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Models of Development, Social Policy and Reform in Latin America

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Introduction

Latin America is one of the regions in the world that has experimented with more development models, in addition, it has been at the forefront in social policies and a pioneer in market-oriented reforms in both areas. From the 1950s to the end of the 1970s most countries in the region followed a mixed model of development characterized by the predominance of the market but with significant state control and intervention. At the start of the 1960s Cuba took a dramatic leap to the state, introducing a fully socialized economy with central planning. Conversely, in the mid 1970s Chile took the opposite direction with a drastic economic reform that followed neoliberal ideas and moved that country to the market. The latter approach influenced policies of the major international financial organizations and has been eventually applied in most of the region.

Some Latin American countries also introduced the welfare state in the continent--the first two being Uruguay and Chile in the 1920s-- and gradually developed to a zenith in the early 1970s. Cuba began this process in the 1930s and consolidated and significantly expanded it in the 1960s and 1970s. Costa Rica's foundations of the welfare state were laid down in the 1940s, consolidated in the 1950s, and expanded in the 1960s and 1970s. Chile was not only a pioneer in both the reduction of the state and market-oriented reform, but also in the process of "privatization" of social services at the start of the 1980s. The severe economic crisis suffered by the region in that decade weakened the welfare state and the Chilean path was partially or fully followed in the 1990s.

This chapter analyzes two important topics on development and social policy in Latin America: (I) the relationship between goals and means in three different models of development in the region: Chile (market), Cuba (statist-socialist) and Costa Rica (mixed), and the socioeconomic performance of these three models; and (II) the reform of the welfare state in Latin America, particularly of its major component social security, and its effects on the people and development.

The following important questions will be addressed in this chapter: (1) are developmental goals (growth versus equity) and means (market versus state) conflicting or compatible and, if the latter is true, what is the optimal combination between them?; (2) which of three models of development have had the best socioeconomic performance and why?; (3) what is the nature of the reform of social welfare (security) and which have been the roles of the state and the private sector?; and (4) which have been the effects of the reform of social welfare (security) on crucial issues such as population coverage, income distribution, fiscal and administrative costs, capital accumulation and markets, and national savings?.

Three Models of Development in Latin America and Their Results

Goals (Growth versus Equity) and Means (Market versus State) Dichotomies

Mkandawire's chapter "Social Policy in a Development Context" accomplishes three significant tasks: (1) comprehensively reviews the literature on the relationship between social welfare and economic development; (2) demonstrates that the negative view of conflicting developmental goals and means (equity versus economic growth/efficiency and state versus market) is returning to the initial positive view that the two may work to reinforce each other; and (3) properly concludes that social policy is a key instrument that works in tandem with economic policy to ensure equitable and socially sustainable economic development.

In addition, Mkandawire sets a research agenda that includes the following needs: (1) explore the empirical linkages that tie together distinct goals and means; (2) bridge the hiatus between theoretical and empirical findings and social policy making; (3) work on more time series analysis using institutional and historical information to heighten research now largely dominated by cross-section and panel data regression analysis; and (4) study the policy implications of different economic, social and political settings.

Dreze and Sen have convincingly argued that the traditional *total* dichotomies of goals and means are false because there are major complementarities between the two pairs of goals/means, and it is important to strive for a balance and avoid extremes. The dilemma in the use of available resources is not between all and nothing but to give *preference* to one goal *complemented* by the other, and properly combine state and private action with other mechanisms (Dreze and Sen 1989).

Three Different Models of Development in Latin America

My latest book applies Dreze-Sen's view and addresses several of Mkandawire's research concerns (use of historical and institutional information, exploration of the linkages between goals and means, evaluation of policy implication of diverse socioeconomic-political settings) to compare three different models of development in Latin America (Mesa-Lago 2000d):

1. Chile. The best and most radical example of the neoliberal market model, particularly under the Pinochet regime (1973-1990), which drastically reduced the role of the state and gave too much a preponderance to growth, stability and efficiency (largely based on privatization), but restricted social policy to a residue or trickled down effect. Such imbalance has been gradually corrected by three successive democratic administrations (1990 on) which, although maintaining the essence of the previous economic model, have

placed higher accent on social policy under the more balanced approach of a "social market economy" (see also Ruiz-Tagle 2000).

2. Cuba. The only example in the region (and one of the few remaining in the world) of the statist, centrally- planned socialist model, which virtually eliminated private ownership of the means of production and placed excessive emphasis on social goals and equity--even egalitarianism in certain stages-- but at the cost of efficiency, productivity and growth (1959-1990). The collapse of the USSR/socialist camp and the severe economic crisis that ensued in the 1990s, has forced a timid market oriented reform which, despite significant government efforts, is threatening some of the previous social achievements (see also Barraclough 2000).

3. Costa Rica. One of the best representatives of the mixed model, which combined a market economy with a considerable state role, and achieved a fair balance between social and economic goals with good results in both (1953-1981). But the debt crisis of the 1980s and the exhaustion of that model (excessive state intervention and fiscal imbalances) led to structural adjustment reforms in that decade and in the 1990s, albeit so far successful in maintaining the most important social gains (see also Mesa-Lago 2000a).

The first two models were extremes: Chile overemphasized the market and economic goals while drastically reducing state functions and social goals, while Cuba did exactly the opposite; Costa Rica managed to fairly balance goals and means. But adjustments have been occurring in the three countries: toward social goals and more state regulatory powers in Chile since the 1990s; toward economic goals and a timid move to the market in Cuba since the 1990s (still with overwhelming state ownership and control); and toward economic goals and the market in Costa Rica since the 1980s. Finally the three diverse economic models have been implemented by different political systems: a military dictatorship in Chile (followed by multiparty democracy), one-party authoritarian socialism in Cuba, and a multiparty democracy in Costa Rica (Mesa-Lago 2000d).

The three countries selected are also important examples in Latin America of a relatively early emphasis on social policies, thus ratifying Pierson's observation that "late starters (in industrialization) tended to develop welfare institutions earlier in their own individual development and under more comprehensive terms of coverage" (cited in Mkandawire 2000: 11). Chile and Cuba were two of five regional "pioneers" in the development of social insurance (respectively in the 1920s and 1930s), while Costa Rica's program started later (in 1943 but this country was less developed that the other two) and yet it was expanded in 1960-1970s and reached the level of the other two counterparts. By the 1980s, the three countries had basically accomplished universal coverage of their

populations although with diverse schemes (Mesa-Lago 1998). The three countries were selected for a UNRISD comparative study that analyzed the unique experience of seven countries that achieved levels of social performance considerably higher than their per capita income (Ghai 2000). The socioeconomic performance of the three models is summarized in the next section.

Socioeconomic Performance of the Three Models

Twenty indicators of development were selected to measure the socioeconomic performance of the three countries and historical statistical series elaborated for 1960-1993 (in Chile the relevant period started in 1973). About half of the indicators dealt with *economic* variables, both internal and external: GDP growth, GDP per capita, investment, inflation, fiscal balance, composition of GDP by economic sector, export concentration/ diversification, import composition, trade partner concentration/diversification, trade balance per capita, and foreign debt per capita. The other half of the indicators dealt with *social* variables: real wages, composition of the labour force by sector, open unemployment, illiteracy, educational enrolment at three levels, infant mortality, rates of contagious diseases, life expectancy, and housing. Five important social indicators had to be discarded in the final evaluation because of two reasons: lack of data from Cuba (income distribution, poverty incidence) or significant differences in the way those indicators were calculated (women's participation in the labour force, access to water and sewerage/sanitation, social security coverage).

Two types of ranking were used in each of the indicators: (1) *absolute*, measuring the starting and ending years in the period, for instance, the infant mortality rate in 1960 (or 1973 for Chile) and 1993; and (2) *relative improvement*, the change in one indicator through time, for instance, the reduction in infant mortality between 1960/73 and 1993. The indicators were merged in each of the two clusters (economic and social), and the two clusters then combined into an index of economic and social development (using various weights).

The results of these comparisons in the absolute rankings among the three countries were as follows: Chile ranked best (first) in economic indicators but worse (third) on social indicators; Costa Rica ranked best in social indicators and second in the economic indicators. Cuba ranked second in social indicators (in the 1990s, but first in the 1980s) and worst in economic indicators.[1] In the relative improvement indicators, Costa Rica managed

[1] The book is 707 pages long and faced numerous methodological problems that cannot even be summarized herein. The results discussed in the text, therefore, considerably simplify the book measurements and conclusions. In

to close the gap with Cuba, despite a worse stand at the starting point, for instance, in 1960 life expectancy was 61.6 years in Costa Rica and 64.0 in Cuba but in 1995-2000 they were 76.5 and 76.0 respectively.

Finally, a comparison was done with international rankings that include the three countries, with similar results. For instance, the Human Development Index (H.I.) ranked the three countries in 1993 (among 174 countries in the world and 20 in Latin America) as follows: Costa Rica 31 and 1, Chile 33 and 3, and Cuba 79 and 10 (UNDP 1996). The balanced approach to development in Costa Rica, therefore, led to a fair performance in economic indicators and to the best results in social indicators. Conversely, the extreme approaches of the other two countries resulted in good performance in one set but sacrificing the other. In Chile there were strong economic growth, lower inflation and a reduction in the fiscal deficit, but social consequences were adverse: poverty incidence worsened, real wages shrank, educational enrolment at secondary and tertiary levels declined, social security coverage decreased, unemployment jumped to a historical record, and morbidity rates rose. [2] At the end of the 1980s Cuba was leading the region in most social indicators (housing was a notorious exception), but the cost of social programs was very high and adverse economic distortions occurred, for instance, open unemployment was kept low but at the cost of significant overstaffing and very low labour productivity, and egalitarianism probably led to the least income inequality in the region but generated perverse incentives for labour absenteeism.

The corrections implemented in the 1990s in Chile and Cuba changed to some degree the previous performance. Chile's social indicators improved considerably (decline in open unemployment and poverty incidence, increase in real wages and secondary and higher-education enrolment) but, at the same time, economic indicators became even better (higher average growth rates, lower inflation, and budget surpluses). After a severe deterioration in the first half of the 1990s, Cuba's economic indicators had a mixed performance in the second half (higher growth albeit still well below the 1989 level, significant reduction in inflation and the fiscal deficit, but increasing external trade deficit and debt), while some social indicators kept improving (infant mortality, life expectancy) and others deteriorated (open unemployment and underemployment rose significantly, real wages and university enrolment declined sharply, and morbidity in several diseases rose). In

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addition, an important section of the book deals with exogenous factors (other than the system) that could affect performance.

[2] Investment on health was halted for almost one decade while real expenditures on health-care were cut significantly. The infant mortality rate, however, continued its decline because scarce resources were targeted on pregnant women and infants.

Costa Rica economic growth continued to be fair (after the decline in 1981-85) and inflation rose and then declined but the fiscal deficit continued to be high, most social indicators kept improving but open unemployment rose somewhat (1998a; ECLAC 1998c; 1999; 2000; Mesa-Lago 2000a; 2000d; 2001c).

In order to update the information of my book on the three countries, Table 1 incorporates the following 1990s data from ECLAC and UNDP: (1) two economic indicators: annual average GDP growth rate in 1991-1999, and real GDP per capita in dollars PPP; (2) nine social indicators in the 1990s: real mean wages, open unemployment, income distribution, poverty incidence (these two indicators are only available for Chile and Costa Rica), illiteracy, enrolment in secondary and higher education, daily caloric and protein intake, infant mortality, and life expectancy; and (3) the Human Development Index (HDI) score.

Table 1: Comparison of Economic Growth, GDP per Capita, and Social Indicators (Outputs) in Chile, Costa Rica and Cuba: 1990s

Indicators	**Chile**	**Costa Rica**	**Cuba**
Economic Growth (1991-99)[a]	6.0	4.1	-2.1
GDP per capita (1997)[b]	12,730	6,650	3,100
Urban real mean wages (1998)[c]	135.5	115.1	57.3
Open unemployment (1998)	6.4	5.4	6.6
Income distribution (1994)[d]	0.473	0.363	n.a.
Poverty incidence (1994)[e]	23	21	n.a.
Illiteracy (1997)[f]	4.8	4.9	4.1
Enrolment secondary (1996)[g]	74.9	50.0	77.3
Enrolment higher education (1996)[g]	30.3	33.1	12.4
Daily caloric intake (1996)	2,810	2,822	2,357
Daily protein intake (1996)	78.9	74.3	52.1
Infant mortality (1996)[h]	11.8	11.8	9.0
Life expectancy (1997)[i]	74.9	76.0	75.7
Human Development Index (1997)[j]	0.844	0.801	0.765

Sources: (1998a; ECLAC 1998c; 1999; 2000; UNDP 1999).

[a] Annual average real rate (absolute).
[b] Real GDP measured in dollars PPP.
[c] Base 1990=100
[d] Gini coefficient urban; rural are 0.409 and 0.372.
[e] Percentage of households below the poverty line.
[f] Percentage of population 15 years and older.
[g] Percentage of the corresponding age cohorts.
[h] Per 1,000 born alive.
[i] Years at birth.
[j] Combines three indicators: GDP $ PPP, education and health.

Table 1 shows that Chile performed best in GDP growth, followed by Costa Rica, and Cuba worst (a negative rate despite the recovery since 1995); Chile also had the highest GDP per capita, almost twice that of Costa Rica and four times that of Cuba. The three countries were fairly close in social indicators but, combining the indicators for which we have data for all

countries, Costa Rica was clearly first, and Chile second, and Cuba third. Costa Rica had the best combined performance: ranked first in four indicators, second in three and third in two (it was also ahead of Chile in income distribution and poverty incidence); Chile was first in two indicators, second in six and third in one; and Cuba was first in three indicators, second in one and third in five[3]. The HDI for 1997 (latest year available) shows Chile first, closely followed by Costa Rica and Cuba behind (Mesa-Lago 2001c).

In summary, despite the clearly best economic performance of Chile in the 1990s and the improvement in its social indicators largely prompted by the return to democracy, Costa Rica still led in social indicators with a fair economic performance. In spite of the recovery in the second half of the 1990s, Cuba trailed the other two countries in both economic and social indicators.

The Reform of Social Welfare and its effects on the People and Development

Mkandawire's chapter devotes a short section to "Social Insurance and Development" and the International Labour Office, in a document just published, discusses the controversy on the economic effects of social security. Some of the alleged negative effects are: it is very costly and harms economic growth, discourages savings, reduces international competitiveness, jeopardizes employment creation, and encourages premature withdrawals from the labour force.[4] Positive effects noted are: it contributes to economic growth by increasing productivity and enhancing social stability (helping to maintain workers in good health and taking care of them in sickness and maternity, preventing work-related accidents and diseases), maintains effective national demand (providing income to unemployed workers), helps employment (easing the departure of older workers from the labour force), helps the reproduction of a healthy work force (providing maternity and infant health care) and contributes to retraining of workers according to technological change (ILO 2001).

It is not feasible herein to deal with this long and complex controversy, but this chapter will discuss the reform of social welfare (actually social security, its fundamental component) in Latin America and assess its impact on the people and development. The term social security will be used in its broader sense, including social insurance (pensions

3 For ranking purposes the nine indicators were added assigning the following points: 1 to the country ranked first, 2 to that ranked second, and 3 to that ranked third; the total was divided by nine to obtain the average ranking; and the final scores were: 1.56 Costa Rica, 1.89 Chile and 2.56 Cuba.

4 It has been shown that as more developed a country is (higher is its GDP per capita) more are is social security expenditures as a percentage of GDP (ILO 2001).

for old-age, disability and survivors; health care and cash benefit for sickness and maternity as well as work injury; and unemployment compensation), family allowances and social assistance (ILO 2001). Because of space limitations the chapter will focus on the three major social security programs: social insurance pensions, health care, and social assistance. First, it will describe the structural reforms, and their degree of privatization and role of the state. Second, it will assess the impact of the reforms on the population and development: freedom of choice of the insured, population coverage and inclusion of the poor, gender discrimination, financial burden on the workers and the state, income distribution, competition and administrative cost reduction, capital accumulation and investment returns, and capital markets and national saving.

Structural Reforms, Degree of Privatization and Role of the State

1. Structural Reforms. In 1980-1981 Chile pioneered a radical structural reform of its social insurance pensions and health care systems, shaped by the neoliberal ideology and through privatization.[5] Largely because of the economic crisis of the 1980s and the Latin American dislike of Chile's authoritarian regime, such reforms did not have an impact in the region until the 1990s and mainly as a result of World Bank policies and conditions attached to structural adjustment loans, which were influenced by the Chilean model (see Mesa-Lago 1998).[6] A summary of the principal characteristics of the pension and health care structural reforms in the region follows.

a. *Pensions*. By mid 2000, ten countries had enacted pension reforms but, instead of copying the supposedly universal Chilean prototype, they followed three diverse general models of reform and with significant differences among all the countries (based on Mesa-Lago 1998; 2001b):

i. *Substitutive*, similar to the Chilean prototype and implemented in Bolivia (1997), Mexico (1997), El Salvador (1998) and Nicaragua (scheduled for 2001). In this model, the old social insurance or public system, usually based on pay-as-you-go (PAYG) and defined benefit or undefined contributions, is "closed" (prohibiting new affiliations). The old system is replaced with a "privately" administered system (in Mexico can be managed also by public and mixed institutions), which is fully-funded (FF), based on defined contributions which are deposited in individual accounts and invested, and benefits are undefined because

[5] Structural reforms are those that significantly alter a public social insurance system by totally or partially replacing it with a private system. Parametric reforms are those that attempt to improve a public system by changing its entitlement conditions or/and strengthening its finances.

[6] Cuba is the only country in Latin America where the pension and health care systems are totally administered and financed by the state, and provision is gratuitous. But the system urgently needs a reform.

they depend on the sum accumulated in the insured individual account at the time of retirement.

ii. *Parallel*, implemented in Peru (1993) and Colombia (1994). In this model the public system is not closed but reformed either partially (Peru) or totally (Colombia) and becomes an alternative option to a private system with similar characteristics to the Chilean prototype; the administration of the latter is exclusively private in Peru but multiple (private, public and mixed) in Colombia.

iii. *Mixed*, implemented in Argentina (1994), Uruguay (1996) and Costa Rica (scheduled for 2001). In this model, the public system is not closed but reformed, and it becomes one of the two integrated mandatory components of the new system: the public component is based on PAYG and defined benefit and pays a basic pension, and the new component is FF and based on defined contribution, administered by multiple institutions (private, public, mixed), and pays a supplementary pension.

b. Health. The process of health care reform is less advanced than that of pensions. Six countries have enacted structural reforms that follow three general approaches and show more diversity than in pension reforms (based on Bertram 1999; Cruz-Saco and Mesa-Lago 1998):

i. *Predominance of the public sector with marginal private collaboration*. In Costa Rica the process began in the 1970s and ended in the 1990s; social insurance has gradually incorporated all curative and most preventive health services and the ministry of health only has supervisory and policy functions. The system coverage is virtually universal because it combines a contributory program (for insured workers) and a non-contributory program (for the poor). There has been a process of decentralization as well as collaboration between private providers and the social insurance institute (CCSS), private services are received by less than one-fifth of the insured. In Mexico the reform of the mayor social insurance institute (IMSS) began in 1996 and has not been completed yet, the rest of the health system remains unchanged. Financing and provision of services is being gradually separated, there is a process of decentralization (from the centre to regions, delegations and local units), and resources are expected to be assigned by capitation and a system of hospital patient classification. Eventually the insured should have the possibility of selecting alternative providers.

ii. *Partial privatization and dual selection*. Under the Chilean pioneering reform (1981), the public sector was not closed but reformed. Facilities and services of various social insurance schemes and the ministry of public health were integrated and decentralized, and they basically cover the poor and low-income population. New privately

managed corporations that resemble Homes (called IS Après) were established; they have better facilities and offer a wider package of services for an extra premium, and cover the middle and high income groups. Theoretically the insured can select between public and private providers but costs of the latter are a barrier, resulting in a dual system in practice.

iii. *Partial privatization with multiple selection*. Peru enacted three reforms in 1991-1997; the latest has a few similarities to Chile's, but there is no linkage between the public and private systems, the counterpart of the IS Après (EPS) may be public, private or mixed, and they offer supplementary services over the basic services provided by social insurance. Colombia began in 1993 the implementation of the most complex reform of the region, with a double tier of administrators and providers (both can be public, private or mixed) and greater possibility for selection among them. There are contributory and subsidized programs, respectively for the insured and the poor and low-income population. Finally Argentina began the reform in 1995 allowing those workers insured in trade-union-managed providers (*boras socialists*) to select and change them, and the same option is given to pensioners, all OS must provide a basic health care package.

2. The Degree of Privatization. Despite the conventionally used term "privatization," half of the systems in the ten pension reforms are not exclusively managed by private corporations, and this is true of the seven health reforms too. Under the pension reform, four countries with substitutive systems have exclusive private administration (Chile, Bolivia, El Salvador and Nicaragua), as well as Peru in the parallel private system. In the three mixed systems (Argentina, Uruguay and Costa Rica) there is a combination of public administration in the basic component and multiple administrators in the supplementary component. In the parallel models of Colombia and Peru the public system is administered by social insurance. Finally, both Colombia's parallel "private" system and Mexico's substitutive system have multiple administrators. The percentage of insured in the "private" system or component varies significantly among the countries, declining from 100% in Bolivia and Mexico, to 97-90% in Chile and El Salvador, 78-79% in Argentina and Peru, and 49-40% in Uruguay and Colombia (no data are available yet on Costa Rica and Nicaragua). Section E will discuss the limitations faced by small countries in terms of entry and competition when relying only on private corporations of exclusive dedication.

Under the health reform, two countries have a dominant social insurance administration (Costa Rica and Mexico), and in the remaining four countries, the bulk of the insured is covered by the public sector o social insurance and the rest is covered by multiple types of administrators (except in Chile). In the most advanced health care reform, that of Chile, only 27% of the insured is affiliated to the private IS Après (Mesa-Lago 2000b; 2001b).

3. The State Role. Neoliberal reformers abhor public intervention but the state has proven to be absolutely necessary for a proper function and sustainability of a “private” system, through the following functions: (a) mandatory affiliation; (b) strong and detailed public regulation of the system; (c) control, monitoring and sanctioning through a supervisory public institution (usually a "Superintendence" of pensions and health care which is state-financed in several countries); (d) strict regulation of investment instruments and ranking of them by a public institution (*Classificatory de Resigns)*; and (e) last but not least, heavy fiscal subsidies and state guarantees throughout the transition and beyond (see section F).

The Insured Freedom of Choice

One of the key objectives of a structural reform in either pension or health care is to break the state monopoly and establish freedom of choice in behalf of the insured to select the system and choose/change its administrators. The reality shows that there is a significant variation in such freedoms among countries.

1. Pensions. Under the pension reform, there are two types of freedoms: to select between the public and the private (or mixed) systems, and to select and change administrators. The ten countries can be ranked, from least to most freedom to select between the public and private (or mixed) systems, as follows: (1) no freedom in Bolivia and Mexico because the "old" insured (all those affiliated at the time of enactment of the reform) and the "new" insured (all entrants into the labour force who are legally covered) must join the "private" system; (2) minimum freedom in El Salvador and Uruguay (the old insured was divided by age and only the younger insured had an option, while all the new insured must enter the private or mixed system); (3) intermediate freedom in Chile (the old insured had a period to decide whether to stay in the public system or move to the private system, but all new insured must join the latter) and Peru (the old insured can always choose to move but once he/she changes to the private system cannot return to the public, and the new insured must join the private system); and (4) maximum freedom in Argentina and Colombia (both the old and new insured can select and move among systems).

Concerning the freedom to change administrators: (1) they are prohibited in Bolivia, unless the insured changes domicile; (2) one annual change is allowed in Mexico and Nicaragua; (3) two annual changes in Argentina, Colombia, El Salvador and Uruguay; and (4) there are no restrictions in Chile and Peru (but in practice one change per year is feasible). Finally the insured does not have any freedom to select investment instruments or the profile of his/her portfolio as these are decided by the administrators, and at the time of

retirement the insured cannot withdraw the sum in his/her individual account but only opt for two or three options: an annuity, a programmed pension or a combination of both (Mesa-Lago 2001b).

2. Health. Under the health reform, freedom of choice is minimal in Costa Rica and Mexico, intermediate in Chile, and maximum in the other three countries. It should be noticed that the poor and the low-income groups do not have in practice the right to select a private provider in Chile and Peru because of the high cost of the extra premium (Bertram 1999).

Population Coverage and Inclusion of the Poor

1. Coverage Prior to the Reform. In general terms, the degree of social security coverage in Latin America has been positively related with the level of development and, specifically, with the percentage of the labour force which is formal and salaried. The 20 countries in the region have been divided into three groups according to the inception and level of development of their social security systems: pioneer, intermediate and latecomers (Mesa-Lago 1998).

a. *Pioneers*. These countries are the most socially developed and introduced social insurance in the 1920s and 1930s; by the 1980s they had virtually achieved universal coverage with a combination of social insurance (contributory programs that covered from 70% to 80% of their labour force) and non contributory social assistance. Three pioneer countries have implemented pension reforms: Argentina, Chile and Uruguay, and the first two and Brazil have undertaken health care reforms also. There were several facilitators of coverage in this group: a predominantly formal salaried labour force, a small informal sector (i.e., self-employed, unpaid family workers, employees of microenterprises, domestic servants, home workers), a small proportion of peasants, relatively low poverty incidence, and mandatory coverage of the selfemployed (in Argentina and Uruguay, voluntary in Chile). In these countries, therefore, all or part of the poor were protected by social security although the level of the social assistance pensions tended to be low.

b. *Intermediates*. These countries introduced social insurance in the 1940s and 1950s. Costa Rica belongs to this group chronologically but, because of the rapid expansion of coverage in the 1960s-1970s and the addition of social assistance pensions, by the 1980s it had 85% of the population covered in health care and 53% of the labour force covered in contributory pensions (the majority of the poor received non-contributory pensions). In addition, Costa Rica's formal salaried sector is a majority in the labour force, the proportion of peasants is small, and poverty incidence is the second lowest in the region, hence, most of

the poor were protected. This country, therefore, has many of the characteristics of the pioneers and has introduced both pension and health reforms. Three other intermediate countries have implemented pension and health care reforms also: Colombia, Mexico and Peru. They have a smaller formal salaried sector, larger informal sector and peasants, and higher poverty incidence than the pioneer group (Peru being in the worst situation), and the selfemployed only is entitled to voluntary coverage. Prior to the reform, coverage of the labour force in pensions was 44% in Mexico, and about 32% in Colombia and Peru.

c. *Late comers*. In this group, social insurance was established in the 1960s and 1970s and these countries are the least developed in the region: their informal sector combined with peasants embrace the majority of the labour force, the formal salaried sector is a minority, and poverty incidence is very high. It is not surprising, therefore, that social insurance coverage was very low, and that there are no social assistance pensions because they would have to cover the majority of the labour force. The poor are thus excluded from coverage. Out of the ten countries that have introduced pension reforms, three belong to this group and are among the poorest of the region: Bolivia, El Salvador and Nicaragua. Prior to the reform coverage of the population on health was 12%, 23% and 14% respectively.

2. Coverage After the Reform. Statistics on coverage after the reform are available on pensions only and they are confusing because can be measured based either on the number of affiliates (who have joined the system at any time) or on the number of active contributors (who have paid their contributions in a recent period). The eight countries for which we have data, had the following percentages of coverage of the labour force in 1998 (first based on affiliates and second based on active contributors): 72% and 66% in Uruguay; 102% and 54% in Chile; 63% and 30% in Argentina; 45% and 23% in Colombia; 36% and 23% in Mexico; 29% and 20% in El Salvador; 26% and 13% in Peru; and 13% in Bolivia --no data are available on active contributors (see Table 2).

Table 2:Performance of Structural Pension Reform in Eight Countries of Latin America 1998-99[a]

Indicators	Argentina	Bolivia	Colombia	Chile	El Salvador	México	Peru	Uruguay
1.% of the labour force covered by both systems (Dec.98)[b] Based on: Affiliates ActiveContributions[c]	63 30	13 n.d	45 23	102 23	29 30	36 23	26 13	72 66
2.Insured Affiliates								
Old System								
Number (thousands)	2,200	0[f]	4,660	205	74	0[f]	544	548
% of total	22	0[f]	60	3	10	0[f]	21	51
New System								
Number (thousands)	7,689	492	3,140	5,996	670	14,622	2,106	521
% of total	78	100[f]	40	97	90	100[f]	79	49
3. No. of Active Contributors %contributors /affiliates	3,576 45	n.d n.d	1,610 51	3,090 52	430 64	9,022 62	922 44	330 65
4.No of administrators	12	2[g]	7	8	3	14	5	6
Concentration of insured in the biggest 3 administrations(%)	54	100	60	74	100	43	75	69
Wage contributions going to individual account	7.58	10.00	10.00	10.00	7.50	10.00	8.00	12.37
7.Total commission charged (%)[d]	3.41	2.50[h]	3.50	2.61	3.18	4.13[k]	3.80	2.63
8. Accumulated Fund								
Million US$	16,787	472	2,448	33,246	118	8,300	2,274	477
%of GDP (1998)	5.1	4.0	2.3	39.8[i]	0.4	2.5[l]	2.5	1.3
9.Annual real average investment yield (%)[e]	13.0	7.5	10.1	11.3	14.0[j]	8.0	7.4[m]	7.4

Note: Numbers 3 to 9 refer to the “private” system or component (FFI).
Sources: (Mesa-Lago 2001b) updated with recent information.

[a] Most data are from mid-1999, except when specified and: Peru Sept. 99; Argentina Sept-Dec. 99 (number of administrators April 2000); El Salvador number of administrators August 2000. [b] Includes those covered in the old system, plus those in the new system; excludes other groups of insured in Argentina, Colombia, Mexico and Uruguay, as well as the armed forces in all countries. [c] According to AIOS 1999, includes all insured who has contributed in the last month, except Mexico which is in the last two months. [d] Includes the commission of the administrator of the old-age program plus the premium for disability and survivors paid to insurance companies. [e] Argentina: July 94-Dec. 99; Colombia: Dec. 95-Dec. 98; Chile: July 81-May 99; El Salvador June 98-June 99; Mexico: July 97-June 99; Peru: Sept. 93-Sept. 99; Uruguay: June 96-June 99. [f] All insured most change to the new system. [g] The number was planned to remain at two until 2000, but by July it remained unchanged. [h] The commission is very low (0.5%) because there is no competition; the cost of the premium is 2%. [i] AIOS 1999 gives 43.9%. [j] Given by AIOS 1999, but the figure is quite doubtful. [k] The commission averages 1.63% and the premium 2.5%, the latter is paid to the social insurance institute. [l] Excludes the housing fund. [m] According to AIOS 1999, the average of the last

five years was 5.9%, the Table shows the average of the last six years. [n] Includes the old system and those who are in the reformed public system but not in the mixed system.

Estimates of coverage based on affiliates before and after the reform, indicate: (a) a decline in coverage in Argentina, Mexico and Peru; (b) no change in Bolivia and Uruguay; and (c) an increase in Chile, Colombia and El Salvador. It is not possible to determine here the causes of the different results in the eight countries but part of the explanation may be due to statistical deficiencies. These are usually noted on the data prior to the reform, but figures after the reform are not exempted from flaws. For instance, in 1998 it was reported in Chile that 102% of the labour force was covered based on affiliates but, in addition of being statistically impossible, that figure excludes: 3% of the labour force covered by the public system, 3% by the separate scheme of the armed forces, and 23% who are roughly estimated as uninsured, for a total of 29%. Adding up everything, coverage would be 131% but based on active contributors would be reduced to 54% (Mesa-Lago 2001a).

Labour force coverage based on active contributors after the reform cannot be compared with the situation prior to the reform due to lack of previous data. Nevertheless, after the reform, the percentage of coverage based on active contributors is significantly lower than that based on affiliates, probably because of the following reasons: (a) a high percentage of non compliance by the insured or payments delays by the employer: only an average of 55% of the affiliates are active contributors (from 46% in Argentina to 65% in Uruguay; see Table 2), the increase in insured contributions could be a contributing factor (see section E); (b) double counting, that is, one insured appears registered in two administrators because of frequent changes and slow clearance of the transfer (this could largely explain the 102% coverage in Chile); (c) part of the affiliates may be temporary workers who only contribute occasionally or have permanently left the labour force; (d) significant unemployment in some countries (e.g., 15% in Argentina); and (e) moral hazard: low-income insured minimize their contributions to earn the right for a minimum pension and maximize state subsidies to finance that pension (Arenas de Mesa 2000; Mesa-Lago 1998; Mesa-Lago 2001a; Mesa-Lago 2001b).

An important step has been taken by Costa Rica in its pension reform of 2000: the creation of a universal assistance pension for all the poor population 65 years and older, who are neither insured nor actually receiving non contributory pensions, and the grating of a fiscal subsidy to the self-employed to compensate for the lack of an employer (Imprenta Nacional 2000). These two measures should help to achieve universal coverage in pensions as is currently the case of health care.

The decline in social insurance coverage of the formal labour force, combined with an increasing trend of the informal sector in the region, raises concern on five important issues: (a) the need of social security to adapt to changes in the labour force to at least maintain current coverage; (b) the worsening protection of the poor in view of a rising poverty incidence and very few countries that provide social assistance pensions; (c) the insufficiency of current social assistance pensions in the few countries that provide them (in most cases they don't cover essential needs); and (d) the need to allocate more resources for social assistance for health care and pensions and how to finance them (Mesa-Lago 2001d).

Gender Discrimination.

Woman workers tend to have a lower coverage than their male counterparts because they are predominant in sectors nor covered by social insurance such as informal labour. Universal health care systems (for instance, in Costa Rica), however, normally offer women the same rights and benefits than men, hence, they promote gender equality (ILO 2001). On the other hand, private health providers (such as ISAPREs in Chile) have discriminated against women because of their higher health needs (i. e., maternity) and costs.

Concerning pensions, insured women often receive lower benefits than their male counterparts, because of three reasons: (a) women's salaries are usually lower than men in the same job, hence, their contributions are also lower; (b) female insured density of contributions are also lower than male's because of pregnancy and temporary absence from the labour force to child rearing; and (c) the age of retirement of female insured is often five years lower than male's in Latin America, but the former tends to leave an average of four years longer. As the rate of participation of women in the labour force increases these inequalities become more salient (Mesa-Lago 2001b).

Through internal solidarity and gender transfers public pension systems have certain features which attenuate labour market inequalities against women, such as minimum pensions and weighted benefit formula that favor the lower paid. Conversely, private (FF) pension systems lack solidarity and distributive elements, therefore, cannot attenuate such inequalities (ILO 2001). In the process of structural pension reform, the gender dimension has not been sufficiently discussed in government, academic and political circles, partly due to ignorance but also to traditional negligence, but increasing attention and discussion are taking place (Arenas de Mesa 2000; Arenas de Mesa and Veronica Montecinos 1999; ILO 2001; Montecinos 1994).

Most studies so far have concentrated on the Chilean reform. Among the discriminatory features of the private (FF) pension system, the following four have been

noted: (1) relatively more obstacles for women to qualify for a minimum pension because it is more difficult for them to fulfil the number of required monthly contributions; (2) replacement rates for women (32% to 46%) considerably lower than for men (from 58% to 83%); (3) the fixed commission on wages (for administrative costs) affects more adversely those workers with low income–a group in which women are over represented--because it subtracts a proportionally higher sum from the amount deposited in the individual account; and (4) lower deposit results in poorer investment yields (Arenas de Mesa 2000).

Financial Burden on the Workers and Fiscal Cost of the Transition

1. Payroll Contributions and the Burden on Workers. Health-care and pension systems are financed mainly by payroll contributions imposed on insured workers and employers, but also by state contributions as a "third party"(fixed as a percentage of the payroll or through special taxes or through budget subsidies to cover deficit), and by investment yields (this section is based on Mesa-Lago 2000c). There is a theoretical and empirical debate on whether employers actually pay their contributions or transfer them "forward" to consumers via prices or "backward" to their workers; if indeed there is a transfer, the contribution should not have an impact on employment although might have an effect on income distribution or competitiveness. It is alleged by one side in the debate that, if employers indeed pay their contributions, that will cause a distorting effect on the labour market: an incentive to substitute capital for labour, hence, restricting job creation. Chile used this argument to eliminate the employers' contribution in both the pension and health systems, and the same was done by Bolivia and Peru on pensions, but that was not the case in the other pension reforms: four did not change the employers' contribution (Argentina, Costa Rica, El Salvador and Mexico), one slightly reduced it (Uruguay), and two increased it (Colombia and Nicaragua). Under the health reform, Peru shifted all the contribution to the employer, and in the other five countries the higher proportion of the total contribution is imposed on the employer (Argentina, Colombia, Costa Rica, Mexico and Nicaragua).

The insured contribution for pensions was slightly reduced in Chile's private system (but not in the public one), it remained unchanged in Argentina, Costa Rica and Mexico (in the latter, the state contribution was increased), and was raised in six countries: Bolivia, Colombia, El Salvador (the highest), Nicaragua, Peru and Uruguay (the smallest). The financial burden of the pension reform has been shifted in most countries from the employer to the insured, justified by the argument (not empirically proved) that it will correct an alleged labour market distortion. The elimination of the employers' contribution leads to either an increase in the insured contribution or the fiscal subsidy as explained below.

2. Fiscal Costs of the Transition. Pension reforms of the substitutive and parallel types induce three fundamental fiscal costs (this section is based on Mesa-Lago 2000c): (a) the deficit in the public system which occurs because it is left without contributors or a minority of them, but with the burden of all current pensions and those that will be eventually granted to the insured who stayed in that system, the state finances such deficits in all countries; (b) the value of the contributions paid to the old system by all the insured who move to the new system (often called "recognition bond"), such value is annually adjusted to inflation (except in Nicaragua) and two countries pay also an interest rate of 3-4% (Colombia and Chile), the state is responsible for this cost in all countries except in Mexico and Uruguay, [7] but there are different restrictions such as ceilings and minimum years of contribution required (Peru has certified a small percentage of the owed recognition bonds); and (c) a guaranteed minimum pension for all insured in the new system whose accumulated sum in the individual account is insufficient to finance such pension, the state is responsible for the difference in five countries (Chile, Colombia, El Salvador, Mexico and Nicaragua), neither Bolivia nor Peru effectively grants this benefit. Under the mixed model, the public component may generate a deficit (Argentina and Uruguay because they are based on PAYG) or not (Costa Rica because it has ample reserves), but there is no need for a recognition bond, as the insured stays in the public component which pays a basic pension, this makes unnecessary the payment of a minimum pension in the "private" component.

In addition, the state grants the following guarantees to the insured in some countries: (a) a social assistance pension to poor non-insured workers (Argentina, Chile, Costa Rica and Uruguay); (b) adjustment of pensions to inflation including the minimum pension (the period of adjustment and its base varies in the countries); and (c) other guarantees such as a minimum annual yield of the investment in case that the administrator's funds are insufficient to pay it, and payment of pensions in case that administrators or insurance companies go bankrupt and their insured and pensioners are left without protection (granted in Chile, Colombia, Argentina and Uruguay, in the last two limited to public administrators not private ones).

3. Two Trade Offs. The parallel and mixed models do not necessarily reduce fiscal costs in the long run but defer such costs because only part of the implicit pension debt (IPD) is made explicit. Conversely, in the substitutive model all the IPD is made explicit,

[7] In Mexico all the insured at the time of the reform has been granted the right at retirement to choose the highest pension between two: the one based on his/her accumulated individual account and the one based on the rules of the closed public system. Uruguay does not grant this benefit because the public system is not closed and is responsible for paying a basic pension.

more rapidly in Bolivia and Mexico than in the other countries because all the insured must move to the new system. This involves a trade off: either a high and immediate fiscal cost that might aggravate a difficult economic situation but would diminish in the long run (40 to 60 years) or a partial postponement of debt that would provide a break to wait for a more economically propitious time. The countries that grant most benefits and guarantees are those that generate the highest fiscal costs (Chile), while those that negate some of those benefits or curtail them considerably are able to reduce such costs (Bolivia, Peru). Here lies another trade off: to reduce fiscal cost or to protect the insured.

Income Distribution

The ILO (2001) properly warns that social security systems should not be expected to promote a more equitable distribution of income by themselves; indeed many social security systems perform a redistribution function but that should not be its principal goal. Social security should be one instrument--albeit an important one-- of a broader package to improve income distribution. In this section we analyse what distributive function, if any social, security performs in public and private systems.

Concerning pensions, public systems with virtual universal coverage tend to have a progressive effect on income distribution if solidarity is properly applied, because transfers are done by the system collecting more from the higher-income insured, placing a ceiling to pensions, and securing a minimum pension for the low-income insured (if these conditions are not met, the system may have neutral or regressive effects). Conversely, systems with low population coverage tend to have a regressive effect on distribution, because the uninsured (low-income and poor) indirectly contribute to finance the minority covered (mostly middle income) through sales taxes and transfers of employer contributions to prices (Mesa-Lago and Fabio Bertranou 1998).

Structural pension reforms, particularly of the substitutive type, are devoid of endogenous solidarity (due to the "neoliberal skepticism about social solidarity" Mkandawire 2000: 11), although they may provide exogenous solidarity, for instance, through the state guarantee of a minimum pension and the granting of social assistance pensions. In principle, a private (FF) system leads to a neutral effect in income distribution because pensions are directly related to salaries and contributions. However, fiscal costs of the transition in countries with a small percentage of the labour force covered (Bolivia, El Salvador, Nicaragua, Peru) should have a regressive effect because the state subsidizes the insured middle- income minority usually through sales taxes that are paid by the uninsured majority (Mesa-Lago 2000c).

Health care reforms seem to have more concern for inclusion of the low-income and poor, and some of such reforms have introduced redistribution mechanisms. In Chile the state provides subsidies according to income, hence, the poor don't pay and the highest-income insured fully pays; however, the right to transfer the entire contribution from the public to the private system (ISAPRE) by upper-middle and high-income insured led to a significant depletion of resources in the public system and its subsequent deterioration in the 1990s. The first version of the Peruvian reform tried to address this problem retaining at the public system part of the contribution of the insured who joined the private system, but successive versions deleted such mechanisms. The Colombian reform has established a Solidarity Fund to finance the "subsidized scheme" that covers the poor and low-income uninsured and is funded with a payroll contribution of 1% (paid by high-income insured) and by the surplus generated by the care of high-income insured. In Argentina, there is a Redistribution Fund that is financed with part of the payroll contributions and compensates the *obras sociales* whose insured are low-income and suffer high sickness risks (Bertranou 1999; Cruz-Saco and Mesa-Lago 1998).

Competition, Administrative Costs and the Burden of Commissions on Workers

1. Competition. Adequate competition among administrators of both pension and health care programs is a key to structural reforms particularly in private systems. In theory, administrators compete for the insured and the latter have proper information to select the best, which should be assessed by the quality of care in health or the payment of a higher capital return in a pension fund, and by relative low commissions or premium charged in both. The scarce available information suggests, however, that competition is working better in health than in pension reforms, and that the size of the insured market is an important factor to facilitate or obstruct competition.

The experience of eight pension reforms in the region demonstrates that the higher the number of insured the higher the number of administrators and vice versa. Thus, Mexico has 14 million of insured and 14 administrators; Argentina 8 million and 12; Chile 6 million and 8; Colombia 3 million and 7 (but it has multiple types of administrators which facilitate entry); Peru 2 million and 5; El Salvador 670,000 and 3; and Bolivia 492,000 and 2 (Table 2). In Bolivia the number of insured was so small that the government decided that there was a market for only two administrators, hence, divided the insured between the two by domicile, and prohibited changes until the year 2000 (such prohibition continued in July 2000); as a result there is no competition but a duopoly. Countries with a small number of

insured should take into account this limitation and allow multiple types of administrators as well as the use by them of infrastructure from other financial institutions, in order to facilitate entry and reduce costs.

Even if there are a fair number of administrators, a significant concentration of insured in the biggest three has been observed: 100% in Bolivia (only 2) and in El Salvador (3); 78-75% in Chile and Peru (concentration in Chile has steadily increased from 59% in 1983); 69-60% in Uruguay and Colombia; 54% in Argentina; and 45% in Mexico--this country sets a maximum of 17% to each administrator (Table 2). A study done in Chile shows that the three administrators with the highest number of insured have not systematically through time charged the lowest commissions and paid the higher capital returns. Reasons behind the insured selecting those three administrators seem to be: (a) the work of salesmen or "promoters" who earn a fee for every insured they move to one of those administrators (in Chile there were 19,000 salesmen in 1998 a ratio of one for 160 active contributors); (b) gifts and other treats given to the insured as an incentive to move; (c) lack of insured information or/and skills to make educated decisions on the selection of the best administrators; and (d) huge advertisement which is essentially symbolic and does not provide data on performance (Mesa-Lago 2001b).

There seems to be more competition among administrators of reformed health care systems because both a larger number and variety of them. For instance in Chile there were 27 ISAPREs in 1997 almost three times the number of administrators (AFPs) existing at that time, and in Colombia the wide variety of administrators and providers is considerably higher than the pension administrators, but more and better data are needed on this important issue.

2. Administrative Costs. Competition is expected to reduce administrative costs, but the previous section cast a doubt on competition and data from the Latin American pension reforms show no significant reduction in such costs. The commission, exclusively paid by the insured, is usually imposed on his/her salary and is sizeable: 4.13% in Mexico; 3.8-3.0% in Peru, Colombia, Argentina, El Salvador and Nicaragua; and 2.6-2.5% in Uruguay, Chile and Bolivia (Table 2; Presidencia 2000). The commission is divided into two components: (a) the charge of the administrator for managing the old-age individual account, which is the major component and ranges from 1.9% to 2.5% of the total, its trend shows significant oscillation but little or no reduction; and (b) the premium transferred by the administrator to a commercial insurance company to manage disability and survivors insurance (in Colombia and Mexico this is done by social insurance), which is the minor component and ranges from 0.6% to 1.6% (except in Bolivia), it has exhibited a declining trend. The combination

of the two trends results in a stagnant commission or very little reduction (Mesa-Lago 2001b).

3. Burden of the Commission on Workers. The heavy burden on the insured of the administration of the pension system can be assessed in Table 2 which compares the percentages of wages that go to the individual account (ranging from 7.5% to 12.37%) and the total commission charged (ranging from 2.5% to 4.13%). The percentage of the latter over the former is as follows: 32-30% in Peru, Argentina, El Salvador and Mexico; 26-20% in Colombia, Chile and Bolivia; and 17.5% in Uruguay. Little or no data are available on health care administrative costs under the reform a matter that demands more research.

Capital Accumulation and Returns

1. Capital Accumulation. There has been significant capital accumulation in the pension fund of the eight countries (figures are in U.S. million dollars and percentages of GDP at the end of 1998 or mid 1999): $33,246 and 40% in Chile; $16,787 and 5% in Argentina; $8,300 and 2.5% in Mexico; $2,925 and 2.3% in Colombia; $2,274 and 2.5% in Peru; $472 and 4% in Bolivia; $477 and 1.3% in Uruguay; and $118 and 0.4% in El Salvador (Table 2). The variation among countries is the result of various factors: (a) the time the reform has been in operation, almost 20 years in Chile but one year in El Salvador (Costa Rica and Nicaragua introduced their reforms in 2000); (b) the size of the insured market and GDP, and the salary level; and (c) the amount going to the individual accounts and the capital return.

2. Capital Returns. One of the flaws of social insurance pension programs prior to the reform was the very low or negative capital returns or real investment yield that they generated; the pioneer countries had little or no reserves and most of the rest did have reserves but they were badly administered (Mesa-Lago 1998). The reform has improved investment management of the pension fund and its yield, although at a high administrative cost. The annual real average yield from the time of the inception of the reform until the end of 1998 or mid 1999 was: 13% in Argentina; 11.3% in Chile; 10.1% in Colombia; 8% in Mexico; and 7.5-7.4% in Bolivia, Peru and Uruguay-the figure from El Salvador is not reliable (Table 2). Granted that this performance is far superior to that prior to the reform, it should be interpreted with the following caveats: (a) data is gross and administrative cost should be deducted to obtain the net return; (b) all systems, except Chile, began to operate in the 1990s when international markets had very high returns; (c) the average yield prior to 1995 was considerably higher, the regional crises induced by Mexico in 1995 and the East

Asian economies in 1997-1998 reduced the yield considerably.[8] The severe decline in the capital market in the United States in early 2001, may have similar adverse effects on capital returns of pension funds in Latin America. All this means that the oscillations of the capital market can generate quite different pensions in times of boom or bust, thus in Chile, the insured who entered the system in the 1980s will have a significantly higher pension that one who joined later (Arenas de Mesa 1999). Such a risk should be diminished in the mixed systems because they combine a defined benefit with an undefined one.

Capital Markets and National Saving

It is argued that the increase in capital accumulation and its investment in the capital market should contribute to its development making it deeper, more liquid, competitive and efficient, thus helping to diversify the pension fund portfolio; these results, in turn, should lead to higher national saving and economic growth. These beliefs are endorsed by the World Bank and have been a motivating force for pension reform in Latin America (Mexico included them in the preamble of its reform law).[9] And yet, among the eight pension reforms in the region, the testing of such hypotheses has been done only in Chile, the country with the longest reform in operation, and its results have been negative or inconclusive.

1. Development of Capital Markets. A long-run econometric study of Chile, commissioned and published by the IMF, concluded that the empirical evidence *coincided* with the claim that the pension reform has contributed to financial market development and a more diversified portfolio, but cautioned: "all this evidence does nor established watertight proof that the establishment of pension funds has been the decisive factor in the impressive development of financial markets since the mid-1980s," the latter "may simply reflect changes in legislation and other lessons learned from the experiences and mistakes of the 1970s an early 1980s" (Holzmann 1997: 163). In summary, there is no proof that the first part of the hypothesis is true.

The pension fund portfolio in Chile has indeed become more diversified since 1983 when it was overwhelmingly invested in public debt instruments or deposited in state banks; the early 1980s crisis made evidently to the Superintendency the danger of such excessive concentration and it began to promote a movement of investment to other instruments and the private sector. And yet after almost two decades, in 1999 still 37% of the portfolio was in state debt paper and only 13% in stocks; actually the crisis of 1997-1998 led to a shift

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[8] The Chilean annual yield in 1981-94 was 13.8% but in 1995-1999 it was 2.6%, due to negative yields in 1995 (-2.5%) and 1998 (-1.1%), resulting in an average of 10.1% for the entire period.

[9] Such claim in the case of Chile is also made by (Mkandawire 2000: 14-15).

away from the latter to the former. In other countries there is little diversification of the portfolio, for instance, in 1999, in Mexico, El Salvador, Bolivia and Uruguay from 64% to 97% of the investment was in government debt paper (51% in Argentina); the good capital return in these countries, therefore, was due to the high interest paid by the state but, although beneficial for the insured, it was costly and difficult to maintain in the long run. Conversely, the proportion of investment in stocks was cero or nil in five countries and only had significant shares in Peru (27%), Argentina (17%) and Chile (13%). The alternative of investment abroad is nonexistent or nil in six countries, Chile is an exception with 12% (AIOS 1999).

2. National Saving. The cited study published by the IMF concluded that the evidence was negative concerning the second part of the hypothesis: "contrary to the common belief . . . the empirical findings suggest that the direct effect of financial market developments on the private saving rate was negative . . . The data indicate that the net pension savings were negative until 1989 and small afterward (therefore) the conventionally assumed impact of a Chilean-type pension reform on private (and national) saving may not hold . . . These results also temper the optimism reigning in Latin America and Easter Europe, where pension reform is seen as an easy vehicle to boost national saving, and thus capital accumulation and growth" (Holzmann 1997: 175).

Another study done by a high official of the Ministry of Finance in Chile also shows that the net effect of the pension reform on national saving was negative and during *the first fifteen years*, that is, seven years after 1989 when the IMF study estimated it to be positive but small. This calculation demonstrated that, in 1981-1996, the annual average saving in the individual accounts was 2.7% of GDP, but the fiscal cost was -5.7%, hence resulting in a negative net outcome of -2.6% of GDP. The study also projected that in the first five years of the 21st century the net outcome should become positive and grow thereafter, but probably it would take 20 years to compensate for the negative balance in the previous 20 years, in summary it would take 40 years to show a cumulative positive balance in national saving (Arenas de Mesa 1999).

Conclusion

Latin America is one of the world regions that has experimented with more development models, it also has been at the vanguard of social policies and a pioneer in the foundation of the welfare state in the American continent. In the same vein, the region has been at the forefront of market-oriented reforms and in the process of privatization of social services. It is important, therefore, to analyze representative diverse models of development in Latin America and evaluate their socioeconomic performance, as well as assess the effects of social welfare (security) reform on the people and the economy.

The analysis of three different models of development in Latin America (Chile-market, Cuba-statist and Costa Rica-mixed) and evaluation of their performance found that: (a) the mixed model was able to combine in the best way the roles of the state and the market, as well as to properly balance social and economic goals; (b) the other two models overemphasized either the market or the state and were able to advance in one set of goals but sacrificing the other; (c) the balanced approach of the mixed model led to a fair performance in economic indicators and the best results in social indicators in the long run; and (d) corrections introduced in three models in the 1990s have reduced somewhat the role of the market in Chile and the role of the state in Cuba, and increased somewhat the role of the market in Costa Rica but without altering the essence of the three models or significantly modifying their performances.

Structural reforms of social security (the most important component of the welfare state) implemented in early 1980s in Chile and in the 1990s in several countries in Latin America, both in pensions and health care, have strengthened the role of the market and led to a larger private sector in those social services. Nevertheless the reforms have followed diverse general models and different in all countries, with different degrees of privatization. Despite the reforms, the role of the state continues to be crucial in al countries.

The effects of the reforms on the people and the economy are mixed but tend to be in the negative side: (a) the freedom of choice of the insured ranges to zero to wide depending on the countries; (b) coverage of the labour force based on the number of affiliates has declined after the reform in three countries, remained unchanged in two and increased in three, but data are flawed in some cases, coverage based on the number of active contributors is significantly lower that based on the number of affiliates; (c) the poor continue to be excluded from social insurance in virtually all countries that have implemented reforms (health care reforms have more concern for the inclusion of the poor than pension reforms), although receives social assistance in four of them even if it tends to be insufficient; (d) inequalities generated by gender discrimination have increased in

“private” systems due to their lack of both solidarity and inter-gender transfers; (e) the financial burden on the worker has become heavier with the reform because the employers’ contribution has been eliminated or reduced in most countries while the workers’ contribution has been increased; (f) the reform has generated three types of fiscal costs during the transition and such costs are high, countries that have tried to reduce such costs have curtail benefits of the insured; (g) some health reforms have introduced redistribution mechanisms but pension reforms have either neutral or regressive effects on distribution; (h) competition has not worked as expected and, hence, administrative costs of “private” systems have not declined substantially, furthermore, such costs are high and borne by the insured; (i) there has been significant capital accumulation in pension funds in all countries but with significant variation among them based on the time that the reform has been in operation and other factors; (j) capital returns have been apparently high but they most be adjusted to deduct administrative costs and they have oscillated with the capital market generated different pensions in times of boom and bust; and (k) there is not evidence that the reform has been the decisive factor in the development of the Chilean capital market, but evidence that the reform has had a negative effect on national saving.

The lessons of the three development models and the structural reforms of social security in Latin America should be carefully studied by other countries in that region and the rest of the world, to avoid adopting policies inspired sometimes by ideological concerns but not well grounded in empirical experience.

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