

# Social Insurance in a Market Economy: Lessons from Central Europe

Elaine Fultz

27 January 2012

# Pension privatization

- Replacement of social insurance with privately managed individual investment accounts
- Latin America
- Central Europe

# Establishment of mandatory, privately managed investment accounts in Central Europe

| Country               | Year |
|-----------------------|------|
| Hungary               | 1998 |
| Poland                | 1999 |
| Latvia                | 2001 |
| Bulgaria              | 2002 |
| Croatia               | 2002 |
| Estonia               | 2002 |
| Lithuania             | 2004 |
| Slovakia              | 2005 |
| Republic of Macedonia | 2006 |
| Romania               | 2008 |

# Recent retrenchment of second-tier accounts in Central Europe

| Country   | Previous rate of diversion of public pension contributions | Recent rate adjustment | State mandate for worker participation |
|-----------|--|------------------------|--|
| Hungary   | 8%   | Repealed               | Repealed                               |
| Poland    | 7.3%   | 2.3%<br>(permanent)    |  |
| Estonia   | 6%   | 3% (temporary)         |  |
| Latvia    | 8%   | 2% (temporary)         |  |
| Lithuania | 5.5%   | 1.5%<br>(temporary)    | Repeal under consideration             |
| Slovakia  | 9%   |                        | Repealed<br>(2008)                     |
| Croatia   | 5%   | --                     | Partial repeal<br>(2011)               |

# Second tier design issues

- Challenge: hybrid status of second tier
  - Publicly mandated
  - Privately managed
  - Which principles will apply?
- Desired design features
  - Preservation of purchasing power
  - Equal treatment of women and men
  - Reward longer work

# Preserve purchasing power

- Regular cost of living increases

# Gender equality

- Annuitize account balance at retirement
- Gender neutral versus gender specific life expectancy tables
- Unisex or gender specific?

# Reward longer work

- Challenges in designing seamless integration of retirement investment accounts (capitalized savings) with disability pensions (social insurance)



# Second-tier retrenchment driven by

- Mismatch between the benefit package that policymakers sought and the one that private funds are able and willing to provide
  - Private benefit packages caught in a quandary that resisted resolution for more than a decade
  - Stalemate eventually weakened support of key stakeholders
  - Global economic crisis was the catalyst for second-tier retrenchment but not the root cause

# Post Mortem

- Workers in market economies face many new risks and need the broad pooling of risks and resources that social insurance provides.