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Pension Coverage and the Informal Sector Workers

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Introduction

- Pension reform has been widely observed around the globe
- However, focus has been given to formal sector workers; thus the informal sector left out
 - Definition of informal sector employees: low income, self-employee, small firm, farmer, part-time/seasonal, etc
 - Higher income owners (e.g. lawyer, consultant) excluded
- Experiences from both OECD & non-OECD countries presented
- Some policy suggestions proposed

Background: some statistics (ILO 2002)

Table 1. Informal employment as % of non-agricultural employment, 2000

North Africa	48	Latin America	51
Algeria	43	Bolivia	63
Morocco	45	Brazil	60
Tunisia	50	Chile	36
Egypt	55	Colombia	38
Sub-Saharan Africa	72	Costa Rica	44
Benin	93	El Salvador	57
Chad	74	Guatemala	56
Guinea	72	Honduras	58
Kenya	72	Mexico	55
South Africa	51	Rep Dominicana	48
Asia	65	Venezuela	47
India	83		
Indonesia	78		
Philippines	72		
Thailand	51		
Syria	42		
Memo			
Developing world (non-agriculture)		60-70 (approx)	
Developing world (all)		80-90 (approx)	
European countries (15)		15-25	

Table 2. Contribution of informal sector to GDP in %, 1990-2000

North Africa	27	Sub-Saharan Africa	41
Algeria	26	Benin	43
Morocco	31	Burkina Faso	36
Tunisia	23	Burundi	44
Latin America	29	Cameroon	42
Colombia	25	Chad	45
Mexico	13	Cote d'Ivoire	30
Peru	49	Ghana	58
Asia	31	Guinea Bissau	30
India	45	Kenya	25
Indonesia	31	Mali	42
Philippines	32	Mozambique	39
Republic of Korea	17	Niger	54
		Senegal	41
		Tanzania	43
		Togo	55
		Zambia	24

Low coverage of the informal sector

- Despite the importance of the informal sector (number of people and contribution to GDP), pension coverage is very low
- No reliable/official statistics found, however it is estimated to be very low, i.e. well below 5-10%.

Countries taking actions to address this issue

- Non-contributory arrangements
- Contributory arrangements
- Others

I. Non-contributory arrangements

- Broaden access to social assistance program (old-age)
 - No contribution necessary
 - Means-tested or universal
- Particularly relevant to the poor who are too poor to save
- It operates in some African countries, e.g. Botswana, Mauritius, South Africa, and Kenya is considering a “zero pillar” pension

Examples of universal and means tested schemes

	Age limit	US\$	% of GDP	
Bangladesh	57	2	0.03	means tested
Bolivia	65	18	1.3	universal
Botswana	65	27	0.4	universal
Brazil (Rural)	60 (M) 55 (W)	140	0.7	means tested
Chile	65	75	0.38	means tested
Costa Rica	65	26	0.18	means tested
India	65	4	0.01	means tested
Mauritius	60	60	2	universal
Moldova	62 (M) 57 (W)	5	0.08	means tested
Namibia	60	28	0.8	universal
Nepal	75	2		universal
South Africa	65 (M) 60 (W)	109	1.4	means tested
Thailand	60	8	0.005	means tested
Vietnam	60	6	0.5	means tested

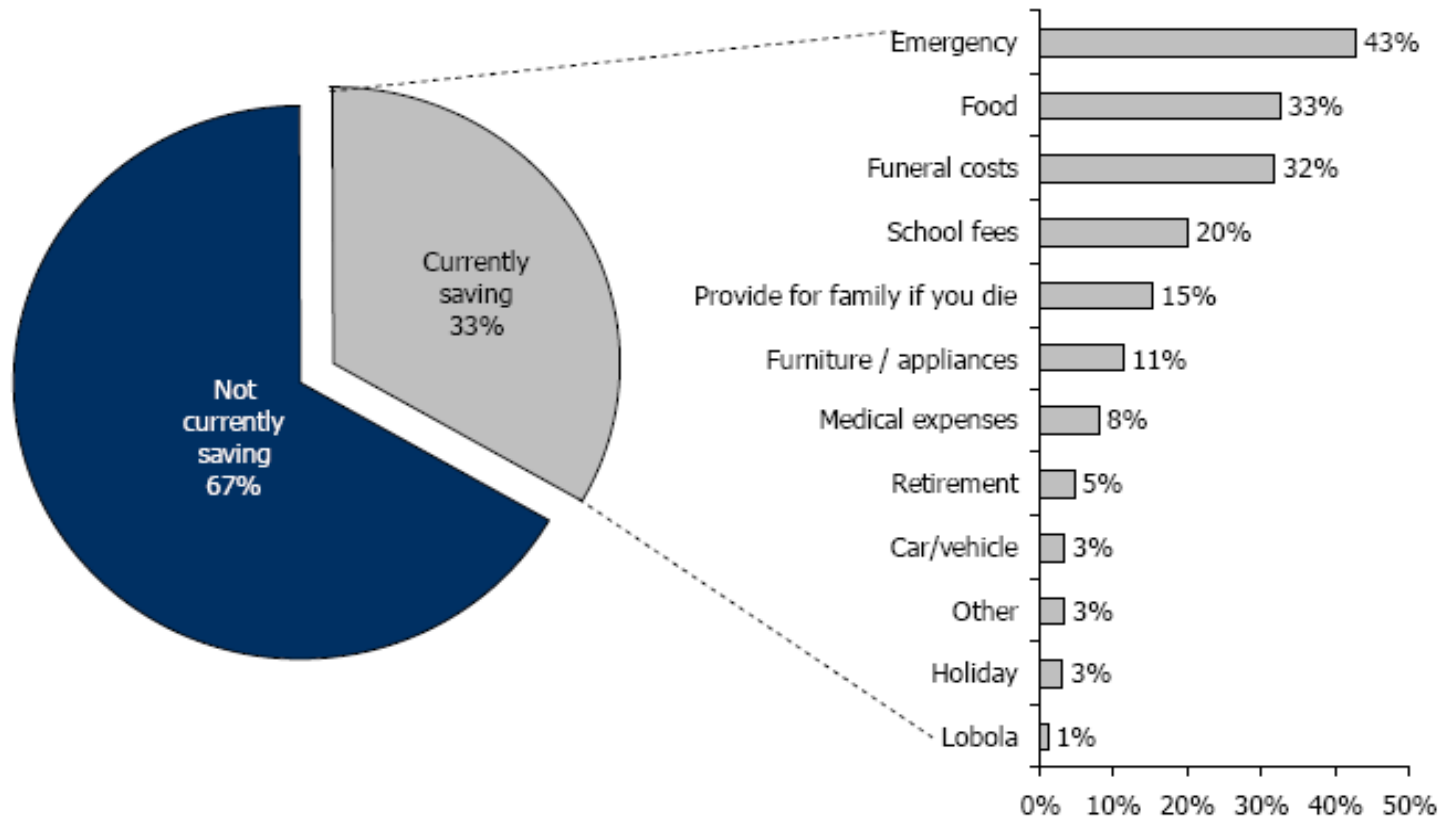


Source: Willmore (2006). Universal pensions for low income countries



Saving decisions of South Africans

Savings activity and reason for savings: LSM 1 - 5



Source: FinScope 2005 Core (Finvudurte)

II. Contributory arrangements: Encourage voluntary contribution

- Flexible terms:
 - contribution requirements (reduced contribution, periodic contribution)
 - vesting policies (earlier withdrawal, e.g. due to emergency, housing, foods)
- Financial incentives: tax credit, tax reduction, and matching contributions
- Financial education: enhance financial/pension awareness. ADB project in India (2006); similar schemes in the UK

II. Contributory arrangements: compulsory contribution

- The main logic: individuals have reluctance, inertia in making complex financial decisions
- Semi-compulsory (or auto enrolment), e.g. the NPSS in the UK, KiwiSaver in NZ, and similar schemes in Italy
- Compulsory, e.g. Chile, Hong Kong, Kenya (under consideration)

III. Other routes

- Utilization of existing (non-pension) infrastructure: banks, post offices, depository agencies
- Utilization of existing (non-pension) financial intuitions - micro-finance
- Creation of new institutions to reduce transaction costs, e.g. central clearing house (India, Sweden and UK)

Some policy suggestions

- Old-age pension guarantee
- Flexible terms
- Target those capable of extra saving
- Utilize existing infrastructure
- Centralised admin. agency

However...

- Any reform options (in developing countries) **MUST** be considered in line with country-specific conditions, which are a function of various parameters
 - economic growth
 - income level
 - consumption preference
 - financial markets
 - governance, etc