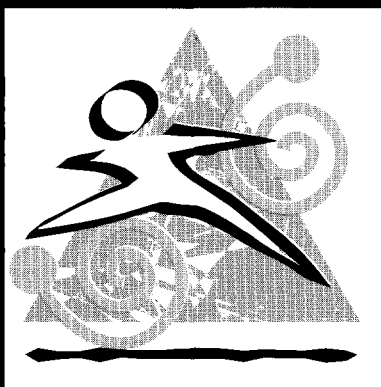


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# The Pension System in Argentina

## Six Years After the Reform

Rafael Rofman

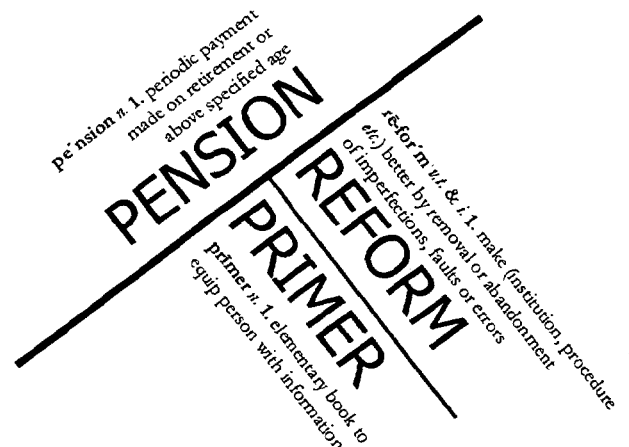
June 2000



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Rafael Rofman\*

Buenos Aires, June 2000



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## Abstract

In a context of a serious financial and legal crisis, Argentina reformed its Pension System in 1994, when a multipillar model with a funded scheme was introduced and first pillar parameters, as minimum age and vesting requirements were tightened. The new system has a significant first pillar (which offers a flat benefit currently valued at 28% of average wage to all retirees) and a second pillar that should provide a similar amount, once the transition is completed.

The new system has developed rapidly and most formal workers have joined the new funded scheme. However, there are some problems that must be resolved. In the first pillar, the reform balanced long term finances, but it will also reduce coverage very rapidly, as a consequence of the combined effect of low formality in the labor market and stricter contribution requirements. The most serious problems in the funded pillar are the administration costs and the need to improve regulation and supervision of insurance companies, that provide disability and survivors coverage and annuities to beneficiaries.

While these problems are important, their consequences can be avoided if adequate policies are developed by the Government. In this sense, the experience of the pension reform in Argentina is an excellent lesson for other countries that are considering a reform in their own systems.



## TABLE OF CONTENTS

1. INTRODUCTION .....	4
2. THE BASIC STRUCTURE OF THE SIJP .....	5
2.1 THE NEW SYSTEM .....	5
2.1.1. <i>The Multipillar Scheme</i> .....	5
2.1.2. <i>Legal Coverage</i> .....	6
2.1.3. <i>Contributions</i> .....	6
2.1.4. <i>Benefits</i> .....	7
2.2 THE STATUS OF THE NEW SYSTEM .....	10
2.2.1. <i>Membership and Coverage</i> .....	10
2.2.2. <i>Transfers</i> .....	12
2.2.3. <i>Fees and Insurance Costs</i> .....	13
2.2.4. <i>Investment Restrictions and Performance</i> .....	14
3. THE PROBLEMS OF THE NEW PENSION SYSTEM .....	18
3.1 COVERAGE .....	18
3.2 THE FINANCIAL FEASIBILITY OF THE PUBLIC SOCIAL SECURITY SYSTEM .....	21
3.3 BENEFIT UNCERTAINTY .....	23
3.4 THE COST-EFFECTIVENESS OF THE FUNDED REGIME .....	24
3.4.1. <i>The magnitude of the costs of AFJPs</i> .....	24
3.4.2. <i>Regulation alternatives to increase the efficiency: The problem of volatility</i> .....	27
3.5 THE INSURANCE INDUSTRY AND ITS RELATION WITH THE PENSION SYSTEM. ....	28
3.5.1. <i>The disability and death insurance</i> .....	28
3.5.2. <i>The benefits in the funded scheme</i> .....	29
4. CONCLUSIONS .....	31
5. REFERENCES .....	33
STATISTICAL APPENDIX .....	35





# The Pension System in Argentina six years after the Reform

## 1. INTRODUCTION

*This document presents a description of the Pension System in Argentina, assessing its performance six years after the major reform that introduced a multipillar scheme. We particularly concentrate our attention on those aspects that are problematic and require further refinement.*

*The Argentine Pension System includes a national system, the SIJP (Sistema Integrado de Jubilaciones y Pensiones - Integrated System of Retirement and Pensions), as well as smaller governmental provincial systems, provincial-level professional funds and some special systems that cover the military and security forces.*

*The legal coverage of the SIJP is almost universal, since it includes public and private employees as well as self employed. The provincial systems cover government employees of the provinces or municipalities that have not yet joined the SIJP (approximately one half of all provinces) and there are a large number of professional funds –mainly provincial –, employers funds (for instance, the Bank of the Province of Buenos Aires) and special systems (like the Military and the Federal Police). Out of the approximately 13 million active, employed workers in Argentina, 4.7 million contribute to the SIJP, around a million contribute to provincial regimes and 500,000 to the other schemes. Roughly 6.8 million workers do not contribute to any system (most of them should belong to the SIJP) and, therefore, may not have adequate retirement savings.*

*This analysis is focused on the SIJP, because it is the system with the widest scope and it is slowly absorbing the other schemes. Nevertheless, it is important to mention that the problems of provincial and sectoral regimes should be carefully addressed, because they appear in some cases to be financially unsustainable.*

*The second section describes the basic framework of the new system. Next, the third section presents information on the evolution of the system in its first five years of operations. Section four discusses the performance of the new system and its success in providing adequate social insurance coverage. Finally, section five presents the main lessons of the Argentinean experience with pension reform.*

## 2. THE BASIC STRUCTURE OF THE SIJP

### 2.1 The New System

Argentina's new pension system, established in 1994, is made up of a Public PAYG Regime and an Individual Funded Regime. In this section, we briefly describe the operation of this new system, including the multipillar scheme, its coverage, contribution rates, benefits, and the Government role in the operation of SIJP. The structure of the new system is somewhat complex, and a diagram describing the main institutions and characteristics is included at the end of the section.

#### 2.1.1. *The Multipillar Scheme*

The national pension system in Argentina (SIJP) is designed according to a model known in the literature as "multipillar". The system has three pillars; one, run by the government, that is mostly compulsory and offers a basic benefit; the second, run by the government and private managers, is also compulsory and pays benefits in relation to past contributions. The third pillar, of voluntary participation, is run by private managers and is very small.

The first pillar is run as a pay-as-you-go scheme, by the National Social Security Administration (ANSeS). It is financed by employers' contributions (16% of gross taxable income, according to the law) and the main benefit from this pillar is a Universal Basic Benefit (PBU), a monthly flat amount of approximately 28% of average wages, that can be claimed by any worker with 30 years of contributions and that has reached the minimum eligibility age.

The second pillar, financed by employees contributions (11% of gross taxable income), consists of two alternative regimes: a pay-as-you-go regime, managed by ANSeS and a Funded Regime, managed by privately owned Pension Fund Managing Companies (AFJP).<sup>1</sup> Disability and survivors benefits are financed by the second pillar, depending on the option (funded or pay-as-you-go) the worker has chosen, while survivor benefits due to death of a retiree are financed in the same way as the retirement payment.

Besides the elements already described, the SIJP has a transitional benefit, aimed at providing benefits to workers that contributed to the old system. All workers with contributions before the reform and retiring after 1994 will receive a Compensatory Benefit (PC), proportional to the pre-retirement income and the number of years with

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1 Assuming that a worker contributes 35 years in a row, with a commission of 3.5% of his salary, a wage increase of 2% annually and 5% annual earnings, he will receive approximately 30% of his last wage as a pension for life.

contributions to the old system.<sup>2</sup> In addition, workers retired before the reform will continue to receive their benefits.

The administration of the new first pillar, the PAYG second pillar, the benefits paid out under the old system and transitional benefits is concentrated in one scheme, called the "Public Pension Regime" (RPP), that is managed by a government agency, the National Administration of Social Security (ANSeS). Additionally, the RPP covers part of the cost of annuities for disability and survivors benefits in the funded regime.

### *2.1.2. Legal Coverage*

Participation in the SIJP is compulsory for wage earners in the private sector, employees of the National Government and of Provincial or Municipal Governments that have joined the system and for self employed workers. Some special groups, as directors and partners of companies, members of administration councils, clergymen, housewives and others may join the system on a voluntary basis. Members of the military and security forces and other small groups are excluded.

When workers enter the labor force they are automatically included in the first pillar scheme, and must choose between the PAYG and the funded regimes for their earnings related scheme. If they choose the PAYG, they can switch to the funded scheme at any time. If they chose funded, they cannot go back to PAYG. The default option (applied if the worker does not make an explicit choice) is the funded scheme.<sup>3</sup>

### *2.1.3. Contributions*

Contributions to the SIJP are compulsory, and workers in the funded scheme can also make additional voluntary contributions. Employees and employers are required to contribute 11% and 16%<sup>4</sup> of taxable income, respectively. The self-employed must contribute 27% of a pre-defined taxable income. Voluntary contributions can be made by workers (called "imposiciones voluntarias") or by employers (called "depósitos convenidos"). The law defined a minimum taxable income, equivalent to approximately 33% of average wages, and a maximum, of about 6 times the average wage.

Employers' contributions, and 16 of the 27 percentage points of the self-employed, are transferred to ANSeS and used to finance the RPP. To complement these contributions, some earmarked taxes are also directed to the ANSeS, and any remaining deficit is covered by the National Treasury.

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2 This method for dealing with the benefits accrued in a PAYG scheme contrasts with the recognition bond method used in other countries such as Chile.

3 Workers in the labor force at the time of the reform were given a five month period to choose which regime they prefer, the default option being the funded scheme.

4 As mentioned before, the employers contribution rate can be reduced by decree. Since 1994 a complex scheme of reductions by location and industry is in place, generating an actual contribution rate of approximately 8% as of the end of 1999.

Employees' contributions, and 11 of the 27 points of the self employed, are transferred to ANSeS and used to finance the RPP if workers choose that regime, or transferred to a pension fund (after AFJP fees are deducted) if workers choose the funded regime. In this case, the AFJPs withdraw their commissions from the employee contributions, resulting in a smaller net contribution of around 7.5% of taxable income. If workers do not make an explicit choice, they are assigned to an AFJP.

#### *2.1.4. Benefits*

The public pension regime pays separate benefits to pensioners under the old system, and to affiliates of the new system. The benefits for the new system are the (a) Basic Universal Benefit (PBU); (b) Compensatory Benefit (PC); (c) Additional Benefit for Permanence (PAP); (d) survivorship and disability benefits. In addition, the funded regime offers (e) Ordinary Retirement (RO); and (f) survivorship and disability benefits to those who choose this scheme.

(a) Basic Universal Benefit (PBU) is a redistributive, flat benefit. Retirees of the SIJP who have contributed to the system (either the new or the old one) for 30 years or more are eligible at 60/65 years old (females/males). The benefit level is approximately 28% of average wage.

(b) Compensatory Benefit (PC) is a benefit for individuals who meet the criteria for the PBU for age and years of contributions and have contributed to the old system. They receive 1.5% of pre-retirement income per year of contributions to the old system. Thus, a worker with 35 years of contributions retiring immediately after the reform would have receive a PC of 52.5% of his/her previous salary, while young workers entering the labor force after the reform will not receive any PC.

(c) Additional Benefit for Permanence (PAP) is a benefit for workers who meet the criteria for the PBU and decided to join the second pillar PAYG scheme. They receive 0.85% of pre-retirement income per year of contributions to the new second pillar PAYG scheme. Thus, a worker with 35 years of contributions to this scheme will receive a PAP of 29.75% of his/her pre-retirement income, while somebody who retired immediately after the reform (or who chose the funded second pillar regime) will not receive any PAP.

(d) Survivors and Disability Benefits are benefits for survivors of contributing workers in the second pillar PAYG scheme (limited to spouse and young children of active contributors) or the workers, if they become disabled. Benefits are pre-defined. Disabled workers receive 70% of their salary before the disability and survivors receive between 50% and 70%, depending on the family structure. Benefits are reduced and even denied if compliance has been too low<sup>5</sup>.

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5 The "regularity" rule establishes that only workers with contributions in more than 29 of the last 36 months receive full benefits, those with less than 30 but more than 17 months receive reduced benefits (by 5/7) and those with less than 18 months receive no benefits.

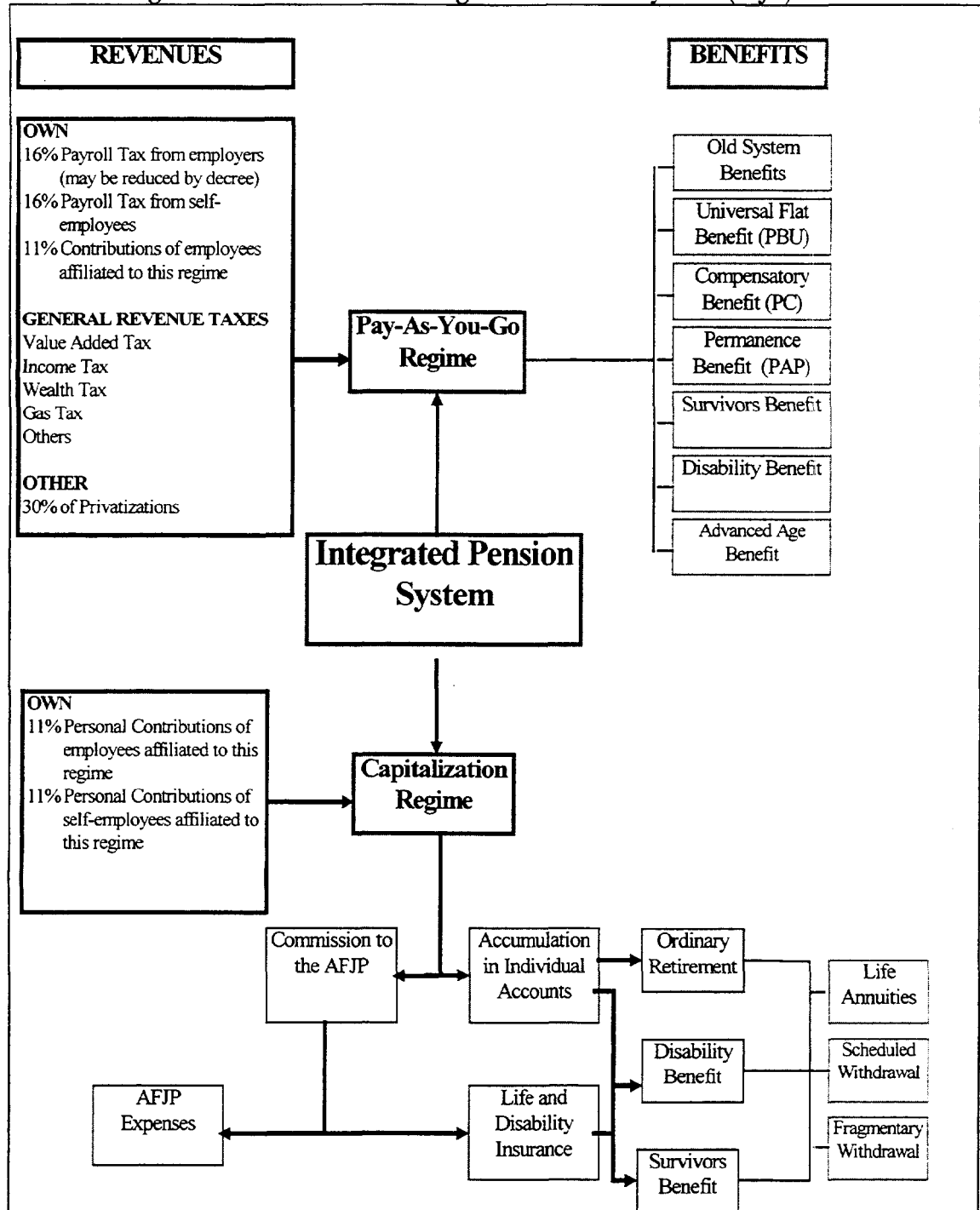
(e) Ordinary Retirement (RO) is a benefit received by affiliates of an AFJP once they retire. This benefit is paid in addition to any other from the RPP that the workers have accrued rights, such as PBU and PC. Benefits are paid in the form of annuities, scheduled withdrawals or fragmentary withdrawals. In the first case, the beneficiary buys an annuity from a retirement insurance company (CSR), and the balance of the account is transferred to this CSR. Annuity contracts are highly regulated and only life annuities that include survivors' benefits are allowed. The basic parameters used to calculate the benefits (life tables and interest rates) are established by the Supervisory Agencies. Alternatively, beneficiaries can leave their balance in the pension fund, and agree with the AFJP to withdraw a monthly amount that cannot exceed what they would get from an annuity. Every year the agreement is reconsidered and amounts are adjusted, with a reduction unless returns were high enough to compensate for the aging process. At any time, the beneficiary may use his balance to buy a regular annuity. In the event of the death of the main beneficiary, the balance of the account is used to finance the survivors benefits (either as an annuity or a scheduled withdrawal, depending on the desire of the survivors) and, if there are no beneficiaries, the balance becomes part of the deceased's estate. The third option, the scheduled withdrawal, consists of a monthly withdrawal from the individual account that exceeds what the beneficiary would get from an annuity, but is less than 50% of the maximum PBU.

(f) Survivors and Disability Benefits are benefits for survivors of contributing workers in the second pillar funded scheme (limited to spouse and young children of active contributors) or the workers, if they become disabled. Benefits are calculated with the same criteria as in the PAYG scheme (including the rules on regularity), but the financial arrangement is different. Once the right to a benefit is established and the monthly amount is calculated, the AFJP must calculate how much capital is necessary to acquire an annuity that would cover such benefit. Then, the AFJP, drawing from the disability and survivors insurance, must complement the balance of the account to reach this amount. Once the money is deposited, the beneficiaries may choose to buy an annuity or agree on a scheduled withdrawal, according to their own preferences. During the transitional years, part of the complementary capital is paid by ANSeS<sup>6</sup>

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<sup>6</sup> The decree 55/94 established that the National Government participates in the constitution of the Complementary Capital with a sum proportional to the age of the workers in 1994.

Figure 1. Scheme of the Integrated Pension System (SIJP)



Source: Isuani, Rofman and San Martino (1996).

As a result of the combination of different benefits, workers in the earnings-related PAYG scheme will receive, once they retire the PBU, PC and PAP, while those in the funded regime will get the PBU, PC and JO. In case of disability or death, members of either scheme will receive similar benefits, although the financial mechanism used is different.

Table 1. Benefits to be received by retiring workers, as percentage of their average salary.

Case	PBU	PC	PAP	JO	TOTAL
A worker with 35 years of contributions to the old system and a salary equal to...					
50% of average	57.8%	52.5%	0.0%	0.0%	110.3%
average	28.9%	52.5%	0.0%	0.0%	81.4%
200% average	14.4%	52.5%	0.0%	0.0%	66.9%
A worker with 20 years of contributions to the old system, 15 years to the new system (in the <b>PAYG</b> regime) and a salary equal to...					
50% of average	57.8%	30.0%	12.8%	0.0%	100.5%
average	28.9%	30.0%	12.8%	0.0%	71.6%
200% average	14.4%	30.0%	12.8%	0.0%	57.2%
A worker with 20 years of contributions to the old system, 15 years to the new system (in the <b>CAPITALIZATION</b> regime) and a salary equal to...					
50% of average	57.8%	30.0%	0.0%	11.1%	98.9%
average	28.9%	30.0%	0.0%	11.1%	70.0%
200% average	14.4%	30.0%	0.0%	11.1%	55.5%
A worker with 35 years of contributions to the new system (in the <b>PAYG</b> regime) and a salary equal to...					
50% of average	57.8%	0.0%	29.8%	0.0%	87.5%
average	28.9%	0.0%	29.8%	0.0%	58.6%
200% average	14.4%	0.0%	29.8%	0.0%	44.2%
A worker with 35 years of contributions to the new system (in the <b>CAPITALIZATION</b> regime) and a salary equal to...					
50% of average	57.8%	0.0%	0.0%	35.8%	93.6%
average	28.9%	0.0%	0.0%	35.8%	64.7%
200% average	14.4%	0.0%	0.0%	35.8%	50.2%

Note: Funded (capitalization) scheme benefits calculated assuming a 4% real interest rate, and 1% real wage growth. Projected mortality rates are used.

Source: Own calculations.

## 2.2 The status of the new system

### 2.2.1. Membership and Coverage

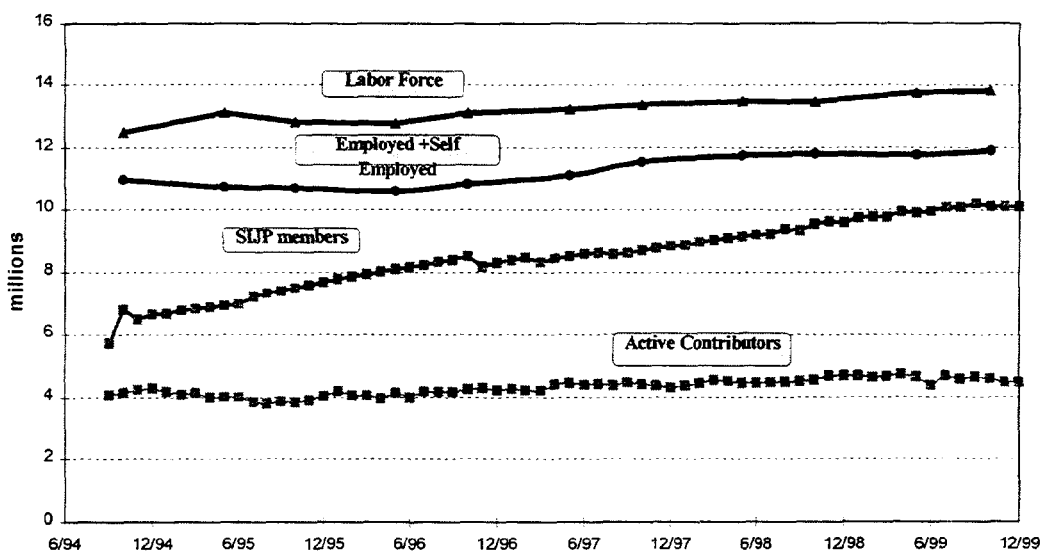
The main difficulty in determining the coverage level of the new pension system is related to the need to define several concepts. Coverage is generally measured by the proportion of labor force that satisfies requirements to receive benefits. Argentina's labor force is currently close to 15 million workers. Not all of them are required to join the SIJP since, as mentioned before, some specific groups are covered by other programs. While there are no official data on this issue, it is estimated that approximately 1.5 million workers are in this group, leaving approximately 13.5 million workers to be covered by the SIJP.

Affiliation to the system (that is, registering and obtaining a social security identification number) is a necessary but not sufficient condition to be covered.

Moreover, it is possible to be affiliated with the system and not to be in the labor force. As of December 1999, approximately 10.1 million workers were affiliated to the SIJP. Of those, nearly 7.9 million were in the funded scheme. Not all affiliated workers contribute regularly. In fact, by the end of 1999, only about 4.5 million workers were contributing, 3.5 million to the funded regime and about one million to the PAYG regime. The ratio of contributors to affiliates shows a steady decline over time, and it is around 45% in 1999. This rate does not reflect compliance, since many workers that should contribute are not affiliated with the system and some affiliates are not required to contribute. This is the case where someone made a few contributions and then withdrew from the labor force, but has not reached the minimum age for retirement. Instead, comparing contributors to labor force not covered by other systems shows that compliance is around 34% (or 39% if unemployed workers are excluded).

Due to the requirements of minimum number of years with contributions, an affiliate is not necessarily fully covered against old age risks. If, for example, a male worker aged 63 years with no contribution history decides to join the system, even if he makes his contributions he will not receive most benefits, because he will not be able to complete the minimum 30 years with contributions. Likewise, somebody with or without contributions in the past, but with no contributions in the last 18 months, is not eligible for survivors or disability benefits according to the rules. The only exception for this is that in both cases, workers have the right to receive a benefit financed with whatever funds they have accumulated in their individual funded accounts, but they have no rights to public benefits or to disability or survivors coverage.

Figure 2. Labor force, employed labor force, affiliates and contributors, 1994-1999

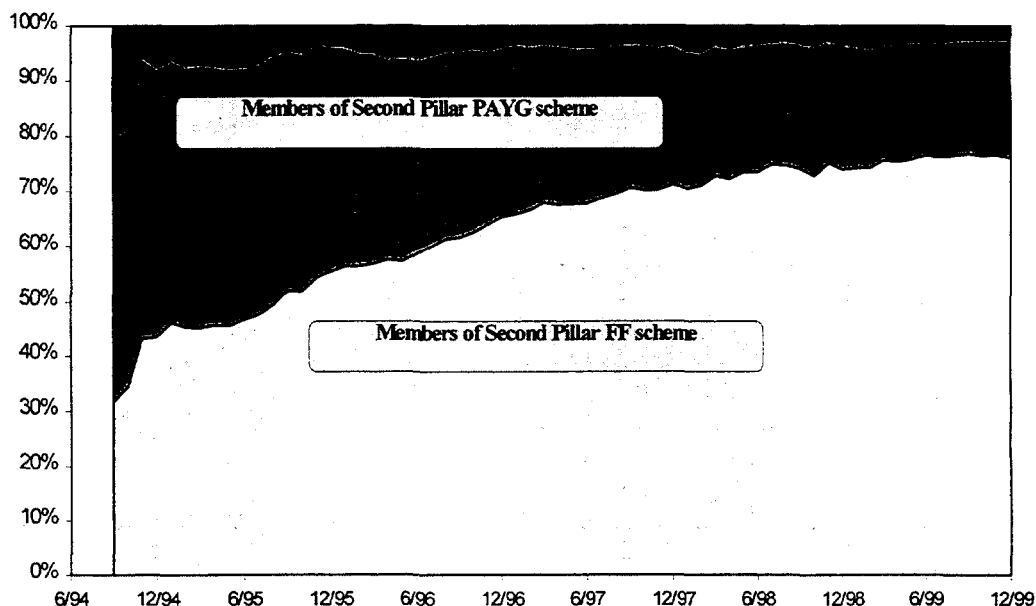


Source: Own, based on data from SAFJP



While no data are available on compliance as defined by the law, information on contributors (defined as affiliates who actually made their compulsory contribution in any specific month) may give an idea of the situation. As of June 1999, the proportion of actual contributors to the estimated number of workers who should contribute was around 37%.

Figure 3. Active contributors to SIJP, according to membership in public and private earnings-related scheme, 1994-1999



Note: The dark area indicates the percentage of contributors that did not make the option and are waiting to be assigned to an AFJP.

Source: Own, based on data from AFJP

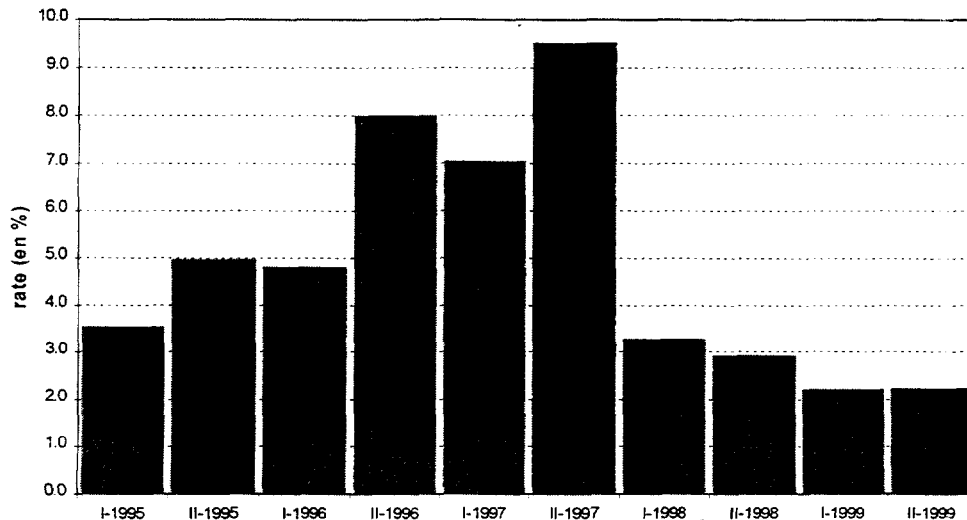
The sustained increase in participation in the funded pillar was caused by several factors. First, the law established that workers entering the system must make a choice between funded and unfunded schemes. If no choice is made, they are assigned to the funded scheme by default. A significant proportion of workers entered the system this way. Nearly 30% of the enrolled labor force at the time the system was created was assigned to an AFJP, and the percentage of new workers that do not express their choice is now as high as 70%. A second reason for this trend is that almost all new workers that do make a choice prefer the fully funded scheme. In addition, most workers that preferred to go into the PAYG scheme were older and consequently, the “replacement” process tilts the balance towards the funded scheme as time passes.

### 2.2.2. Transfers

One of the main characteristics of the new funded scheme is the existence of competition between AFJPs and the possibility for affiliates to switch between them. Argentina’s system allows workers to make up to two transfers per calendar year, with a minimum of four contributions to the fund they are leaving. In five years, there have been 2.6 million transfers, a figure equivalent to approximately about 75% of total

contributors at the end of the period. There have been some significant changes in the rate of switching funds during this period. After transfers were authorized in early 1995, the rate began to increase and reached a maximum during the second semester of 1997, when approximately 9.5% of all affiliates switched funds. A change in the regulations, together with an implicit agreement among the largest AFJPs led to a reduction in the number of transfers. During the second semester of 1999, only 2.2% of affiliates changed funds.

Figure 4. Percentage of affiliates that switched funds in one semester, 1994-1999



Source: Grushka & De Biase (1997) and SAFJP

This phenomenon is of particular interest because, on one hand, it shows the level of satisfaction of affiliates with the service they receive from managing companies and, on the other, the effort to attract affiliates from other AFJP (and to convince their own to stay) explains a significant part of the companies' operating costs.

A study measuring and analyzing affiliate flows since the beginning of the new system found that the most important determinant of the number of incoming transfers is related to marketing policy of the AFJPs. More precisely, the expenditures on marketing and the size of the sales force were found to be critical. On the other hand, the total commission, that represents the cost of the service offered by AFJP, showed no significant correlation with transfers. (Grushka and De Biase, 1996).

### 2.2.3. Fees and Insurance Costs

Managing companies can only charge fees on affiliates' contributions, either as a flat amount or as a proportion of taxable income. The managing companies charge a commission, and use it to pay a life and disability insurance policy and all operational costs of the AFJP.

Fees can take the form of a flat amount, payable every month when a new contribution is made, and/or a percentage of the taxable income payable as a part of the

contribution. The combination chosen is determined by the marketing strategy of the AFJPs. Thus, some companies have adopted a niche strategy, setting a high flat amount and a low percentage, attracting high income affiliates. Others, targeting a wider market, have preferred to charge no flat amount and a higher percentage on taxable income.

Average total charges, including disability and survivors insurance premia, have been around 3.4% of taxable income since the system began, with little change over time. In July 1994, the average was 3.44% (about 31,12% of contributions) and, five years later, it was 3.41%. While total charges did not change, their composition experienced a major transformation: when the system first began, 63.6% of commissions were used to pay insurance premiums and the remaining 36.4% for AFJPs expenses. By mid 1999, the distribution was 27.7% for insurance and 72.3% for the AFJP expenses. This trend started to reverse during 1999 and it is expected that the new insurance policies, valid from mid-2000, will result in a distribution closer to 50-50%.

While selections of insurance companies are made through a bidding process, most AFJP contracts are with an insurance company related to them through ownership. Consequently, it is possible that changes in life and disability insurance premiums are more linked to financial strategies of the related financial entities than to changes in market conditions.

#### *2.2.4. Investment Restrictions and Performance*

##### Description of AFJP structure

Pension fund assets are independent and separated from AFJPs assets. The funds belong to the members and cannot be seized in case of bankruptcy of the managing company. The companies have no property rights over them and the balance sheet is completely separate. Managing companies cannot withdraw money from the funds except for payment of benefits or transfers of affiliates' balances to other funds. Consequently, all expenses related to managing the funds must be covered by the AFJPs, using the commissions they collect on contributions.

The funds are divided in shares of equal value and characteristics. The value of the shares is calculated daily, based on the market value of assets. Annual returns are calculated monthly on a rolling basis, as the ratio of the average share value in a given month to the average share value twelve months before. All AFJPs are required to guarantee a minimum return equivalent to the average for the industry minus 30% or two percentage points, whichever is smaller. Symmetrically, if returns of any fund exceed the average plus 30% or two percentage points, the share value has to be reduced to this maximum level and the excess is credited to a special account (that is part of the pension fund) that serves as a profit reserve.

When in any given 12-month period, a fund's return is below the minimum guaranteed, the AFJP must compensate the affiliates, transferring funds from the profit reserve and, if necessary, from an investment reserve. If both reserves are exhausted and

compensation is still due, the State must pay the difference, take over the administration of the fund and withdraw the license of the AFJP.

The investment reserve is the property of the AFJP and must be maintained at all times. This reserve must be \$3 million or 2% of the fund, whichever is larger. The reserve must be invested and is subject to the same investment restrictions as the pension fund. In short, there is a multi-tier guarantee system to cover possible deficiencies in returns. First, a reserve is formed with the own fund resources. As a second level guarantee, the AFJP maintains an investment reserve. Finally, the State assumes a residual guarantee in case it becomes necessary.

### Investment limits

As part of the system of safeguards, managers confront a number of limitations regarding investment instruments. The limitations aim to force a minimum amount of diversification (setting limits by type of instrument), reduce concentration of risks (limiting the percentage that can be invested in securities issued by one company), eliminate conflicts of interest (prohibiting investments in assets issued by companies related to the AFJP) and reduce overall risk (setting minimum risk rating levels). All certificates, stock shares and any other physical evidence of investments must be maintained under the control of a custodian institution, separate from the AFJP. Valuation of all instruments is made daily by the Supervision of Pension Funds, based on market value. A special valuation method is used for certain public bonds that will be kept until maturity in the funds' portfolios, in order to reduce the volatility of the fund. The AFJPs may invest the pension fund assets in the following categories listed below. There is a maximum limit for each category, defined as a percentage of total assets.

Type of Assets	Limit % of funds
a. Bonds Issued by the National Government	50,0
a.1. Bonds Issued by the National Government, market value	50,0
a.2. Bonds Issued by the National Government, investment account	30,0
b. Bonds Issued by Provincial and Local Governments	15,0
b.1. Bonds Issued by Provincial and Local Governments, market value	15,0
b.2. Bonds Issued by Provincial and Local Governments, investment account	2,0
c. Commercial Papers, long term	28,0
d. Commercial Papers, short term	14,0
e. Convertible Commercial Papers	28,0
f. Convertible Commercial Papers, issued by Privatized Companies	14,0
g. Certificates of Deposits	28,0
h. Equity	35,0
i. Recently Privatized Companies Equity	14,0
j. Mutual Funds	14,0
k. Foreign Government Bonds	10,0
l. Foreign Commercial Papers	7,0

m. Options and Futures	2,0
n. Securities with Mortgage Warranty	28,0
ñ. Direct Investment Funds	10,0
Regional Economies (only Nación AFJP)	max. 50,0 min. 20,0

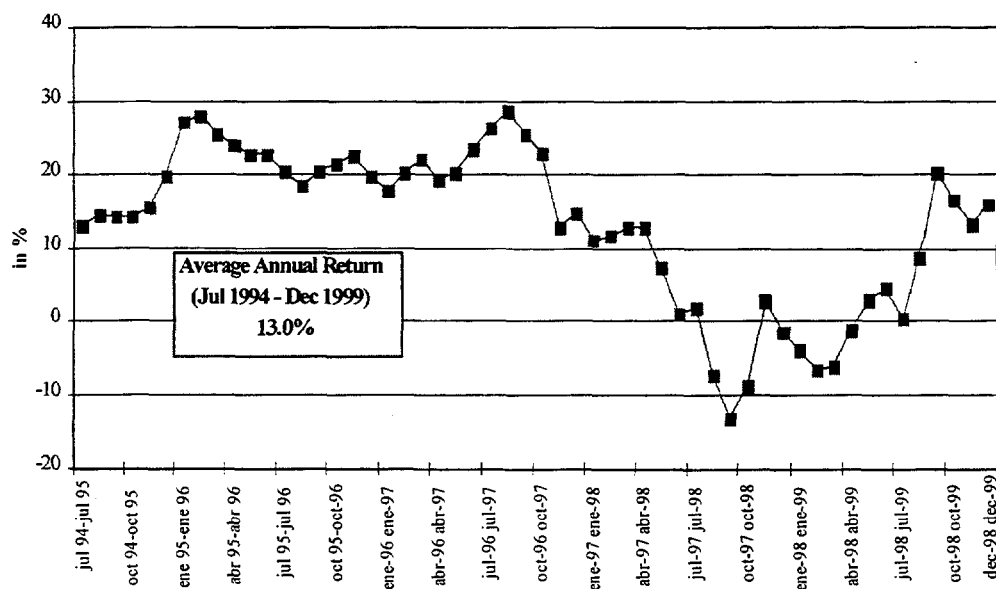
Source: SAFJP

### Performance of the Funds

As of December 1999, pension funds had assets valued at US\$16.8 billion, or about six percent of GDP. Accumulated revenue since the start of the system is US\$ 18.5 billion, almost totally from compulsory contributions. Monthly revenue has been growing over time, as a consequence of the growing number of contributors. The average in the last twelve months is US\$ 360 million. The market is relatively concentrated; the largest six funds receive 83% of contributions, while the six smallest have less than 5%. Because of the wide variation in taxable income, monthly collection per contributor ranges from US\$225 to US\$67, with an average of about US\$100.

Accumulated nominal annual returns for the first six years of operation were around 13%, in a context of very low inflation. Annual returns, measured on a rolling 12-month period, have shown a significant volatility, with a maximum level of 28.8% (in August 1996-August 1997) and a minimum of -13.1% (September 1997-September 1998).

Figure 5. Annual rates of return of pension funds, 1994-1999

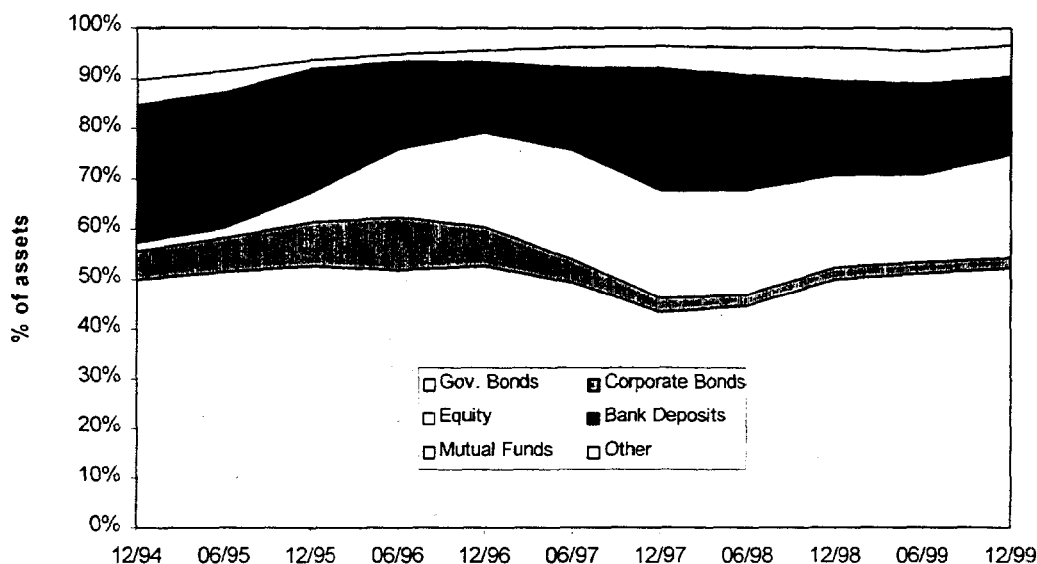


Source: SAFJP

Pension funds are invested in different types of instruments, according to the limits described above. During the first years of operation, government bonds have

absorbed around 50% of the funds, although the percentage was temporarily smaller for some months in early 1998. Certificates of deposit, which started at 27%, have declined to between 15 and 20%. The investments in commercial papers and equities represent approximately one fourth of the assets.

Figure 6. Structure of pension funds portfolio, 1994-1999



Source: SAFJP

The portfolio structure is very similar across pension funds, reflecting a herding behavior described by Srinivas and Yermo (1999). The lack of differentiation among asset managers may be caused by two different regulations – the investment limits and/or the relative rate of return guarantee. The limits have not been binding at any time, with the exception of those affecting government bonds. Instead, the risk of falling below the minimum return and having to compensate fund members with their own assets may have worked as a strong disincentive for diversification among pension fund managers. Returns have been high (13% annual average), but Srinivas and Yermo showed that they might have been higher if asset managers had followed a benchmark portfolio. On the other hand, volatility has been much lower, reducing the short term risk for future pensioners.

Investment in foreign assets has been minimal, well below 1%, despite the fact that regulations allow a maximum of 17%. The main reason for the lack of international diversification seems to be that asset managers preferred to invest in local instruments, aiming at higher short term returns.

### 3. THE PROBLEMS OF THE NEW PENSION SYSTEM

The new pension system in Argentina has several important advantages over other pension systems –both traditional and those recently reformed ones. Having two clear and explicit pillars, a redistributive pillar based on a pay-as-you-go design, and another one proportional to contributions as a fully funded scheme, the SIJP allows a better distribution of short and medium term risks, both institutional and financial.

However, there are some serious problems with the Argentine Pension System. These problems are not necessarily caused by the system design or performance, but nevertheless they result in lower coverage, lower benefits or higher costs, and, consequently, influence the efficacy of the system. Some of the main problems that can be identified when considering the design and performance of the new pension system are with the PAYG scheme, while others are specific to the funded regime. Regarding the PAYG scheme, there are the problems of low coverage of the system and the financial sustainability of the scheme in the medium and long term. The most serious problems in the funded scheme are those related to the charges paid by members.

#### 3.1 Coverage

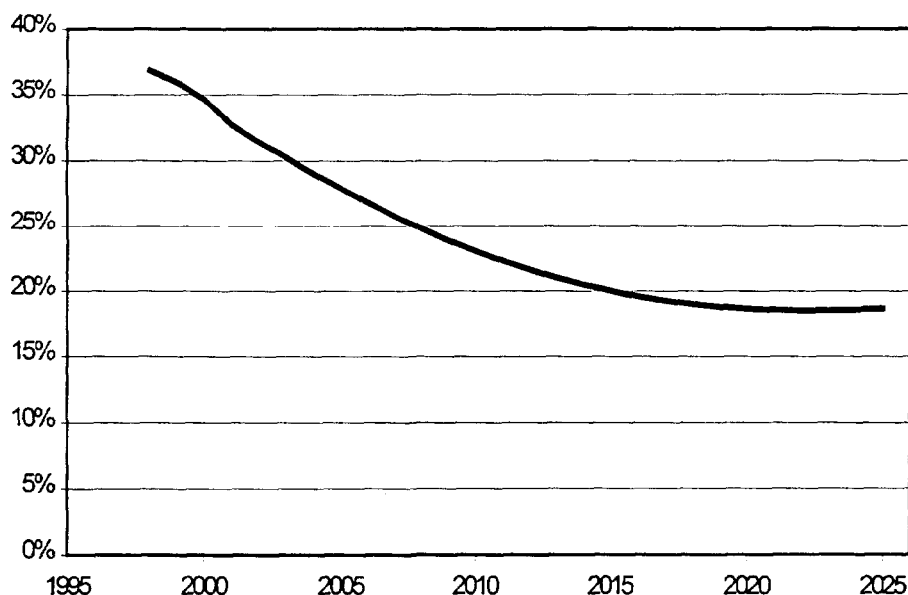
Public pension systems around the world have the general goal of offering the highest possible benefits to the largest possible population, within a budget constraint. The Argentine Social Security System has traditionally had both a high level of benefits (replacement rate target of 82% of gross wages), and coverage. As of 1995, nearly 70% of the population over 65 years of age had a pension benefit. To achieve these levels however, the pension system incurred huge financial obligations, and one of the main reasons behind the reform in 1994 was to control rapidly growing pension expenditures.

In the past, high coverage, despite historically low female labor force participation that has only recently begun to increase, was due to relatively easy access to benefits. Low contribution year requirements, plus a number of exemptions resulted in a high coverage rate measured by the proportion of elderly receiving benefits. As the number of beneficiaries expanded without a corresponding increase in revenue, the resulting financial difficulties led to a reduction of average payments and increasing deficits. The new social security law established several new restrictive requirements, including a five year increase in the minimum age and a ten year increase in the number of years of contribution required to retire. Requirements for eligibility for disability and survivors benefits were made more stringent. The combination of these measures will gradually reduce the percentage of older persons receiving pensions, other things constant.

The trend could be reversed or at least reduced if the level of formality in the labor force and compliance of social security contributions increase significantly in future

years<sup>7</sup>. Unfortunately, the evidence from 1994 to date shows that the number of actual SIJP contributors has decreased slightly in absolute terms once we exclude the effect of the absorption of several provincial systems. Moreover, due to the aging in society, projections indicate that coverage will seriously decline in the next few decades. For instance, the proportion of individuals reaching the normal retirement age who will actually receive a retirement benefit could decline by nearly 50% in the next 25 years, even if the level of formality in employment increases steadily.<sup>8</sup> This decline is mostly explained by the increase in the vesting period to 30 years and the declining formality in labor markets in the last 20 years. Many of today's retirees obtained their benefit under much easier eligibility rules years ago, and the proportion of the labor force with formal employment is now below 50%. Thus, as current beneficiaries age and die, the flow of new beneficiaries will be barely enough to maintain the total number of retirees around the current level, while the older population will grow steadily, resulting in a decline in coverage.

**Figure 7. Persons older than the minimum retirement age in the SIJP eligible for first pillar benefits as a percentage of the same age population. 1998-2025\***



NOTE: (\*) The indicated percentages do not represent the total social security coverage of Argentina, but only the proportion receiving a Retirement benefit from the SIJP.  
Source: Stirparo (1999)

7 This effect was expected by proponents of the reform in the early 1990s. The main argument was that the higher incentives to contribute would increase compliance quite rapidly.

8 The values projected assume that the female activity rates will grow slowly, reaching 50% by 2050; unemployment is assumed to decline to levels close to 7% in 2009, and the percentage of employed who contribute to the SIJP will reach 50% in that same year.



The stagnation in the number of contributors to the SIJP is worrisome, since it was expected that the introduction of the individual account scheme and the reductions in employers' contributions established in recent years would act as incentives to increase participation. Although it is not possible to determine unequivocally the reason for such low compliance, a number of processes, such as an increase in unemployment, and the proliferation of informal hiring mechanisms had a role in the poor performance of the new system with regard to participation. The solution to this problem is not simple, mainly because informality has deep structural causes that go beyond the design of the pension system.

The first issue to address urgently is related to the situation of self-employed workers. Law 24.241 requires that they contribute 27% of a predefined income to the social security system plus 5% to old age health insurance. There are ten income categories, and workers are assigned to them according to activity, seniority, et cetera. This structure generates important inequities among self-employed workers (because workers with similar income levels pay different contributions) and between self-employed workers and employees. Any self-employed worker who receives an average monthly income of \$300 has a clear disadvantage in relation to employees, because the labor taxes paid will be higher. In the same way, self-employed workers with higher income could be affected because they are included in an excessively high category for their real incomes. In other cases, they may be paying too little. The low percentage of total contributions that is effectively transferred to their individual accounts (approximately 23%), and the regulations on collection from self-employed workers that have had a tendency to raise the required contributions (by almost 65% in real terms from the beginning of 1994 to 1997) are a strong incentive to evade the system. Besides, the system currently includes several discriminating features for this group, such as not applying the recent reductions to the employer contribution rates or the requirement that contributions be paid within established terms to be considered in the estimates of regularity for survivors and disability benefits – a condition that does not apply to employees. Because of these problems, the number of self-employed contributors to the SIJP dropped between 1994 and 1999 from approximately 1.3 millions to slightly more than 700,000<sup>9</sup>.

It is both necessary and feasible to implement policies that facilitate the participation of self-employed workers. Certain measures like improving the link between contributions and net income would improve the transparency and the equity of the system. It also seems reasonable to extend to self-employed workers any benefit that is given currently to employees, like the reduction of employer contributions. The link between contributions and real income would eliminate the huge incentive to evade that currently exists for self-employed workers who do not hold a regular activity, because it would eliminate an important bureaucratic constraints to entering and exiting the self-employed condition, currently in force.

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<sup>9</sup> Further research on the elasticity of participation among the self-employed to the marginal tax rates imposed on them would be useful for assessing the potential for increasing coverage.

A second measure worth considering is a serious review of the collection system. For many reasons, the Tax Authority has not been efficient in reducing evasion. Broad policy measures, such as reductions of contributions by employers and tax amnesty offers have been taken without much success. Clearly, it is necessary to improve the enforcement strategies of the collecting agency, which seem to be weak.<sup>10</sup>

Finally, it is important to mention that, even if participation by active workers increases, the number of individuals who will reach retirement age without the minimum contributions will grow in the next ten to twenty years, due to their lack of contributions early in their labor careers. For the lower income members of this group, a non-contributory pension will be needed.

### 3.2 The financial viability of the Public Social Security System

The financial viability of the public scheme or RPP has been a controversial issue, due to the difficulties it will face in paying benefits due both to the underlying structural deficits as well as the loss of revenues during the transition period. Additionally, the policy of reducing employer contributions has significantly affected the finances of the ANSeS, reducing contributions by approximately 40% by mid 1999.

In the analysis of the financial situation of the public system, it is important to look separately at the expenditure and revenue issues. The system expenditures on Social Security benefits are related to the number of beneficiaries and their average benefit levels. The process of population aging in Argentina, along with the maturity of the pension system meant that the number of beneficiaries tended to grow steadily over time. The 1994 reform tried to restrict this effect by increasing the retirement age and imposing more stringent requirements to obtain benefits. It also reduced future benefits payable by the PAYG scheme, by effectively transferring part of them to the new fully funded scheme.

The future evolution of the PAYG revenue is not simple to analyze, mostly because the scheme is not expected to be self financing in the future. The Argentine pension system has been allocated a growing flow of earmarked non-payroll taxes in recent years. The system was running a significant deficit before the reform and, of course, the creation of the second pillar reduced revenue. However, other policy measures had an even greater effect on collection. As discussed above, the Government has slowly reduced the employers' contribution rate from 16% of gross wages to nearly 7.5% by the end of 1999. In addition, new legal contractual forms were authorized to promote labor demand, allowing in many cases the deferment or elimination of contributions for some categories of workers. Consequently, by the end of 1999, almost 65% of benefit expenditures were financed by sources other than payroll tax contributions and this percentage continues to grow.

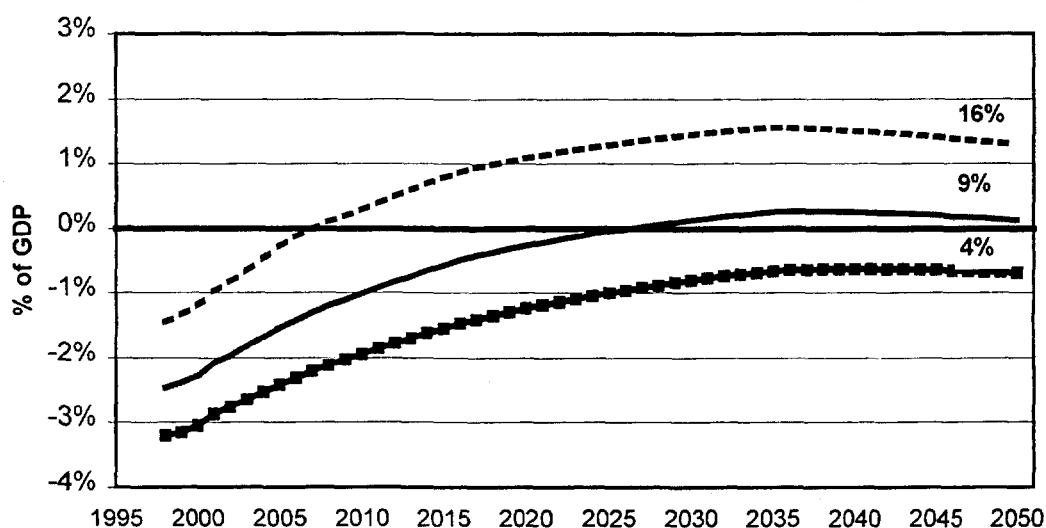
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<sup>10</sup> For a detailed description of the collection system in Argentina and other Latin American countries, see Demarco and Rofman (1998).

The evolution of the financial situation of the RPP will improve in future decades for the same reason that the coverage problem will emerge. The projections show that the public scheme's finances should improve significantly due to stagnation and even a decrease of the number of beneficiaries and to a reduction in the amounts paid as benefits begin to be replaced by those of the funded scheme. Obviously, if that happens, the system will be in better financial shape, because of the exclusion of an important part of society from the system. On the other hand, if the population excluded from the Social Security system were covered by a non-contributory pension of some kind, part of the financial savings would be offset by new expenditures in this area.

Of course, the financial outcomes for the RPP<sup>11</sup> will depend directly on the decisions adopted in relation to employer contributions. Figure 8 shows the results of a projection under three different assumptions regarding the rates of contributions: 16% (indicated by law), 9% (approximately the current level) and 4%, a minimum level<sup>12</sup>.

Figure 8. Projected financial result of the RPP, according to different levels of employer contributions. 1998-2050



Source: Own, based on Stirparo (1999)

As shown, if a 16% rate were applied, the accounts would tend to equilibrate by 2010, while, with the current rate, an equilibrium level would only be reached by 2028.

11 In this paper, we consider the financial result of the RPP as the difference between ANSeS revenues coming from social security contributions and its expenditures due to social security benefits. Consequently, we exclude the effect of tax resources, transfers from the treasury, collection or payments of other ANSeS managed systems, etc.

12 This model assumes a slight growth of the activity rate, a drop of unemployment rate to levels close to 7%, an increase in the percentage of employed people who contribute from current 40% to 50%, a drop in the percentage of employed workers and a steady increase of participation in the funded scheme, reaching 100% of workers by 2025.

If further reductions were made the system would not be able to avoid a chronic deficit situation. The fiscal effect of the reduction of employer contributions is clear: each point of reduction in the rate currently translates into a loss of approximately \$450 million (0.15% of GDP) per year in revenues that must be financed with funds coming from other sources. This does not take into account any positive impact on the number of contributors that could be linked to lower labor costs, but four years after employers' contributions began to be reduced, there is no evidence that such an effect can be expected.<sup>13</sup>

### 3.3 Benefit uncertainty

Law 24.241, which created the SIJP, established an automatic indexation mechanism for all the financial variables of the system. Benefits of the RPP, the minimum and maximum contributions, the fines applicable to AFJPs and contributions of self-employed workers were all defined as a function of the Average Individual Mandatory Contribution (Aporte Medio Previsional Obligatorio-AMPO). The AMPO would be recalculated every semester and its evolution would follow the evolution of average wages of the economy. Therefore, the system would be completely indexed to the wage level. This criteria was an important advance with regard to the previous system, which established multiple criteria for the different variables in particular, a link between the benefits and a wage index estimated by the Ministry of Labor and Social Security, whose methodology was far from being transparent and led to thousands of lawsuits. The value of the AMPO was calculated by the end of 1993 based on the Social Security collection during the first semester of 1993 at \$61. Between this date and the first semester 1997, this value was increased by 31% reaching \$80. This important change does not reflect an increase in workers wages (which, based on data from the same source, grew by approximately 3% between 1993 and 1999), but several methodological effects, in some cases unexpected and in other cases resulting from clear mistakes made by government officials. As a reaction to the fiscal cost that indexing all benefits would produce, the government modified the law and replaced the AMPO with a new index (the Social Security Module, Módulo Previsional-MOPRE). The MOPRE value is defined by the Ministries of Economy and Labor (its value has been set at \$80 since 1997).<sup>14</sup>

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14 At the beginning of 1995, and because of the evidence that a 14.3% increase in the AMPO would generate a similar increase in Social Security system expenditures, the national government issued a Decree of Necessity and Urgency, afterwards confirmed by the Social Security Solidarity Law, that eliminated indexation, and instead ties adjustments to the definition the Congress adopts every year when it discuss the National Budget. This measure, justified by the impossibility of paying the foreseen increases, eliminated a quite important component of Law 24.241, the automatic indexation procedure. Additionally, the Social Security Solidarity Act determined the freezing of benefits that were being paid, but it did not modify the mechanism to determine new benefits. Consequently, inequities started to emerge, since different workers received different amounts of money as PBU, depending on the date of retirement. By the end of 1997, again through a decree, the national government replaced the AMPO with the Social Security Module (Módulo Previsional-MOPRE), a unit whose value is determined by the Ministries of Labor and Economy and that would determine the movement of all variables in the system.

The lack of automatic indexation mechanisms seriously affects the predictability of the system, for both beneficiaries and policy makers, and it increases the possibility of political manipulation. Therefore, it is necessary to reinstall a methodology that ties the value of the benefits to an objective indicator.

### 3.4 The cost-effectiveness of the Funded Regime

#### 3.4.1. *The costs of the AFJPs*

The system is designed in such a way that the funded scheme channels improvements in the economy at the macro level to beneficiaries. It also diversifies risks and protects the contributors from possible political manipulations of benefit levels. To fulfill these functions adequately, it is necessary for the system to generate reasonable rates of return, with reasonably low costs and limited risk.

Two of the main problems the funded scheme has faced since its creation are its relatively high operating costs and the risks to which contributors are exposed. Currently, the average commissions including disability and survivor insurance premia are slightly over 3.4% of the taxable income (or 30% of the tax collection). This seems high when compared with other countries with similar systems.<sup>15</sup> It is interesting to note that this high average is due, in part, to the existence of very low price elasticity in demand. The average commission could be approximately 2.95% if each contributor chose the cheapest AFJP for his/her level of income. (Of course, this comparison makes the possibly unrealistic assumption qualitative differences (e.g., service) across the AFJPs are not related to price.)

The debate on the magnitude of the costs has been heated<sup>16</sup>. It is obvious that to define whether a service is expensive or cheap is necessary to have a reference criterion, comparing the cost with other similar services, or trying to evaluate the utility the contributors get from the service. Whitehouse (2000) points out that the key question is what effect do charges have on the net rate of return. While costs may be high relative to comparators, returns in Argentina have also been high, even after these charges.

Fees of approximately 30% of contributions look high. However, it must be noticed that there are no asset fees or any other charges except for the up-front fees. Considering an individual with contributions for 35 years before retirement, it is simple to estimate that a 30% fee on contribution is similar to a 2% annual fee on assets, if we include the cost of disability and death insurance in the calculation, and 1% of we exclude this cost. Thus, it is possible to estimate that the effect of administration fees on

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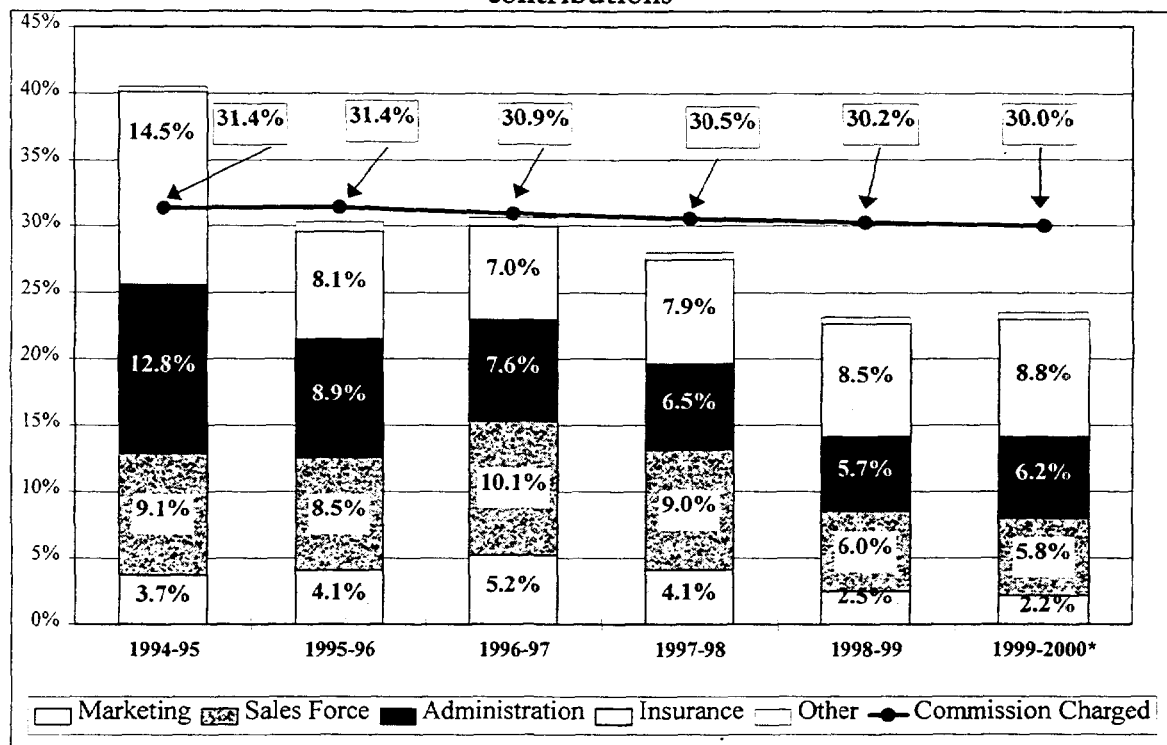
<sup>15</sup> Currently, the commissions in other Latin-American countries reach 27.2% in Peru, 25.9% in Colombia, 21.5% in Chile (where there has been a decreasing tendency from the inception of the system) and 17.6% in Uruguay, always in relation to total contributions and including insurance premia.

<sup>16</sup> For the international debate, see Whitehouse (2000).

long term returns should be between 0.7 and 1.5 percentage points. Of course, this effect will be larger if workers participate in the system for shorter periods (as would be the case of an older worker that joined the funded scheme in 1994) and smaller if workers contribute for more than 35 years. Nevertheless, lower costs are clearly desirable, and recent returns may not be maintained at such high levels in the long run.

While some analyses have found that the costs are actually low when compared with other alternative financial products, this comparison is fraught with problems. While comparisons are complex, it is interesting to consider the destination of the resources received by the AFJPs. Figure 9 shows the structure of operating expenses of the AFJPs, as a percentage of the social security collection for each fiscal year (July-June), since the beginning of the system.

Figure 9. Commissions and operating expenses, as a percentage of the collected contributions



Note: 1999-2000 includes July 1999 to March 2000.

Source: Own, based on data from the SAFJP.

We can easily observe that the total costs have decreased since the beginning of the system –when they exceeded 40% of the collection–, up to the fifth year –when they are below 25%. This reduction was due originally to lower costs of disability and death insurance and the reduction of administrative expenses. Since late 1997, the reduction in expenditures on marketing and sales force has been greater. Regardless of the evolution of expenses however, the level of commissions has been practically fixed from the beginning of the system, with a slight downward tendency. Therefore, the operating profits reached by the AFJP in recent years have been positive and with a tendency to

grow, reaching a record of 7% of total collection (or 23% of AFJPs' gross revenue). The reduction in costs may have reached a limit in recent months, as sales force compensation has leveled and insurance costs are rising. Nevertheless, the high operating profits could be indicating that the market is not as competitive as it could be, and some policy measures to increase competition should be adopted.

Two different approaches have been proposed to reduce the fees in the system. One proposal is that the government should promote a reduction in costs of the managing companies, as an indirect way to reduce charges. For example, a draft law has been presented in Congress to set maximum levels of commissions. While well intentioned, such measures could result in higher market concentration and decline in quality of service, as well as market cartelization. Instead, policies that would promote price competition may achieve a similar result without the negative outcomes.

In an attempt to reduce costs, industry representatives have proposed limiting workers' rights to switch funds. The logic of this restriction is that fewer switches will lead AFJPs to reduce expenses in areas related to attracting new contributors. This measure could facilitate a reduction in the expenses of AFJPs (because they would not need to spend as much on marketing), but it would limit the possibility of choice of the contributors and, therefore, the efficiency driven by competition. Consequently, the drop in AFJP costs would not necessarily be translated into reductions of charges if the administrators tend to collude, and we could end up with a more concentrated, less competitive and equally expensive system.

Alternatively, other authors as Braberman and Chisari (1999) have proposed simplifying and liberating the rules for transfers. The idea in this case is that the existing restrictions to transferring from one AFJP to another reduce competition in the market, and increase the benefit a managing company obtains when a worker joins them. Instead, if the contributor could change without the intervention of sales representatives (through automated mechanisms) and as often as he/she wants, the "value" of adding a contributor would be lower and the AFJPs would not spend large amounts to attract new affiliates.

Clearly, an approach that promotes higher competition should result in lower fees. However, if the sensitivity of the contributors to differences in AFJPs costs is low, then incentives for the AFJPs to compete on prices are small. If all contributors chose to transfer to the lower cost AFJP according to his/her income level, the average commission will be reduced by 15% without changes in fees by any AFJP. To increase cost awareness among fund members, it is necessary that the supervisory agency (the Superintendency of AFJPs) provide information about the AFJPs costs and their effect on future benefits. Both mass media and traditional communication channels with the existing contributors should be used as much as possible.

An interesting approach can be observed in the mechanism of allocating undecided affiliates. According to the current regulation, workers entering the SIJP must choose within 30 days whether they want to join the second pillar PAYG scheme or any specific AFJP. If they do not act, they are distributed randomly among the existing AFJP. The number of workers who have entered the funded regime through

this mechanism is quite high, almost 30% of the total number of current contributors. The figure is even greater with respect to the flow of new contributors in the year, reaching almost 60%. The criterion for allocating undecided workers from the beginning of the system up to September 1997 was to assign them proportionally by their market share. Since then, they have been assigned in equal proportions to all AFJPs. If, instead, they were assigned to the AFJP with lowest commission, this should reduce the average cost. On one hand, more contributors would be in the lowest cost AFJP, but it would also create a strong incentive to compete on prices<sup>17</sup>.

### Market Concentration

The process of concentration in the sector –which had 24 administrators operating when the system began and 13 by the end of 1999 – should be carefully monitored. As of the end of 1999, more than 70% of the contributors belong to 4 AFJPs, with the largest one covering 21% of the market. While it is desirable to allow the different companies to develop their own strategies to reach the optimum number of contributors for their scale of activity, the risk of an excessive concentration that restricts competition in the industry should be considered. In this context, it would seem reasonable to consider concentration limits (e.g., a maximum 20% share) in order to avoid a situation where one or two firms control the market.

#### *3.4.2. Regulation alternatives to increase the efficiency: The problem of volatility*

Another issue that deserves some attention is the risk AFJP contributors face due to volatility of returns on investments. Volatility generates two different problems. First, volatility of the funds while workers are still active affects credibility of the system, since workers may see their individual account balances drop rapidly in some periods. This does not generate any immediate harm to the workers, because their benefits depend on the balance of their personal accounts when they retire, and not before. Nevertheless, the Superintendency limits investment in highly volatile instruments as well as investments on low liquidity instruments with non-transparent markets.

Volatility at the time of retirement is more important, because of the real possibility that individual account balances are abruptly reduced immediately before an annuity is purchased. One question to consider is how sensitive is the benefit a worker will receive from the SIJP to changes in capital markets. Considering the role of PBU and PC, plus that an important percentage of pension funds assets are fixed return instruments, it is possible to show that a drop in the capital markets would have a minor effect for all the workers who retire in the next few years. This is because neither the PBU nor the PC are affected by capital market volatility, and, at the same time, the benefit generated by the individual account of the funded scheme will be small. In the longer term, the effect would be still be small for many workers, since more than 50% of them may expect to receive more than half their retirement benefit in the form of a

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17 Additionally, it would seem reasonable to give to the undecided people who are entering the system a period of time to decide if they want to shift to the pay-as-you-go regime, in order to increase the possibility of exercising their freedom of choice.



PBU. These lower income workers will receive a high share from the flat, public benefit because the level is high relative to their own wages.

Although the magnitude of the problem seems to be smaller than thought, it is reasonable to explore alternatives that restrict its effect. One possibility is that the AFJPs offer their clients a second portfolio concentrated in fixed earnings instruments. This fund would allow members to restrict their exposure to market volatility, decreasing the risk of retiring at a relatively low level, although it is clear that the costs of more security will be reflected in lower expected returns. If a measure like this is implemented, it would be important to limit the possibilities of making fast and full transfers from a “traditional” to a “conservative” funds, in order to reduce the negative effects of financial panics.<sup>18</sup>

Another alternative is to allow the progressive acquisition of deferred annuities. If, for instance, a worker is five years from retirement, he could start to progressively acquire an annuity, transferring 20% of the individual account balance to the retirement insurance company chosen by him every year. This would further reduce his exposure to short term variations in the market, because these would only affect part of the funds. This mechanism is relatively simple to implement, because it would only require a choice of retirement insurance company in advance with an automatic transfer the funds progressively. The application of such an idea should be seriously considered for the medium and long term, when the benefits of the funded regime start to be a more significant part of the retirement payment. However, a successful implementation requires the existence of annuity providers operating in the context of a strong and well-regulated insurance industry, a requirement that is far from being fully achieved in Argentina, as we will see next.

### 3.5 The insurance industry and its relation with the pension system.

Insurance companies have a role in the pension system at two different stages. First, AFJPs are required to buy an insurance policy to cover disability and mortality risks. If a worker contributing to the fully funded scheme dies or becomes disabled, the AFJP is required to complement his individual account balance up to an amount enough to buy an annuity that would provide a lifetime defined benefit. In addition, beneficiaries may choose to receive their monthly payments through an annuity provided by an insurance company. The markets for both activities seem to have serious problems of competition and regulation as discussed next.

#### 3.5.1. *The disability and death insurance*

In the case of disability and life insurance, practically all the insurance companies are part of the same economic group as the AFJP that contracts them (the only AFJPs that do not contract related companies are the two smallest, with less than 1.5% of the market). This situation makes it very difficult to assess whether the prevailing insurance rates correspond to reasonable market value or if they reflect financial transfers between

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18 This option is already available in the private pension systems in Chile and Poland.

related companies. Grushka (1999) showed that there is an important dispersion in the fees, ranging (in December 1998) from 0.59% to 1.45% of the taxable income, with no relationship between these differences and any characteristic of the insured population, such as the scale of the AFJP, gender, employment condition, age or income level of the contributors.

Additionally, there are no serious studies about incidence rates, making extremely difficult to assess if insurance companies' reserves are adequate, insufficient or excessive. Currently, the retirement insurance industry reports an annual loss of \$25 million, and re-insurance companies lost more than 120 million. These figures should be analyzed considering that there are serious difficulties in defining the adequacy of the established technical reserves. As a matter of fact, a generalized problem in the industry is that the reported deaths and disabilities are significantly less than the expected ones, therefore it is possible that excessive reserves are accumulating, affecting the result in a negative way<sup>19</sup>.

Insurance company officials have mentioned that available data indicates a possible underestimation of real costs by re-insurance companies, allowing them to charge less than expected. If this is correct, we could expect an increase in insurance cost in the next few years, as re-insurers correct their estimations. Also, the participation of ANSeS in financing the transition period will decline over time. The increase in individual account balances (due to longer periods of contributions) may not seem to be enough to compensate this, resulting in an additional trend towards increasing insurance costs. An active role of the Supervision to increase transparency in the contracting process and generate reliable incidence data will be important to prevent the disability and survivors benefits from becoming a major problem in the system.

### *3.5.2. The benefits in the funded scheme*

The new system allows beneficiaries from the fully funded scheme to choose whether they want to receive their payout as an annuity (through a retirement insurance company) or as a scheduled withdrawal. In this last case, the beneficiary remains a member of the pension fund, and he makes monthly withdrawals from his individual account, maintaining the ownership of the funds<sup>20</sup>. The main reason to create this mechanism was to introduce competition with annuity providers. But it also has several negative effects in the system. It gives workers the possibility of opting out of annuity markets, opening room for adverse selection. Since regulations establish that in the case of death of the beneficiary with no spouse or underage children the balance of the account will be inheritable following normal criteria, part of the resources accumulated for retirement may end up being transferred out of the system, reducing the average

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19 The reason why there are "too few" deaths is not clear. On one hand, it is possible that the assumptions made by the insurance companies are exaggerated, but it is clear that the mortality levels reported are significantly lower than the expected ones for the Argentine population in general. Among the possible causes, we could find an important delay in processing the applications, ignorance by survivors, etc..

20 The amount withdrawn every month must be agreed with the AFJP, with a maximum limit equal to what an annuity would pay to this beneficiary.

benefits that are paid to the beneficiaries. Grushka (1999) estimated that the loss of funds might cause a reduction of as much as 15% in average benefits as a result of unintended bequests.

With regard to market transparency, there is a serious problem in the annuity providers industry. More than 85% of annuities are issued by a retirement insurance company tied to the AFJP where the beneficiary was affiliated prior to retirement. This suggests that competition is very weak. A partial explanation of this situation is the total lack of transparency in the market. Each insurance company offers an annuity product structured in a different way, making almost impossible to fully compare them. Regulations should aim to produce simple product, making easier the comparison among different offers.

There are other problems in the way annuities are defined that make them more expensive for retirees, reducing the benefits. On one hand, mortality assumptions currently used are based on higher life expectancies than the real ones for the Argentine population, generating a reduction in benefits of 6 to 8% (Grushka, 1997). It is not clear whether these reductions are justified by higher life expectancy of annuitants. At the same time, no indexation is included in the contracts, so that the real value of benefits could drop significantly. This problem is partially solved since annuities can be defined as variable (with a percentage of returns obtained over the guaranteed 4% being transferred to beneficiaries) and they can also be defined in U.S. dollars, reducing the country-specific risk.

Finally, the mechanisms of financial and institutional supervision of the retirement insurance companies seem to be less solid than those applied to AFJPs. The reason is, partly, the institutional weakness of the National Superintendency of Insurance, as well as differences in criteria used by insurance versus pension system regulators. The debate over the need for appropriate regulations and market transparency in the annuity providers industry in Argentina and other Latin American countries has been growing over the past couple of years. Palacios and Rofman (2000) present a detailed discussion on the current situation and policy options on this issue.

#### 4. CONCLUSIONS

This paper presents a general overview of the pension system in Argentina after the 1994 reform, describing the basic features of the new system and presenting some information on performance during its first six years. The main section is devoted to considering the problems that have to be confronted and solved in order to guarantee successful development of the system in the future.

Four areas critical for the consolidation of the system are identified. The first one is the coverage level, which will tend to decrease in the future unless structural changes take place quickly in the labor market in Argentina. The reform of the social security system implemented in 1994 made the contributory elements stricter in terms of eligibility (especially the thirty year vesting period). This leads to greater financial stability but at the cost of excluding a group of individuals that would have otherwise received benefits. While this goal may seem reasonable to promote compliance, it has made it necessary to develop an efficient and transparent non-contributory pension system, in order to offer some financial support to the people who do not have access to the benefits of the system. This would of course, offset the fiscal savings from the reformed public scheme to a certain extent.

The second issue, financial sustainability of the public scheme (which includes the old system, the new first pillar, the new PAYG second pillar and the transitional benefits) seems stable in the medium term, as a consequence of the reform. Nevertheless, the financing of the transition process, that will take approximately 20 years, should be planned in more detail. In addition, the reductions in the current and planned employer contributions will strongly influence the system's financial balance. In particular, there should be an explicit allocation of tax resources to cover the projected deficits caused by the reduction in earmarked labor taxes. It is interesting to note that there is so far no evidence that reducing labor taxes has had any positive impact on formal sector participation and compliance, although more study is needed before conclusions can be made.

Due to errors in the original implementation, the automatic indexation of the benefits of the public regime was eliminated in 1995, so that benefit adjustments are now defined on a discretionary basis by the government. It is important to reintroduce a technically and financially reasonable mechanism for automatic indexation, to increase the transparency and predictability of the pay-as-you-go system.

The challenge of reducing administrative costs of the fully funded scheme was highlighted. Mechanisms to reduce them should be found while protecting the competitive aspects of the new system. Among the reasons identified that may explain costs, it is clear that the low price elasticity of demand is fundamental. In fact, the contributors do not seem to make their choice of AFJP taking into account the commission they are charged. To correct this, it is critical that supervising institutions make an effort to increase the information the affiliates have on the subject. An issue that should also be considered carefully is the level of concentration of the industry,

which could lead to cartelization and price collusion. Therefore, careful supervision is required. Replacing the current mechanism of allocation of undecided contributors with one that favors the AFJP with lower fee would certainly generate an incentive to reduce the commissions.

Much has been said about the need to protect contributors from short-term market volatility. This problem may have received more attention than warranted in Argentina, since a large part of benefits will still come from the public scheme, and short term volatility during contributing years have no serious consequences for most workers. Some additional protection to retiring workers could be devised, such as creating a second, less volatile portfolio for those close to retirement, or allowing the acquisition of deferred annuities before retirement, but neither solution seems critical, nor are the proposed solutions without their own problems.

The disability, life insurance and retirement annuities market present potential conflicts that should be resolved. The main problems in this area are concentrated in the lack of reliable studies on incidence rates (which might be much higher than currently estimated), the use of unreasonable assumptions in actuarial estimates, and the weak competition in the markets. Besides, the supervision of the industry is also weak and rather slow, generating important risks to the system. Regarding annuities, we conclude that mandatory annuitization of benefits (eliminating or limiting scheduled withdrawals) is to be recommended, although serious work to improve efficiency and competition in the annuities market is required.

In short, the new Argentine social security system, after six years of operation, is still going through a development process and a number of problems, some of them important in the medium term, and others more urgent, should be corrected.

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## STATISTICAL APPENDIX

(Source for all tables: Superintendency of Pension Funds).



**TABLE I  
PENSION FUND MEMBERSHIP**

AFJP	Dic-94	Jun-95	Dic-95	Jun-96	Dic-96	Jun-97	Dic-97	Jun-98	Dic-98	Jun-99	Dic-99
ACTIVA	108,420	122,107	132,235	-	-	-	-	-	-	-	-
ACTIVA ANTICIPAR	101,047	121,880	143,368	340,139	312,755	-	-	-	-	-	-
AFIANZAR	13,241	17,765	21,941	23,161	22,563	23,752	25,447	38,930	-	-	-
ARAUCA BIT	60,423	69,565	82,812	86,344	86,108	90,136	103,130	127,647	160,352	196,096	234,661
BANAT	69,080	n/d	448	369	335	339	-	-	-	-	-
CLARIDAD	205,026	222,842	263,433	274,864	288,029	271,824	272,282	287,019	-	-	-
CONSOLIDAR	478,731	534,033	667,209	740,427	821,445	907,346	971,695	1,256,414	1,298,880	1,336,634	1,376,674
DIGNITAS	70,260	-	-	-	-	-	-	-	-	-	-
ETHIKA	578	1,454	2,208	2,826	-	-	-	-	-	-	-
JACARANDA	46,036	54,672	60,650	59,628	61,633	50,189	48,009	60,767	74,643	90,948	-
FECUNDA	98,206	116,728	150,345	181,020	195,176	214,717	224,094	-	-	-	-
FUTURA	32,220	36,067	44,007	46,895	49,567	51,586	52,195	65,084	79,107	97,983	117,119
GENERAR	28,597	30,801	37,071	39,886	40,110	46,051	54,573	70,030	81,878	104,875	131,981
MÁS VIDA	7,376	21,700	76,665	85,599	68,474	52,954	-	-	-	-	-
MÁXIMA	454,162	511,756	635,991	723,528	795,186	880,775	1,067,219	1,126,120	1,171,728	1,227,246	1,277,751
NACIÓN	394,378	412,884	476,112	487,270	456,343	481,694	514,928	537,470	564,903	596,070	626,185
ORÍGENES	295,801	383,341	517,398	565,826	587,203	957,767	1,095,953	1,135,509	1,460,117	1,492,097	1,518,669
PATRIMONIO	109,030	112,437	128,442	130,408	119,414	108,011	-	-	-	-	-
PREVINTER	193,298	277,078	387,174	460,389	501,076	549,545	586,306	623,516	644,257	668,550	690,258
PREVISOL	105,106	117,668	132,069	140,425	156,015	156,881	165,490	184,304	199,341	221,101	243,722
PROFESIÓN + AUGE	6,671	10,427	18,062	21,155	21,400	21,104	23,775	38,591	53,675	74,710	96,788
PRORENTA	80,223	85,973	101,971	111,154	122,105	130,217	135,276	155,147	219,650	236,558	344,494
SAN JOSÉ	22,041	23,322	27,760	28,776	27,065	28,215	28,479	41,459	54,694	73,652	-
SAVIA	44,798	43,999	46,590	-	-	-	-	-	-	-	-
SIEMBRA	392,093	498,958	606,060	674,174	716,727	771,920	860,516	907,221	948,518	983,382	1,100,258
UNIDOS	14,170	15,642	19,221	20,945	23,342	25,511	27,076	41,020	55,380	75,348	95,803
<b>TOTAL FUNDED SCHEME</b>	<b>3,431,012</b>	<b>3,843,099</b>	<b>4,779,242</b>	<b>5,245,208</b>	<b>5,472,071</b>	<b>5,820,534</b>	<b>6,256,443</b>	<b>6,696,248</b>	<b>7,067,123</b>	<b>7,475,250</b>	<b>7,854,363</b>
PAYG SCHEME	2,900,793	2,839,948	2,708,948	2,598,248	2,544,382	2,396,397	2,328,468	2,280,960	2,251,419	2,238,692	2,224,773
UNDEFINED	322,498	293,475	207,234	322,470	295,547	370,030	254,698	217,082	260,368	242,892	293,640
<b>TOTAL</b>	<b>6,654,303</b>	<b>6,976,522</b>	<b>7,695,424</b>	<b>8,165,926</b>	<b>8,312,000</b>	<b>8,586,961</b>	<b>8,839,609</b>	<b>9,194,290</b>	<b>9,578,910</b>	<b>9,956,834</b>	<b>10,372,776</b>

**TABLE II**  
**CONTRIBUTORS, BY AFJP or PAYG scheme**

AFJP	Dic-94	Jun-95	Dic-95	Jun-96	Dic-96	Jun-97	Dic-97	Jun-98	Dic-98	Jun-99	Dic-99
ACTIVA	65,050	63,057	70,877	-	-	-	-	-	-	-	-
ACTIVA ANTICIPAR	55,104	59,039	71,559	146,829	143,479	-	-	-	-	-	-
AFIANZAR	7,571	9,263	11,015	10,666	9,759	9,656	9,298	13,677	-	-	-
ARAUCA BIT	33,403	37,409	49,201	45,869	45,224	47,856	54,044	70,754	91,913	105,205	126,008
CLARIDAD	124,369	110,355	132,187	119,123	111,336	107,433	97,701	104,621	-	-	-
CONSOLIDAR	303,272	301,773	401,617	399,175	443,275	489,281	504,173	646,913	663,725	637,519	644,360
DIGNITAS	43,731	-	-	-	-	-	-	-	-	-	-
ETHIKA	206	679	1,203	1,456	-	-	-	-	-	-	-
ETHIKA	23,491	22,885	26,430	21,307	18,776	17,451	14,880	20,389	27,138	29,298	-
FECUNDA	59,368	58,429	83,120	83,965	106,664	121,175	114,411	-	-	-	-
FUTURA	27,262	29,633	33,998	32,814	34,375	34,910	34,249	39,413	44,920	47,526	52,486
GENERAR	19,297	20,024	24,267	25,093	26,660	31,527	37,230	45,776	48,899	57,314	69,467
MÁS VIDA	3,900	9,150	19,828	24,440	23,187	20,198	-	-	-	-	-
MÁXIMA	281,890	272,858	355,230	368,724	432,510	484,917	539,426	570,805	594,528	570,708	583,601
NACIÓN	212,519	197,456	253,059	227,482	208,868	223,945	230,436	241,647	259,735	248,246	263,538
ORÍGENES	166,466	198,900	287,479	286,136	304,108	472,322	518,031	535,030	667,555	625,685	634,484
PATRIMONIO	59,241	54,928	63,273	55,948	44,781	38,946	-	-	-	-	-
PREVINTER	125,984	153,646	230,633	247,600	277,212	304,755	306,401	319,623	326,601	312,101	312,610
PREVISOL	70,350	66,638	77,753	70,145	68,805	71,045	71,408	80,732	86,530	88,229	94,782
PROFESIÓN + AUGE	5,863	7,262	11,016	11,516	11,455	11,595	12,052	18,817	26,093	32,061	39,627
PRORENTA	53,620	46,565	54,074	51,574	58,704	62,527	60,085	67,344	93,495	91,305	126,408
SAN JOSÉ	14,855	14,091	17,486	15,287	12,545	12,762	12,000	16,853	21,988	26,806	-
SAVIA	12,910	12,580	12,771	-	-	-	-	-	-	-	-
SIEMBRA	247,148	274,575	342,153	326,165	365,087	407,955	441,234	460,214	477,861	462,199	496,835
UNIDOS	11,783	12,198	13,870	14,540	15,440	16,411	16,478	22,239	28,195	32,004	39,059
<b>TOTAL FUNDED SCHEME</b>	<b>2,028,653</b>	<b>2,033,393</b>	<b>2,644,099</b>	<b>2,585,854</b>	<b>2,762,250</b>	<b>2,986,667</b>	<b>3,073,537</b>	<b>3,274,847</b>	<b>3,459,176</b>	<b>3,366,206</b>	<b>3,483,265</b>
<b>PAYG SCHEME</b>	<b>2,099,551</b>	<b>1,844,194</b>	<b>1,660,959</b>	<b>1,426,603</b>	<b>1,318,893</b>	<b>1,259,600</b>	<b>1,110,792</b>	<b>1,044,022</b>	<b>1,029,080</b>	<b>910,137</b>	<b>914,183</b>
<b>UNDEFINED</b>	<b>322,498</b>	<b>293,475</b>	<b>138,172</b>	<b>225,432</b>	<b>154,421</b>	<b>165,341</b>	<b>139,394</b>	<b>136,585</b>	<b>148,556</b>	<b>119,325</b>	<b>107,518</b>
<b>TOTAL</b>	<b>4,450,702</b>	<b>4,171,062</b>	<b>4,443,230</b>	<b>4,237,889</b>	<b>4,235,564</b>	<b>4,411,608</b>	<b>4,323,723</b>	<b>4,455,454</b>	<b>4,636,812</b>	<b>4,395,668</b>	<b>4,504,966</b>

**TABLE III  
BENEFICIARIES IN THE FUNDED SCHEME**

DATE	Type of benefit											TOTAL
	Retirees*					Disability	Survivors*					
	Frac.	Sched.	Ann.	N/D	TOTAL		Frac.	Sched.	Ann.	N/D	TOTAL	
Dic-95	2	2	0	37	41	143	0	126	172	2,051	2,349	2,533
Jun-96	4	5	0	101	110	366	0	265	684	3,424	4,373	4,849
Dic-96	50	20	0	268	338	766	0	683	1,595	4,562	6,840	7,944
Jun-97	151	72	1	550	774	1,198	0	855	3,037	5,066	8,958	10,930
Dic-97	427	233	4	1,316	1,980	2,370	6	988	7,346	4,469	12,809	17,159
Jun-98	1,022	436	12	3,136	4,606	3,832	34	1,164	10,856	6,912	18,966	27,404
Dic-98	1,356	621	38	5,284	7,299	5,363	98	1,596	12,991	10,466	25,151	37,813
Jun-99	1,968	804	81	6,372	9,225	6,413	198	1,661	16,649	12,195	30,703	46,341
Dic-99	3,385	1,084	131	7,036	11,636	8,523	579	1,360	21,420	13,763	37,122	57,281

Note: Retirees and Survivors may receive their benefits as:

- Frac: Fractionary withdrawal
- Sched: Scheduled withdrawal
- Ann: Annuity
- N/D: Not defined, in most cases due to delays in processing benefit requests.

**TABLE IV**  
**AVERAGE FEES AS % OF INCOME, INCLUDING INSURANCE COSTS.**

AFJP	Dic-94	Jun-95	Dic-95	Jun-96	Dic-96	Jun-97	Dic-97	Jun-98	Dic-98	Jun-99	Dic-99
ACTIVA	3.61	3.61	3.60	-	-	-	-	-	-	-	-
ACTIVA ANTICIPAR	3.55	3.55	3.53	3.53	3.54	-	-	-	-	-	-
AFIANZAR	3.88	3.76	3.72	3.46	3.49	3.47	3.45	3.45	-	-	-
ARAUCA BIT	3.40	3.40	3.29	3.29	3.28	3.11	2.94	2.85	2.82	2.79	2.78
CLARIDAD	3.55	3.82	3.73	3.74	3.83	3.79	3.74	3.74	-	-	-
CONSOLIDAR	3.30	3.30	3.30	3.30	3.30	3.30	3.30	3.30	3.30	3.30	3.30
DIGNITAS	3.83	-	-	-	-	-	-	-	-	-	-
ETHIKA	3.30	3.30	3.30	3.30	-	-	-	-	-	-	-
JACARANDA	3.45	3.45	3.44	3.44	3.07	3.05	3.29	3.21	3.20	3.17	-
FECUNDA	3.71	3.71	3.69	3.69	3.50	3.48	3.48	-	-	-	-
FUTURA	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00
GENERAR	2.87	2.87	2.86	2.69	2.68	2.64	2.61	2.59	2.41	2.42	2.47
MÁS VIDA	3.25	3.25	3.25	3.25	3.25	3.25	-	-	-	-	-
MÁXIMA	3.58	3.58	3.57	3.57	3.58	3.57	3.56	3.56	3.56	3.56	3.57
NACIÓN	3.58	3.58	3.57	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25
ORÍGENES	3.62	3.62	3.59	3.59	3.60	3.57	3.56	3.55	3.56	3.55	3.55
PATRIMONIO	3.30	3.77	3.74	3.74	3.79	3.76	-	-	-	-	-
PREVINTER	3.51	3.51	3.50	3.51	3.51	3.50	3.49	3.49	3.49	3.50	3.51
PREVISOL	3.44	3.44	3.56	3.57	3.58	3.56	3.55	3.55	3.55	3.56	3.58
PROFESIÓN + AUGE	3.50	3.50	3.49	3.50	3.51	3.20	3.20	3.00	3.00	3.00	3.00
PRORENTA	3.50	3.50	3.50	3.50	3.50	3.50	3.50	3.50	3.50	3.50	3.50
SAN JOSÉ	3.40	3.40	3.40	3.40	3.40	3.40	3.40	3.40	3.40	3.40	-
SAVIA	3.67	3.67	3.55	-	-	-	-	-	-	-	-
SIEMBRA	3.73	3.74	3.72	3.73	3.74	3.72	3.71	3.71	3.71	3.70	3.71
UNIDOS	3.41	3.41	3.39	3.40	3.41	3.40	3.40	3.40	3.42	3.43	3.47
<b>TOTAL</b>	<b>3.51</b>	<b>3.54</b>	<b>3.52</b>	<b>3.49</b>	<b>3.48</b>	<b>3.47</b>	<b>3.45</b>	<b>3.44</b>	<b>3.42</b>	<b>3.41</b>	<b>3.41</b>

<b>TABLE V</b>									
<b>ANNUAL RETURN OF PENSION FUNDS (in %)</b>									
<b>AFJP</b>	<b>dic-94 dic-95</b>	<b>jun-95 jun-96</b>	<b>dic-95 dic-96</b>	<b>jun-96 jun-97</b>	<b>dic-96 dic-97</b>	<b>jun-97 jun-98</b>	<b>dic-97 dic-98</b>	<b>jun-98 jun-99</b>	<b>dic-98 dic-99</b>
ACTIVA	14.95	-	-	-	-	-	-	-	-
ACTIVA ANTICIPAR	21.16	20.89	20.09	-	-	-	-	-	-
AFIANZAR	16.95	21.43	14.94	15.77	10.08	0.64	-	-	-
ARAUCA BIT	19.69	19.99	18.28	23.70	15.79	2.30	-0.40	4.58	15.37
CLARIDAD	17.68	20.46	19.36	22.00	10.44	-1.62	-	-	-
CONSOLIDAR	19.90	23.65	19.54	23.17	14.55	1.32	-0.25	6.20	17.93
ETHIKA	17.47	20.83	-	-	-	-	-	-	-
JACARANDA	19.32	20.30	19.79	22.01	12.92	-	-	-	-
FECUNDA	23.73	19.42	18.51	23.31	10.83	-	-	-	-
FUTURA	16.05	20.42	18.83	21.84	13.90	-0.24	-2.82	3.23	14.54
GENERAR	18.42	20.48	20.16	23.53	10.04	-1.64	-0.12	4.41	15.30
MÁS VIDA	19.20	17.43	19.36	21.12	-	-	-	-	-
MÁXIMA	22.29	24.56	20.59	23.00	14.65	1.54	-1.52	4.28	15.24
NACIÓN	16.37	19.22	18.76	21.86	15.58	2.93	-0.02	7.03	16.04
ORÍGENES	20.99	23.55	20.68	24.73	16.57	1.95	-2.37	3.99	16.08
PATRIMONIO	14.67	18.35	15.63	18.76	-	-	-	-	-
PREVINTER	21.50	22.81	18.56	23.95	15.80	0.71	-2.31	3.00	14.60
PREVISOL	19.39	22.02	20.46	24.30	15.09	0.50	-1.48	5.92	17.55
PROFESIÓN + AUGE	18.54	19.69	17.48	22.62	11.54	-1.59	-0.08	5.90	15.35
PRORENTA	23.21	25.66	20.31	21.82	14.74	1.66	-1.12	4.98	15.12
SAN JOSÉ	15.73	22.93	19.39	21.86	13.43	1.74	0.21	6.08	-
SAVIA	14.20	-	-	-	-	-	-	-	-
SIEMBRA	18.72	23.51	20.78	24.57	15.75	0.81	-1.90	4.10	15.56
UNIDOS	17.94	25.66	21.49	20.22	9.90	-0.49	-2.04	2.83	14.77
<b>AVERAGE</b>	<b>19.72</b>	<b>22.83</b>	<b>19.84</b>	<b>23.48</b>	<b>14.78</b>	<b>1.06</b>	<b>-1.47</b>	<b>4.52</b>	<b>15.98</b>
<b>MAXIMUM</b>	<b>25.64</b>	<b>29.68</b>	<b>25.79</b>	<b>30.52</b>	<b>19.21</b>	<b>3.06</b>	<b>0.53</b>	<b>6.52</b>	<b>20.77</b>
<b>MINIMUM</b>	<b>13.80</b>	<b>15.98</b>	<b>13.89</b>	<b>16.43</b>	<b>10.35</b>	<b>-0.94</b>	<b>-3.47</b>	<b>2.52</b>	<b>11.19</b>

**TABLE VI**  
**PENSION FUND ASSETS, IN MILLIONS OF US\$**

AFJP	Dic-94	Jun-94	Dic-95	Jun-95	Dic-96	Jun-96	Dic-97	Jun-97	Dic-98	Jun-98	Dic-99
ACTIVA	17,872	44,937	69,315	-	-	-	-	-	-	-	-
ACTIVA ANTICIPAR	12,238	36,076	64,103	215,940	289,226	-	-	-	-	-	-
AFIANZAR	1,061	3,436	6,410	9,902	11,647	14,923	16,435	18,559	-	-	-
ARAUCA BIT	8,146	24,649	46,623	71,802	102,451	152,316	224,975	320,874	473,543	677,098	951,146
BANAT	5,433	329	329	329	329	329	-	-	-	-	-
CLARIDAD	24,520	56,317	94,377	133,144	158,512	192,624	194,481	217,505	-	-	-
CONSOLIDAR	80,936	214,813	404,936	621,534	887,193	1,235,057	1,456,576	1,922,404	2,199,652	2,631,003	3,196,565
DIGNITAS	9,948	-	-	-	-	-	-	-	-	-	-
ETHIKA	97	735	1,877	3,210	-	-	-	-	-	-	-
JACARANDA	5,757	15,157	24,798	33,940	42,125	50,612	57,402	67,808	93,957	97,632	-
FECUNDA	13,690	35,061	67,248	113,887	158,297	215,990	246,912	-	-	-	-
FUTURA	11,039	31,407	56,099	86,065	113,241	154,067	176,991	194,641	206,118	240,536	278,145
GENERAR	13,053	34,276	63,845	101,480	153,995	239,400	337,823	415,366	451,708	573,770	787,328
MÁS VIDA	1,114	4,632	12,085	23,815	34,462	39,399	-	-	-	-	-
MÁXIMA	71,425	189,550	342,908	559,963	848,543	1,175,914	1,490,608	1,687,443	1,890,163	2,217,643	2,620,568
NACIÓN	45,820	109,884	195,750	285,989	347,298	480,089	588,239	667,619	782,090	968,011	1,176,522
ORÍGENES	34,861	104,294	220,111	356,931	496,482	1,048,210	1,338,749	1,540,573	1,983,486	2,377,841	2,862,844
PATRIMONIO	11,868	29,307	46,926	60,369	67,285	76,696	-	-	-	-	-
PREVINTER	38,250	114,660	236,566	380,254	553,307	792,537	917,923	1,031,155	1,125,828	1,291,718	1,454,770
PREVISOL	17,101	44,446	72,922	102,998	129,915	169,864	197,145	223,565	246,780	293,545	361,019
PROFESIÓN + AUGE	1,636	5,469	11,274	18,013	25,136	34,326	37,232	45,095	57,454	76,697	100,238
PRORENTA	13,638	32,705	49,908	72,759	99,357	133,263	151,517	169,423	212,278	260,368	377,768
SAN JOSÉ	3,566	9,239	15,034	21,461	24,673	31,727	34,108	38,904	42,516	53,168	-
SAVIA	2,789	6,276	9,735	-	-	-	-	-	-	-	-
SIEMBRA	75,709	208,594	368,725	541,651	750,760	1,065,464	1,311,485	1,484,450	1,696,791	2,023,646	2,522,503
UNIDOS	3,319	8,395	15,135	23,145	31,639	42,097	48,546	56,698	64,030	78,491	97,685
<b>TOTAL</b>	<b>524,885</b>	<b>1,364,645</b>	<b>2,497,040</b>	<b>3,838,583</b>	<b>5,325,872</b>	<b>7,344,904</b>	<b>8,827,147</b>	<b>10,102,083</b>	<b>11,526,393</b>	<b>13,861,167</b>	<b>16,787,099</b>
As % of GDP	0.20	0.52	0.97	1.46	1.96	2.60	3.01	3.38	3.87	4.75	5.85

**TABLE VII**  
**PORTFOLIO STRUCTURE OF PENSION FUNDS (in %)**

TYPE OF ASSET	Dic-94	Jun-95	Dic-95	Jun-96	Dic-96	Jun-97	Dic-97	Jun-98	Dic-98	Jun-99	Dic-99
<b>CASH</b>	6.33	2.27	1.68	2.24	1.83	1.38	0.98	1.37	1.52	1.92	0.97
<b>Government Bonds</b>	41.90	45.94	47.33	47.38	48.13	45.50	40.90	42.29	47.98	48.30	48.50
<b>Local Government Bonds</b>	7.93	5.53	5.35	4.41	4.57	3.76	2.46	2.33	2.01	2.99	3.80
<b>Corporate Bonds</b>	5.84	6.77	8.71	10.66	7.78	4.80	2.86	2.33	2.50	2.29	2.13
<b>Certificates of Deposit</b>	27.55	27.07	24.76	17.57	14.19	16.42	24.44	22.96	18.83	18.15	15.47
<b>Stock</b>	0.55	0.88	4.47	11.42	16.22	19.32	19.05	18.83	15.82	16.12	19.06
<b>Stock of privatized companies</b>	0.98	1.09	1.38	2.06	2.52	2.44	2.41	2.06	2.53	1.22	1.48
<b>Mutual Funds</b>	5.01	4.20	1.74	1.46	2.34	4.13	4.47	5.48	6.59	6.46	6.28
<b>Foreign Government Bonds</b>	0.08	1.35	0.44	0.22	0.02	0.02	0.01	0.00	0.00	0.00	0.00
<b>Foreign Private Assets</b>		1.49	0.29	0.23	0.13	0.42	0.36	0.40	0.25	0.23	0.36
<b>Regional Economies</b>	3.82	3.40	3.85	2.32	1.73	1.36	1.49	1.40	1.42	1.56	1.41
<b>Futures and Options</b>		0.00				0.00			0.01	0.23	0.24
<b>Direct Investment Funds</b>			0.01	0.03	0.05	0.07	0.10	0.11	0.19	0.24	0.19
<b>Mortgages</b>					0.48	0.40	0.47	0.42	0.35	0.29	0.08
<b>TOTAL</b>	<b>100.00</b>	<b>100.00</b>	<b>100.00</b>	<b>100.00</b>	<b>100.00</b>	<b>100.00</b>	<b>100.00</b>	<b>100.00</b>	<b>100.00</b>	<b>100.00</b>	<b>100.00</b>





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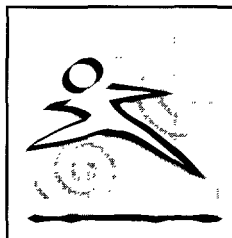
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## Summary Findings

In a context of a serious financial and legal crisis, Argentina reformed its Pension System in 1994, when a multipillar model with a funded scheme was introduced and first pillar parameters, as minimum age and vesting requirements were tightened. The new system has a significant first pillar (which offers a flat benefit currently valued at 28% of average wage to all retirees) and a second pillar that should provide a similar amount, once the transition is completed.

The new system has developed rapidly and most formal workers have joined the new funded scheme. However, there are some problems that must be resolved. In the first pillar, the reform balanced long term finances, but it will also reduce coverage very rapidly, as a consequence of the combined effect of low formality in the labor market and stricter contribution requirements. The most serious problems in the funded pillar are the administration costs and the need to improve regulation and supervision of insurance companies, that provide disability and survivors coverage and annuities to beneficiaries.

While these problems are important, their consequences can be avoided if adequate policies are developed by the Government. In this sense, the experience of the pension reform in Argentina is an excellent lesson for other countries that are considering a reform in their own systems.

HUMAN DEVELOPMENT NETWORK

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