synthesized as part of the Bank's knowledge management and training and provided to policymakers to inform these decisions. Through policy lending, the Bank also can provide budget support to recognize governments willing to tackle difficult structural reforms.

Brazil and China) and international (Asian migrant workers in the Gulf countries).

- Evidence so as to better advise our clients on the possible role of social pensions, where collaboration with the Safety Net team is critical.

In addition, there are potential areas of collaboration with partners to develop standards for reporting key indicators for financial sustainability and coverage, along with other useful indicators of the performance of pension systems. The collaboration with the Organization for Economic Co-operation and Development (OECD) and the Inter-American Development Bank (IADB) to produce APEX indicators for Latin American countries is an existing example. There is also the potential for joint efforts with the International Labour Office (ILO) and International Monetary Fund (IMF) regarding measurement and reporting of unfunded pension liabilities and better data quality and management information systems for social insurance agencies. Producing internationally comparable indicators and a robust framework for measuring progress will contribute to operational support as the World Bank and other donors increasingly focus on results.

