Book Review

Lessons from pension reform in the Americas

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This volume contains a series of interesting articles dealing with the way pension reform has been discussed and implemented in parts of the American continent. Although there are articles looking at pension reform in the United States and Canada, the focus of this book is directed towards the countries of South America. Particular attention is paid to the extent to which the introduction of individual savings accounts in certain South-American countries has led to a sustained increase in contributions actually paid into these accounts, and therefore the extent to which this has actually promoted pension savings.

The Americas do seem to hold general lessons for pension reform in this respect. Chile, for example, blazed a trail here by introducing individual, funded defined contribution accounts as far back as the 1980s. Other countries in Latin America have since followed suit, and in the United States a commission was set up in 2005 to look at the feasibility of introducing individual savings accounts along similar lines (although for political reasons not much has yet come of this). Lessons learned in this part of the world regarding pension reform should therefore be of wider interest to all those grappling with the intricacies of pension provision, and this book provides a worthwhile contribution.

And as if to reassure any readers who might be tempted to dismiss this book as being of regional interest only, the editors make the point themselves, noting in the Preface that: ‘The Americas have been the site of the world’s most

significant pension reforms. The analyses presented here by leading experts provide valuable insight as governments everywhere consider how best to proceed with pension reform’.

The individual articles are all very thorough, and perhaps this betrays the background of the book’s editors. They both have backgrounds in research. Stephen Kay is the coordinator of Latin America analysis in the Research Department of the Federal Reserve Bank of Atlanta. Tapen Sinha is, among other things, the ING Chair Professor at ITAM, Mexico and the founder and director of the International Center for Pension Research. The authors of the individual chapters are also for the most part academics, with an emphasis on public policy and economics.

The book is divided into two parts, which together contain 16 chapters. The first part deals with system design and implications, whereas the second part focuses on the individual country studies. The first part is an interesting mixed bag, including a chapter on Chilean pension reform, but also looking at such diverse topics as gender inequality and its relevance to social security reform and the impact of default options on retirement saving. The second part contains studies looking at Canada, Mexico, Brazil, Costa Rica, Peru, Uruguay as well as Argentina. In addition, as mentioned above, there is a chapter on the Presidential Commission on Social Security Reform in the United States.

The chapter on Chile provides the backdrop to the individual country studies. It shows how Chile's PAYGO state pension was stabilised by raising retirement ages, increasing contribution rates and eliminating certain special schemes. From 1980, the Chilean government then introduced a new system of funded, defined contribution individual accounts. The authors conclude that the reforms have not been a failure, but that more needs to be done to ensure that Chilean workers obtain optimal results from their individual savings accounts. Greater financial literacy would enhance contribution and investment patterns.

But it is the chapters dealing with the experiences of some of the other countries that are equally worth looking at. A careful conclusion from these chapters might be that the introduction of a strong, individual savings component alone will not 'solve' the problem of a savings deficit. Many of the South-American countries that have followed Chile's lead seem to have found that more yet needs to be done beyond introducing individual saving opportunities if people are to have a prudently financed retirement. A good example of this is the chapter on Mexico: as in Chile, the new system of voluntary accounts was supposed to encourage workers to contribute. Many low-income individuals in particular do not have enough money in their accounts to finance their retirement, and it seems that those people that are contributing are the ones who can get some immediate tax breaks from doing so. The country

studies on Peru and Uruguay show similar experiences.

Canada, on the other hand, which did not base its pension reform largely on individual savings accounts, but instead strengthened its supplementary state pension system, the Canada Pension Plan, seems to have avoided some of the problems faced by the South-American countries. Does this mean that 'privatising' pensions might paradoxically lead to falling savings ratios?

The authors do not support such a pessimistic conclusion, but some general lessons need to be learnt. These are usefully discussed in an epilogue, which makes it clear that more must be done to ensure that people start saving at a young enough age. In addition, each country needs to examine what is required to finance the minimum benefits that have to be paid. Third, all countries need to examine how to make best use of the financial (capital) markets to guarantee the optimal results for pension investments. Finally, more microeconomic, household-based data are required to help policymakers devise solutions to ensure better saving for retirement.

This is an interesting volume with thought-provoking studies. Everyone, in whatever jurisdiction, who takes more than a passing interest in the problems surrounding retirement provision, will find it worthwhile to peruse this book as a contribution to the ongoing pensions debate.

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