

QUALITY OF SOCIAL PROTECTION IN PERU

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INTRODUCTION

This presentation is based on the preliminary results of some focus groups and surveys that we are conducting for a long-term survey being carried out by the Inter-American Development Bank (IADB). I will also use data from Peru's National Household Survey and the Survey on Prevention of Social Risks carried out by the World Bank (Prieso). I insist, the results are still preliminary ones; the survey will mature even more between now and approximately one year's time, but we do have a few first impressions that we want to share with you.

A complete discussion about the significance of a social protection network should touch upon several issues. The agenda for the discussion of social protection among policy makers has emphasized the issues of health, education, employment, poverty, pensions and public safety. Within our focus groups, we asked people in the street what they understood as social security. Interestingly, their answers revealed some coincidences and some discrepancies with the subjects being debated on the public agenda. These citizens put the problem of health as top priority; followed by the need for economic stability; protection in the event of accidents, crimes, etc; public safety; a range of services, and among them, also, the subject of pensions. Now, particularly given today's audience and the subject of interest of our meeting, we are going to refer to the pension angle of social security. In this document we shall discuss the role of pensions within a social protection network for people who are of working age and for people who are past that age. In this sense, allow me to propose the following outline for the presentation.

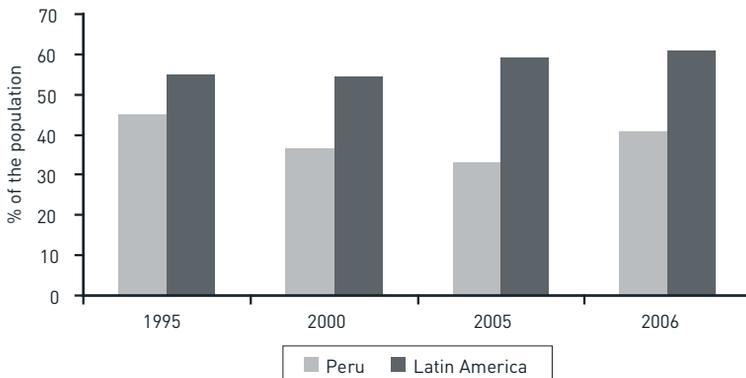
We shall refer, first of all, to the issue of coverage, distinguishing between people of working age and the elderly. Then we will make a brief analysis of people's opinions about the system, making a distinction between those who are covered by the pension system and those who are not, on the one hand; and, in the same way, between those people who are of working age and the elderly, on the other. The third part of this presentation asks the question: What happens with elderly people? How do they finance their expenses during their old age, especially those who are

not covered? Finally, in the fourth section of this document we shall say a little more about the experimental study we are carrying out.

I. PENSION SYSTEM COVERAGE IN PERU

Let us start with coverage. There are probably some facts here that we are all familiar with already, but let me put a few things on the table. Social security and health coverage in Peru is below what exists in Latin America. However, there are some very interesting changes in the current trend. Coverage began to fall from the late 90s and early 2000s, but in 2005 we already see that coverage starting to recover. Coverage is beginning to increase in Latin America and in Peru in particular (see Figure 1).

FIGURE 1
PERCENTAGE OF URBAN WORKING POPULATION WITH PROTECTION AND HEALTH AND/OR PENSIONS



SOURCE: ILO, LABOUR OUTLOOK 2007

In spite of this recent upturn, it is important to remember that enrolment in our social security systems is low. Three out of every four people of working age (between 25 and 64 years old) are not enrolled in any pension plan. Among members, approximately two out of every three have decided to enrol in the private pensions system. A factor that makes the problem of low enrolment even more serious is the density of contributions, which is also very low. Here I am going to coincide on several points with what was mentioned earlier by Eduardo Morón, who came before me. The point that poverty plays an important role here is very relevant. Only

one out of every five poor people of working age are actually paying contributions into a pension plan; by contrast, three out of every five non-poor people in the same age-group do manage to pay contributions. It is also important to mention that the average of the contributions in 2007 was S/. 227 which is a fairly low figure by the standards of our labour markets.

The coverage provided by the pension systems is low among active people but also very few elderly adults are covered by a pension. Figures taken from the National Household Survey by the INEI² suggest that between 22% and 29% of elderly adults are covered by some pension. In other words, three out of every ten elderly adults, at the most, can be sure of a pension. But, unfortunately, 48% of the elderly adults who do receive a pension, receive a sum that is below the minimum wage. Moreover, among the poor, pensions are practically non-existent.

II. OPINIONS ABOUT THE PENSION SYSTEM

Now let us see what the man-in-the-street thinks of the pension system. When people are asked: "What do you think of the pension systems?", it turns out that people's opinion is not so bad, among those who are members. About 40% say that the pension systems are fine; they have no major issues with regard to the problem. However, a similar percentage of people say they do not know or do not express an opinion and it is important to contrast this figure with the figure we are about to obtain from people who are not covered by the system. On the other hand, those people who contribute find the product interesting. Those who are paying contributions do so in the knowledge that they are generating income for their old age, because that is the most important reason they mention when asked to indicate why they are paying contributions into a pension system.

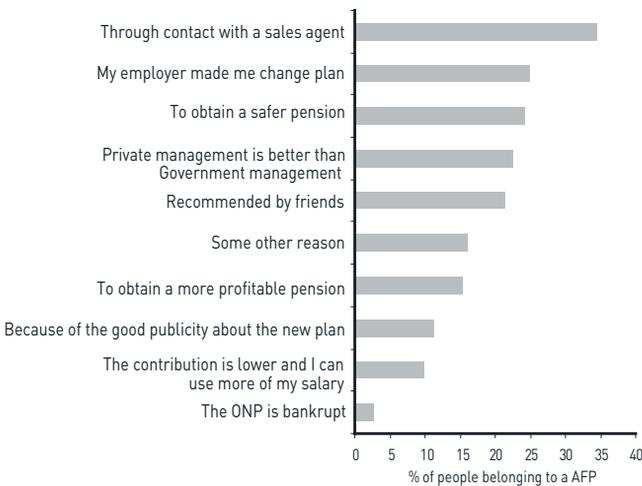
Members' stances with regard to the quality of the pension systems in Peru appear not to be too bad. The figures show that among those who are covered, who are contributing to the system, perceptions are good. But let us try to make a slightly greater distinction between the public and the private system. For this purpose, we can look at the 2002 World Bank surveys. All those in the private system were asked: "Why did you choose an AFP and not the ONP³ when making a decision about your pension plan? (see Figure 2). We see that the strongest element here is the existence of a person, someone who gave the system a human face and then offered it. That mechanism involves major elements of inter-personal trust and is very important

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when deciding on a pensions system. I will refer to this point again at the end of the presentation, because this subject is the motivation behind the long-term study that we have been carrying out.

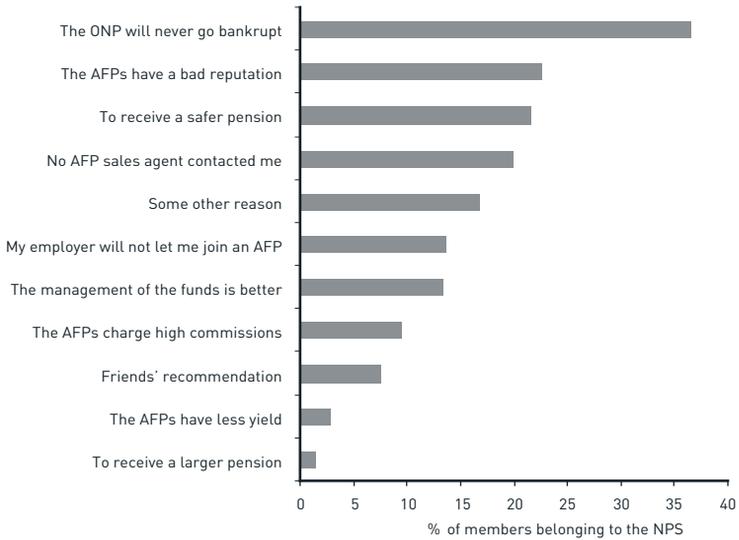
FIGURE 2
"WHY DID YOU CHOOSE THE AFP AND NOT THE ONP OR ANOTHER PLAN" (MULTIPLE CHOICE QUESTION)



SOURCE: WORLD BANK, 2002

On the other hand, the people enrolled in the public system were asked the opposite question: "Why didn't you pay contributions into a private system rather than the public system?" The most frequent answer was that the reason for their choice was the belief that the ONP would never go bankrupt (see Figure 3). The people interviewed were of the opinion that if there were a financial problem with the ONP, the State would step in to salvage the situation. This perception is an additional element of individuals' confidence in the system, which is playing an important role.

FIGURE 3
"WHY DID YOU CHOOSE NOT TO JOIN AN AFP"
(MULTIPLE CHOICE QUESTION)



SOURCE: WORLD BANK, 2002

Now for the opinions of those without coverage: What is the perception of people who are of working age and are not covered? We can summarize this in four points. The first and most recurrent is that social security saving is not a basic asset. People are short of money, they have to cover some basic, immediate needs before being able to think about pensions. Social security savings are an asset that is beyond most people's reach.

The second point is that the system does not yet inspire much confidence. Non-members feel that they do not have sufficient confidence in the system to deposit their money and wait 20, 30 or 40 years to get it back.

In third place is the problem of insufficient information about the system. We asked those without coverage a series of questions about the operation of the system, to find out if they were aware of the basic rules, for example: at what age can one retire? What is the contribution rate? What is the administrative cost of the pension? and other related subjects. It was sad to see that people knew absolutely nothing about how the system works; and this is linked to the last point.

Fourth: generally speaking, the product is of no interest to the average citizen.

Table 1 is very revealing about the fourth point I have just mentioned. We show here some of the basic rules or characteristics of the system: retiring age, amount of pensions, monthly contributions, commissions, etc. Here we have columns indicating what actually happens, and some of the results that we obtained with the focus groups. People's perceptions have absolutely no connection with the reality. In other words, information has apparently hardly filtered to the population at all. This also has to do with a recurrent subject of discussion in this seminar, which is the problem of the financial literacy of our populations. This is a very important element that we must take into account if we are to generate confidence in our pension systems.

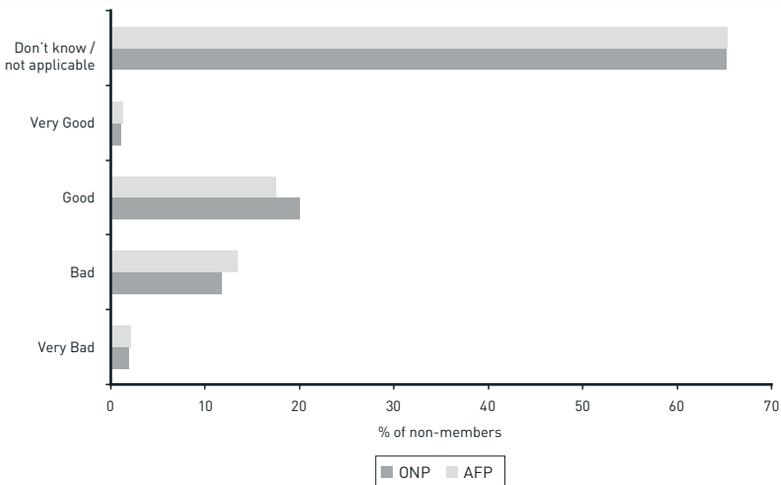
TABLE 1
PENSION SYSTEMS: REALITY VERSUS PERCEPTIONS

	The reality		People's perceptions
	NPS	PPS	
Retiring age	60	65	78% of enrolled workers and 54% of non-enrolled workers know what the retiring age is (IADB 2008) "I don't have a clear idea about the retiring age, I've been told that you can only retire with the ONP after 25 years of paying contributions, otherwise you lose your fund"
Amount of the pension (new sols / month)	Minimum 415 Maximum 857	Maximum No	Only 3% of workers know how pensions are calculated in either of the two pension systems (IADB,2008) "One knows what people say, what comes out in the papers or by experiences of third parties, which are generally always bad: that they are paid very little, that it is not worth paying contributions."
Monthly Contributions	Varies	Varies	60% of members do not know how much is deducted from their salaries and 94% of non- members do not know either (IADB, 2008) "Don't know how it will be, I imagine they deduct a percentage"
Commissions	Varies	Varies	Only 33.65% of the members know how much they pay in commissions. Of non-members only 9% know how much is paid (IADB, 2008) "Nobody notices that, I don't know."

NPS: NATIONAL PENSION SYSTEM
PPS: PRIVATE PENSION SYSTEM
SOURCE: PREPARED BY THE AUTHOR.

Figure 4 offers quite an interesting contrast with the previous table in terms of individuals' perception of the pension systems. I was telling you before that around 30% or 40% of members had a good impression of the system and a similar percentage either did not know or did not express an opinion about the system. What happens among non-members is quite different: around 65%, almost two out of every three non-members, have no opinion on the subject at all; they do not know, they express no opinion, they do not know what it is all about, they have no information.

FIGURE 4
"HOW WOULD YOU GRADE THE QUALITY OF THE SERVICES OFFERED BY... ONP? ... AFP?"



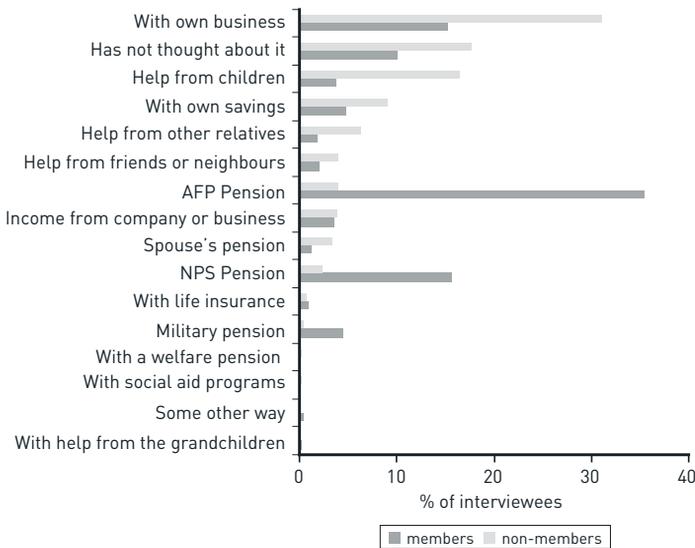
SOURCE: IADB, 2008

III. FUNDING OLD AGE

What actually happens is that people don't think much about the future. Here we can look at a few explanations that have to do with the short-sightedness of the agents. People have not given much thought to the future and when asked about what they are thinking of doing to fund their old age, people generally reply: "Well, I am going to open up my own business and that will eventually produce some profits that will allow me to support myself in my old age." (see Figure 5). And when we ask the next question "Given that plan, what have you done about it?", the

answer we receive is that they have not really done much. In other words, this is an ideal on which they have not yet done much work. The issue of funding for old age is a subject that concerns people to a certain extent, but it is not immediate or close to them in time, so they do not take concrete action in that direction. Another piece of information that emerged from our focus groups is that most elderly adults who do not have pensions receive transfers from their children. Among non-pensioners, the main sources of income are these current transfers and, to a lesser extent, income from property.

FIGURE 5
"ONCE YOU STOP WORKING, HOW ARE YOU THINKING OF FINANCING YOUR OLD AGE?"



SOURCE: IADB, 2008

Another important point, which cannot be omitted here, is that one might think that reducing the costs of social security savings might be a good strategy for increasing coverage. In fact, this was the line of reasoning until very recently. We asked people: "If social security costs were half what they are now, would you save more? And the reply was not very convincing. Only 40% of non-contributors replied: "Ah, yes, I would contribute more to the system." Reducing costs does not mobilize large crowds.

So then, this outlook is characterized by the fact that: (i) cost reduction does not apparently have a major impact on an increase in coverage; (ii) a quite limited flow of information suggests a lack of perfect harmony between the issuer of the information and the person receiving it; and (iii) it is also necessary to work on people's trust. In the light of this, we at the IDB are proposing to carry out a study that analyses the potential of information and trust as tools to improve social security coverage.

IV. EXPERIMENTAL STUDY: INFORMATION AND TRUST

The problem does not seem to be one of costs, the problems seem to have more to do with information and trust. These are the elements that we believe at the moment to be important in the diagnosis and it is for this reason that we are designing an experimental study. At present we are drawing up the baseline with a representative group of 6,000 households in metropolitan Lima, households from all social strata, with a series of characteristics that will represent the population. This representative sample will be the subject of a survey comparable to the National Household Survey (Enaho) carried out by the INEI in terms of its basic structure, but to which we are adding a few modules. In other words, we are gathering socio-demographic information about these households, exploring their working and welfare conditions; but also asking questions about the degree of financial knowledge and the information that individuals have about the pension system, their savings strategies (short and long-term) and their investment strategies (in the financial markets and outside them).

The knowledge we can acquire on the basis of the data gathered from the baseline will be complemented with an experimental treatment. The individuals in the sample will be distributed in four groups to which we shall be applying combinations of treatments. Basically, there are two treatments: financial literacy classes and making people's access to the pensions system simpler. So, to one treatment group we shall only be giving financial literacy sessions; with a second group, we shall only make access to the pension systems easier; a third group will be given both treatments (information and ease of access) and a fourth group, which will serve as control, will not be assigned any treatment.

The financial literacy classes will transmit basic financial concepts and the ideas about how pension systems operate that are needed to enable the average citizen to make more well-informed choices about his/her social security savings strategies.

In addition to transmitting concepts, these classes will try and transmit life experiences so that individuals leave them with a greater awareness of the

importance of social security savings.

In order to facilitate access to the pensions systems, a fair will be organized at which participants will have the opportunity to speak to promoters from each of the AFPs and the ONP. Also, individuals will have the opportunity to enrol in a pension system on-site. This is very much in line with what has been discussed in other sessions in this seminar: “pensions are not bought but sold.” It is necessary to put a face to the system and put a person out there to interact with the potential members. In that way, we hope to minimize certain transaction barriers and enable people to become members.

Given these combinations of treatments, we shall carry out follow-up surveys nine months after these operations. Through these surveys we will be able to answer questions of the kind: Up to what point did these interventions influence people’s enrolment, people’s contribution or their savings mechanisms in general? But all of this can be shared on another occasion.