THE POLITICAL ECONOMY OF PENSION REFORM IN CENTRAL AND EASTERN EUROPE

PRACTICAL LESSONS IN PENSION REFORM: SHARING THE EXPERIENCES OF TRANSITION AND OECD COUNTRIES
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SUMMARY

This study seeks to explain the observable pension reform outcomes in six transition countries as a result of the interplay of economic and political variables: The two earliest Central European cases, Hungary and Poland, are contrasted with two more recent cases of pension privatisation: Croatia and Bulgaria. The cases of the Czech Republic and Slovenia are presented, where policymakers did not opt for the radical changes advocated by the ‘new pension orthodoxy’. The paper describes and explains how different pension reform choices came to be made in these countries, by analysing the behaviour of individual and collective actors under economic, political and institutional constraints. The cases analysed indicate that, contrary to conventional wisdom in social policy research, far-reaching pension reform is possible in a democratic context.
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Introduction

1. In the past decade, many post-socialist countries witnessed not only a fundamental transformation of their societies and economies, but also of their retirement schemes (Fultz and Ruck 2000; Müller 2002b). In recent years, reforms implying full or partial pension privatisation1 were started in Kazakhstan (1998), Hungary (1998), Poland (1999), Latvia (2001), Bulgaria (2002) and Croatia (2002), while Estonia and Macedonia have enacted similar reforms and are expected to implement them in 2002. Other transition countries, such as Armenia, Georgia, Lithuania, Mongolia, Romania, Russia, Slovakia and Ukraine, are considering this type of reform for the future. Interestingly, policymakers in the Czech Republic and Slovenia, two of the most advanced transition countries, dismissed the privatisation of old-age security and decided to improve the financial health of public pay-as-you-go (PAYG) scheme with a series of parametric reforms, while complementing it with a voluntary private tier.


3. These analyses, that concentrate mostly on the explanation of the recent waves of pension privatisation in Latin America and Eastern Europe, were written in response to a bias in earlier research, that is limited both in terms of the geographical scope and of the types of reforms analysed. In spite of their differences in methodology and theoretical objectives, most contributions by economists, political scientists and sociologists show one interesting similarity: they focus on the remarkable resistance of social security arrangements to substantial downward adjustments and on the political feasibility of moderate retrenchment.2 It has been claimed that ‘pay-as-you-go schemes may face incremental cutbacks and

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1. The notion of pension ‘privatisation’ has been criticised, since the state continues to play a role in the new schemes. Here, the term is thought useful to indicate the scope and direction of the recent reforms in Latin America and the transition countries. For a more detailed discussion of the public-private interaction in the new schemes see Müller (2002c).

2. For an overview see Müller (1999).
adjustments, but they are highly resistant to radical reform’ (Pierson 2001: 416). Ultimately, however, research on the politics of pension reform will need to take the full range of policy outcomes into account.

4. It is to shed more light on different policy choices that six cases of pension reform in Central and Eastern Europe are analysed here. The two earliest Central European cases, Hungary and Poland, are contrasted with two more recent cases of pension privatisation: Croatia and Bulgaria. Then, the cases of the Czech Republic and Slovenia are presented, where policymakers did not opt for the iconoclastic move advocated by the ‘new pension orthodoxy’ (Lo Vuolo 1996: 692). The subsequent section seeks to come up with a comparative explanation of the paradigm choices in the post-socialist context, while the paper ends with some concluding remarks.

Post-Socialist Pension Reform: Six Case Studies

Privatising Pensions in Central and South-Eastern Europe

The case of Hungary

5. By 1989, the need for fundamental reforms in Hungarian old-age security was widely acknowledged, as the inherited PAYG system was seen as inequitable, inadequate and unsustainable. Its financial problems increased significantly during economic transformation. Early reforms introduced some changes to the organisation, financing and eligibility of the Hungarian pension scheme, but were not sweeping enough to ensure its financial viability. Inadequate indexation practices added further distortions. Moreover, trade unions succeeded in delaying important reform measures. In contrast, the introduction of voluntary pension funds in 1994 – the first move towards a diversification of old-age provision – did not meet with political obstacles. In spite of the largely unsuccessful attempts to bring about thorough reform within the existing Hungarian old-age scheme, the Ministry of Welfare and the self-government of the Pension Fund continued to adhere to the Bismarckian and Beveridgean traditions.

6. Meanwhile, Lájos Bokros, the author of a severe structural adjustment package, put pension privatisation on the political agenda while serving as Minister of Finance, but it was up to his successor, Péter Medgyessy, to implement radical reform. The stalemate between the Ministries of Welfare and Finance in the pension reform issue lasted almost two years, until it was finally settled in spring 1996 when Medgyessy threatened to resign. The joint reform blueprint subsequently presented by both Ministries strongly resembled the Ministry of Finance’s earlier stance. Yet, its mixed overall approach can be interpreted as satisfying both of the previously competing Ministries. A pension reform committee led by a commissioner to the Minister of Finance was set up to work on the planned pension reform, thereby bypassing the previously exclusive competency of the Ministry of Welfare. The reform team was actively supported by the World Bank resident mission in Budapest and by the US Agency for International Development (USAID). In mid-July 1997, after only six weeks of parliamentary debate, the government won legislative approval for the envisaged pension reform package. Hungary’s new pension system, in force since 1998, combines a mandatory public PAYG scheme with a partially mandatory funded tier, with three-quarters vs. one-quarter of contributions going to each of the tiers. Even though the public tier still

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4. From July 1998, all new entrants to the labour market were obliged to join the two-tiered scheme, alongside the public pension tier (mixed pension path). Individuals that already had an insurance history but were not yet retired could do the same – alternatively, they could stay in the old scheme (purely public
plays an important role in Hungarian old-age security, the Argentine-style reform implies a reprioritisation between public and private retirement provision (Charlton, McKinnon and Konopielko 1998).

7. It is interesting to note that the first (partial) pension privatisation in Central and Eastern Europe was enacted by a Socialist-led government. As the overall policy context was marked by a rising external debt burden, a near currency crisis and a drop in Hungary’s credit rating, the centre-left coalition was forced to demonstrate its commitment to market-oriented reforms. It can be argued that Hungarian policymakers opted for pension privatisation to signal their resolve to tackle outstanding structural reforms. The PAYG system’s dependence on budgetary subsidies had granted the Ministry of Finance an important stake in the pension reform issue. Thorough parametric reform had already proved hard to implement, while the public pension scheme exhibited a persistent deficit. Hence, an economic emergency and the financing needs of the public pension scheme had resulted in a significant change in the actor constellation in the pension reform arena. After the principal ally of the new pension orthodoxy, the Minister of Finance, had been strengthened, he could outweigh the Welfare Minister’s opposition. Moreover, in the light of Hungary’s external debt burden, that had been piling up since the 1970s and 1980s, the international financial institutions (IFIs) were important players. Clearly, agenda-shifting in Hungarian old-age security was facilitated by the World Bank, aiming at the creation of a precedent: ‘Passage of the Hungarian pension reform by Parliament has demonstrated the political and economic feasibility of this type of reform in Central Europe’ (Palacios and Rocha 1998: 213).

8. Pension reform was made politically palatable by a bundling strategy. Most of the politically sensitive parametric reforms were legislated simultaneously with the introduction of individual pension fund accounts – a highly visible move that distracted public attention from the changes in the public tier. The funded tier was perceived as granting tangible property rights, while also implying a change of constituencies by the creation of new stakeholders (Graham 1997). Moreover, reformers resorted to direct financial compensation when stipulating a compensatory pension payable to those who partially opted out of the public scheme and switched to the private funded tier. The extraordinary quick passage of the pension reform laws in Congress was not only due to the governing coalition’s strong parliamentary majority, but also to pre-legislative negotiations with relevant opponents over the pension reform draft, most notably the trade unions. In reference to corporatism, Congress had conditioned its approval of the pension laws to the consent of trade unions. It should be noted, however, that the reformers were only willing to compromise on first-tier reforms, while their basic paradigm choice - partial pension privatisation instead of a mere parametric reform – was not put up for discussion. This implied that many deficiencies of the public scheme either remained unsolved or were shelved until 2010 (Augusztinovics et al. 2002). The government’s strategy to opt for a mandatist approach to the legislature – instead of using Congress as a policy forum to build political consensus for the iconoclastic laws – ultimately backfired, as the incoming Orbán government showed little commitment to the reform and changed some of its basic parameters (Müller 2002d).

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5. James (1998) points to the fact that Hungary’s credit rating from Moody’s improved after partial pension privatisation was adopted, in spite of the fiscal costs of the move.


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pension path). From 2002, the Orbán government reopened the purely public pension path to new entrants to the labour market.
The case of Poland

9. While economic crisis had afflicted Poland’s main pension system, ZUS, since the 1980s, the financial strain was greatly aggravated by economic transformation. However, policymakers had experienced strong resistance from the ‘grey lobby’ when they attempted to introduce relatively modest reforms. Subsequently, the Ministry of Finance and economists advocated Latin American-style pension privatisation, while the Ministry of Labour and professors of social insurance law argued that a thorough reform of ZUS was sufficient. For a year and a half, pension reform was deadlocked by the conflict between the Ministries of Labour and Finance. In early 1996, after a cabinet reshuffle, a new Minister of Labour was appointed, Andrzej Baczkowski, who quickly became the most important individual actor in Polish pension reform, moving his Ministry considerably closer to the Ministry of Finance’s position. The idea was to combine a reformed, down-sized ZUS with a newly created, mandatory fully funded tier, and to get all pension reform laws passed before the parliamentary elections, due in September 1997. However, Baczkowski’s sudden death delayed reform preparations.

10. Eventually, the outgoing government, dominated by the post-socialist SLD, enacted the new private pension fund tier before the elections and presented itself to the electorate as the author of a nearly completed pension reform. The more intricate part - ZUS reform, without which the private tier could not come into force - was left to the incoming government, formed by Solidarity and the liberal UW. Throughout the entire legislative process, the pension reform team negotiated with potential opponents of the envisaged reform, notably trade unions and pensioners’ organisations, and agreed to some modifications of the first-pillar reforms, that were finally enacted in late 1998. Poland’s new pension system came into effect in 1999. The old ZUS scheme was fundamentally restructured, the most important change being a shift towards the notional defined contribution (NDC) principle. In addition, a new private pension fund tier has been set up, to which 37.4 per cent of contributions are channelled, while 62.6 continue to go to the first tier. The introduction of a NDC scheme makes Polish first-tier reforms more sweeping than the ones in Hungary.

11. When this iconoclastic reform package was being prepared, the severe transitional crisis was already over. Yet, fiscal imbalances persisted, and the pension system was seen as ‘the most important source of the budget deficit’ (World Bank 1997b: 72). By that time Poland was still severely indebted and closely monitored by its creditors who expressed concern about the slow-down of reforms. By the mid-1990s, pension privatisation was much recommended by the World Bank and soon turned into a key element on Poland’s outstanding agenda of structural reforms. As in Hungary, the move was initiated by an ‘unlikely’ post-communist government, facing a special need to signal its commitment to market-oriented
reforms and to fiscal sustainability. The macroeconomic blessings ascribed to pension reform and the fiscal impact of ZUS turned the Minister of Finance, Grzegorz Kolodko, into a key actor in the pension reform arena, emerging as the winner from his conflict with Labour Minister Leszek Miller. Afterwards Miller’s successor Baczkowski took a lead in the pension reform project. Contrary to their Hungarian counterparts, Polish reformers managed to build a cross-party consensus on the need for structural pension reform, allowing for a continuation of the unfinished legislative agenda in spite of the 1997 government change. The political alternatives were clearly less attractive: a continuation of the high subsidies to ZUS at the expense of other government expenditures, or drastic retrenchment in the public pension system - a politically sensitive if not impossible move, given that the Constitutional Court had effectively vetoed modifications of acquired pension entitlements (Hausner 2001).

12. The World Bank supported the Polish pension reform with expertise, international networking and financial assistance. A special task force for pension reform was established, headed by Michal Rutkowski, an economist on leave from the Bank, in an effort to circumvent intra-government resistance. The reformers’ early idea to bundle the sensitive ZUS reforms with the introduction of the new funded tier was soon replaced by deliberate unbundling and sequencing, thereby enabling fundamental pension reform in a pre-electoral context. The incoming government decided to bundle up pension privatisation with three other major public sector reforms, starting simultaneously on 1 January 1999. This strategy has been linked to the severe implementation problems that occurred, as there was virtually no vacatio legis. It should be noted that pension reform was legislated by the only two subsequent post-1989 governments with a large majority in Congress. Nevertheless, policymakers did not opt for mandatism, but for parliamentarism and concertation, negotiating with the opposition in the legislature and beyond. However, they compromised only on first-tier reforms, not on pension privatisation.

The case of Croatia

13. In the 1980s, when Croatia still formed part of Yugoslavia and the country was hit by a severe economic crisis, a federal law introduced wage-based pension indexation to halt the decrease in the standard of living of the elderly. Consequently, replacement rates reached more than 90 per cent of wages (World Bank 1997a). After independence, economic transformation and the consequences of the war only added to the dire situation of Croatia’s pension finances, as the ratio of contributors to retirees experienced a dramatic drop. As part of the 1993 fiscal adjustment package, the wage-based indexation of retirement benefits was discontinued. Other parametric changes were put off during wartime, yet the continuous worsening of all relevant indicators made it ever more evident that comprehensive pension reform was unavoidable. The paradigmatic turning point is marked by an international pension conference held in Opatija in November 1995, attended by José Piñera and other prominent experts. It was at this conference, sponsored by the World Bank, that the Prime Minister publicly endorsed the introduction of a mandatory funded tier. The Chilean reformers had managed to challenge the strong cognitive reference that the German model had constituted in Croatia’s early post-independence years.

14. However, the fiscal implications of pension privatisation were a matter of concern, leading to a lowering of envisaged second-tier contributions from 10 to 5 per cent of wages. In 1997 a World Bank report recommended a sequenced strategy: if first-tier reforms would be carried out first, cutting down on existing pension entitlements, they would allow for a lowering of the subsequent transition costs of partial

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11. For the credit that the move earned see World Bank (1999b: 10): ‘Poland can take pride in the fact that it is one of a limited number of countries which has successfully launched a complete restructuring of its social security system.’

pension privatisation. In the same year a law on first-tier reforms was submitted to Congress. In its first two articles, it established the three-pillar model, although the second and third tiers required separate legislation. In 1998, when the first-tier law had its second reading, the Constitutional Court ruled on the suspension of the wage-based indexing of pensions. The move was declared unlawful, and pensioners were to be compensated for the drop in replacement rates. With its significant fiscal implications, the verdict provided a major impetus for the approval of the first-tier law, while also distracting public attention from the parametric changes. Second- and third-tier legislation was passed in May 1999. The political regime change occurring in early 2000 delayed the establishment of the funded tiers until January 2002, while first-tier reforms had taken effect from January 1999.

In 1994, when the World Bank published its global pension reform proposal, Croatia had not yet gained access to international capital markets and depended on the IFIs for external financing, while the war and its consequences amounted to a severe drain on the state budget. With its ascribed potential to boost the rate of domestic savings, policymakers hoped that pension privatisation would give them more financial leeway. At the same time, the move seemed useful to signal the government’s commitment to market-oriented reforms at a time when the country suffered from political isolation and had fallen behind in the transition to a market economy. By all accounts, the World Bank was the principal agenda shifter in the Croatian pension reform arena. It sponsored the crucial Opatija conference and subsequent preparatory work, provided technical assistance, financed IT systems and promised a loan to co-finance transition costs. It is interesting to note the double role of former Assistant Finance Minister Anusic, a key domestic actor, who later joined the Bank and was then seconded to the Croatian pension reform team.

Throughout the reform process, the Ministry of Finance played an important role, while the Ministry of Labour remained passive. The Pension Institute, running the public old-age security scheme, rejected the funded tier, while actively preparing first-tier reforms. The strong role of the Ministry of Finance in pension privatisation can be linked to the ever-worsening financial situation of the public pension scheme, translating into substantial budgetary transfers. The sensation of crisis intensified significantly after the Constitutional Court ruling on the indexation problem, thus facilitating the passage of substantial first-tier reforms. However, the considerable delay in legislating and implementing pension privatisation in Croatia reveals concerns that the move would worsen the severe financial situation of the Pension Institute in the short and medium run, thus complicating compliance with budgetary targets. Moreover, in the Croatian case poor capital market development was perceived as a constraint to the swift introduction of a mandatory funded tier.

To ensure passage of the reform laws, the Tudjman regime relied on a mandatist style, without making a great effort to achieve consensus with opposition parties and social partners (Zrinscak 2000). The sequencing strategy chosen by the Croatian government, that started with a downsizing of the public scheme and introduced an funded tier only three years later, also deserves attention and can be linked to a fiscal rationale. Unbundling was not complete, however, as the government had stipulated the multi-pillar approach in the first two articles of the first-tier law. The Tudjman era was marked by authoritarian traits, a

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13. The insured are divided into three age groups: for those younger than age 40, it is mandatory to split the contribution between the reformed PAYG tier (14.5 per cent of wages) and the second, funded tier (5 per cent of wages). Those aged between 40 and 49 are given six months to choose between the mixed and the purely public pension path, while those aged 50 and above are mandated to stay in the public tier with their entire contribution (19.5 per cent of wages).

14. When the three-pillar model was eventually legislated, the move earned its credit: ‘Pension reform is a policy area in which Croatia joined the ranks of other reformers in Central and Eastern Europe’ (World Bank 2000a: 8).

15. Jacoby (1998: 18) has defined agenda shifting as the power to intervene at critical moments, introducing crucial new models in a policy arena.
single majority party and a powerful presidency. Interestingly, this context did not guarantee quick pension reform – six years elapsed between the first public announcement of pension privatisation at Opatija and its actual implementation, while it is also remarkable that the iconoclastic project survived a major regime change.

**The case of Bulgaria**

18. The process of economic transformation had a profound impact on the Bulgarian PAYG scheme. The number of insured plunged, as many workers lost their jobs, while others left the country in search of a better future. At the same time, the number of old-age pensioners in the general scheme increased substantially. The system dependency ratio jumped to 82.7 per cent in 1994, and the pension scheme was in permanent need of subsidies from the state budget. At the same time, average replacement rates had dropped to a mere 29 per cent of average monthly salaries by 1997, leading to a crisis of confidence in the public scheme. ‘At present in Bulgaria old age is virtually synonymous with poverty’ (Ministry of Labour 1994: 77).

19. In post-1989 Bulgaria, a frozen communism/anti-communism cleavage translated in short-lived governments, with political modernisation and economic reform running markedly behind schedule. Bulgarian pension reformers had received conflicting advice from the International Monetary Fund (IMF) and the World Bank, on the one hand, and the ILO, on the other. In a White Paper, the Labour Ministry explicitly rejected the idea of pension privatisation (Ministry of Labour 1994). Fully reflecting the ‘new Bulgarian political system of post-communist corporatism’ (Deacon and Vidinova 1992: 86), only the existing minimum consensus between the government and the social partners was turned into law in 1995: pension finances were separated from the budget, and an autonomous National Social Security Institute ( NSSI) was created, featuring a tripartite supervisory board. When the NSSI needed to be equipped with sophisticated IT, the Bulgarian government decided to approach the World Bank in this matter and was promised help. The loan for the public pension scheme triggered the socialist government’s commitment to a supplementary funded tier for privileged labour categories, while the Bank’s initial proposal to downsize the public tier to a flat-rate scheme was rejected in the light of the country’s long social insurance tradition.

20. The World Bank’s leverage and agenda-shifting took effect in a two-step process. While the funded tier was initially limited to those occupations that enjoyed privileged treatment, the second-tier plans were extended to include a universal funded scheme when a centre-right government took office in 1997. In the midst of an acute economic crisis and near-default on the country’s external debt, the first government in post-1989 Bulgaria to serve its entire term of office was fully committed to multi-lateral recommendations on economic policy. In this context, pension privatisation was useful to signal the government’s commitment to a market-oriented course. Moreover, there was an interaction among structural reforms: the strict fiscal discipline required under the newly introduced currency board arrangement heightened the impetus for pension reform, while reformers also thought that private pension funds could transform privatisation vouchers into tangible benefits. This account points to a two-layered crisis shaping pension reform: in a first step, the dire state of the pension system turned far-reaching reform into a necessity, while the subsequent decision for partial pension privatisation was taken in the midst of a general economic emergency that granted the IFIs a powerful role, enabling them to condition structural adjustment loans to pension privatisation.

21. As to local actors in the Bulgarian reform arena, it is remarkable that the Ministry of Labour took the lead in all pension reform preparations throughout the 1990s, even after the paradigm change, while the

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Ministry of Finance played a less visible role than elsewhere. Moreover, it is interesting to note that trade unions turned out to be supportive of the envisaged multi-pillar model. Previously, they had been granted a role in the NSSI’s tripartite board of directors and were thus aware of the PAYG scheme’s financial difficulties. Moreover, both trade union confederations – the post-communist KNSB and the independent Podkrepa – had developed business interests in the pension fund industry that preceded structural pension reform. In a similar vein, Labour Minister Ivan Neikov’s harmonious co-operation with the new pension orthodoxy can be related to the fact that he had been a vice president of KNSB, while also serving a spell on the managing board of its private pension fund, Doverie. Other participants in the voluntary pension fund sector, such as insurance companies, were also among the stakeholders inclined towards a mandatory funded tier, although the strict third-tier regulations turned out to affect the industry.

22. The Bulgarian reformers chose a sequenced approach to the legislative process. While legislation for the first and second tier was still being prepared, the need to regulate the existing third-tier industry implied that the respective piece of legislation was sent to Congress ahead of the other laws, being passed in July 1999. Afterwards, the Mandatory Social Insurance Code, the main legislation covering all obligatory pension tiers, was submitted to Congress. Most objections concerned first-tier legislation, and reformers had to compromise on the increase in retirement age on the request of trade unions. Moreover, parliamentarians gave in to pressures from the pension fund sector to move the envisaged start of the universal second tier forward from 2004 to 2002, while the cut-off age was increased, thus speeding up second-tier development and guaranteeing a larger market. Eventually, the pension reform package was approved in December 1999, while it was phased in gradually from January 2000 to January 2002, supported by a USAID-sponsored team of experts.17

23. The Bulgarian reform process was marked by a corporatist policy style. Although trade unions were not vested with formal veto points, pension reformers made an effort to obtain their consent both before and during the legislative process. Familiar with non-Bismarckian types of pension provision and granted with stakes in the pension fund industry, they turned into important allies of the pension reform team, the cuts in the public scheme notwithstanding. Congress was another important forum to discuss and negotiate the reform, hence the reform process also exhibits parliamentarist features. Meanwhile, the iconoclastic reform has survived its first regime change after being endorsed by the newly elected government of Bulgaria’s ex-monarch, Simeon Saxe-Coburg-Gotha.

**Dismissing pension privatisation in the Czech Republic and Slovenia**

**The case of the Czech Republic**18

24. Compared with other post-socialist countries, the drop in the insured/pensioner ratio occurring in the context of economic transformation hit the Czech Republic only in the second half of the 1990s, after economic crisis had pushed unemployment rates up. In the first half of the decade, when labour market

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17. The first tier, run by the NSSI, underwent substantial reform and is still mandatory for all insured. The second tier consists of occupational funds and of universal pension funds. The former scheme started in January 2000 and is run by private pension funds. Since then, employers are mandated to contribute 12 per cent for their first- and 7 per cent for their second-category workers to these newly created institutions.

indicators were still relatively favourable, the basic conflict surrounding pension reform in the Czech Republic had been about the scope of parametric reform. Against the fierce opposition of trade unions, the government obtained parliamentary approval for a very controversial Pension Insurance Act in 1995, that introduced a two-part pension formula and raised the retirement age. Advocates of full or partial pension privatisation made themselves heard only afterwards. Young Czech economists connected with the international orthodoxy – ‘market komsomols’ in local jargon – had joined forces with the stakeholders from the local financial community and the liberal Union of Freedom to place pension privatisation on the political agenda.

25. However, these efforts at agenda-shifting did not succeed in having an impact on the overall reform strategy pursued by the Czech government. After simulating the impact and costs related to a partial privatisation of the pension scheme, as against the alternative, a thorough reform of the existing pension scheme, the experts at the Ministry of Labour concluded that there was still sufficient leeway within the existing public PAYG system to face the challenges of the next decades. The World Bank, the main promoter of pension privatisation elsewhere, was absent from the Czech reform arena. The Bank’s lack of leverage in the Czech Republic coincides with a low level of external debt.

26. For almost a decade now, the only portfolio involved in the Czech pension reform efforts has been the Ministry of Labour and Social Affairs, traditionally inclined towards Bismarckian and Beveridgean concepts. As the public pension scheme was financially viable without subsidies from the general budget until contribution rates were lowered in 1997, it came as no surprise that the Ministry of Finance, a potential intra-governmental advocate of pension privatisation, had no stake in pension reform. However, the Czech pension scheme has been in the red for almost five years now, and successive Finance Ministers have still remained passive. One possible explanation is related to the fact that pension privatisation implies substantial fiscal costs on the short and medium run. On the other hand, the severe economic and financial crisis that hit the Czech Republic in 1997 should be recalled. Given the still shaky bases of the local capital market, the introduction of a mandatory funded tier was deemed particularly inappropriate. Owing to the substantial costs of bank bailouts, the financial sector crisis also translated into a fiscal burden, thereby contributing to a narrowing of the budgetary scope for pension privatisation.

27. The Czech trade unions, another relevant political actor, used to be a fierce critic of the parametric reforms envisaged in the first half of the 1990s. This became particularly manifest during the conflicts surrounding the 1995 Pension Insurance Act. Even if they were in no position to veto this law, their opposition raised public awareness about the unpopular retrenchment measures and contributed substantially to the electoral defeat of the conservative coalition in 1996. Yet, with the appearance of pension privatisation on the Czech agenda, unions changed their stance. Instead of pushing for the maintenance of the status quo, they now claim that the existing options to reform the public PAYG scheme have not yet been exhausted in the Czech Republic, opposing a full or partial shift to funding. Given the vociferous role that unions have played in the past, policymakers are likely to take them into account, in spite of the absence of strong corporatist decision-making structures in the Czech Republic. Politically, their campaigns translated into support for the Social Democrats and the Pensioners’ Party, with the latter single-issue party failing to enter Parliament.

28. This country’s paradigm choice beyond the dominant international mainstream might appear particularly surprising, given the neoliberal discourse of the long-standing Czech Prime Minister, Václav Klaus – seemingly an excellent ideational match for the new pension orthodoxy. However, Klaus frequently departed from his ‘market economy without an adjective’ rhetoric when it came to practical politics (Stark and Bruszt 1998). His favourite pension reform path involved very low replacement rates in the public tier to create incentives for Czechs to join the new voluntary pension tier introduced in 1994. Klaus, inspired by Thatcherite social policy and an outspoken critic of corporatism, had pushed for an individualistic approach. A proposal by the Ministry of Labour and Social Affairs, supported by trade
unions and employers’ associations, to introduce occupational pension schemes as in Continental Europe was dismissed.

29. It should also be remembered that since 1996 - i.e. the very moment when the Poles and Hungarians started preparing their partial pension privatisations - Czech governments could not count on a parliamentary majority. The Social Democrats, governing since 1998, were opposing pension privatisation, together with their main political ally, the trade unions. Public support for such a paradigm shift was also minimal (Vecernik and Mateju 1999: 201). In the past years the executive’s control of the legislature was so limited that the government’s plans for a substantial parametric reform were not politically feasible either, thus only increasing their urgency. With elections due in 2002, it is likely to be the next government that will determine the future of the Czech PAYG scheme.

**The case of Slovenia**

30. In Slovenia, high replacement rates dating from the recent Yugoslav past led to a high level of pension expenditure, second only to Poland in the entire post-socialist region. With net replacement rates peaking at 89 per cent of wages in 1990, while still reaching 76 per cent in 2000, the Slovene Institute for Pension and Disability Insurance relied on budgetary transfers throughout the whole decade. Contrary to other transition countries, Slovenia enjoyed considerable fiscal leeway, but the level of these ever-rising transfers indicated the need for action. In Slovenia, two major legislative efforts to fix the PAYG system stand out - the Pension and Disability Insurance Acts of 1992 and 1999. While the former mainly introduced stricter eligibility rules, the 1999 Act followed four years of substantial negotiations, both within the ruling coalition and with social partners. It introduced a system of penalties and bonuses for early and delayed retirement, increased the pensionable age for women, decreased accrual rates and further tightened eligibility. It also transformed branch privileges into an employer-financed, pre-funded scheme managed by Kapitalska družba, the Pension Management Fund.

31. Although a shift to a universal funded tier was eventually disregarded by local policymakers, the new orthodox template did play a temporary role in the Slovene pension reform arena. According to the account in Stanovnik (2002), the relevant agenda shifters in the local reform debate appear to have been the IMF and the World Bank. During an expert mission to Slovenia in 1995, the IFIs emphasised the need for more fundamental reforms in the public pension scheme and also proposed the introduction of a multi-pillar scheme. Subsequently, the World Bank sought to support pension privatisation in Slovenia by means of an earmarked loan, while also co-sponsoring an international pension conference in October 1997 and a workshop on second-pillar issues in March 1998, both in Ljubljana, as well as trips to Switzerland and the Netherlands for first-hand experiences with multi-pillar schemes.

32. As regards local actors, the multi-pillar agenda was pursued by Tone Rop, clearly one of the most influential individual policymakers in Slovenia and a leading figure in the LDS - the centre-left party that dominated Slovene politics since independence. An economist and former State Secretary of Privatisation, he assumed the Ministry of Labour after the resignation of his social democratic predecessor in 1996. Pension reform soon became his top priority. The initial policy document, elaborated with a significant input of Milan Vodopivec, a former World Bank official, strongly advocated partial pension privatisation. The subsequent White Paper on Pension Reform was co-authored by a team of Phare consultants, among them a leading ILO specialist. These French and Italian social security experts took a more cautious stance on the proposed mandatory second tier, notably with regard to its fiscal implications, a concern

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corroborated by simulation exercises. However, the final version of the White Paper, published in November 1997, still included pension privatisation.

33. When the White Paper was discussed with social partners in a working group in January 1998, the Slovene trade unions used this pivotal chance to veto pension privatisation irrevocably. Soon thereafter, they held several large rallies against some of the envisaged parametric reforms and the introduction of a mandatory second tier. The Pensioners’ Party, another ally within the ‘grey lobby’ and a member of the governing coalition during the pension reform process, also declared its opposition. Moreover, criticism against the government’s plan to partially privatise old-age security was raised by some well-known social security experts with a background in economics and law. One of the most influential Slovene economists, Velimir Bole, highlighted the substantial fiscal costs of the proposed multi-pillar scheme in a paper commissioned by the World Bank. At this point, the Minister of Finance, Mitja Gaspari, publicly declared that a mandatory second tier would not be fiscally feasible, inducing Tone Rop to give up on pension privatisation.

34. At a cabinet meeting four weeks later, the pension reform course was quietly changed. The draft law on pension and disability insurance, approved by the Slovene government in June 1998, proposed a reform of the public PAYG scheme in combination with the introduction of a voluntary funded tier. As noted above, a small mandatory funded scheme, run by Kapitalska družba on a supplementary basis, covers only those insured involved in particularly hard and unhealthy work, or performing activities which cannot be continued after attaining a certain age. After lengthy negotiations within the ruling coalition and with social partners, this pension reform law was passed in December 1999. With a rather broad political alliance governing Slovenia from 1997 to 2000, policymaking was characterised by the search for consensus rather than by the rapid enforcement of radical structural reforms.

A Comparative Analysis of Pension Reform Choices

The new pension orthodoxy

35. In many East European countries, the public-private mix in mandatory pension provision has been changed significantly over the past decade. Before structural pension reform was implemented, monolithic public pension systems dominated the post-socialist region, and supplementary private old-age schemes were introduced only gradually. The above account has shown that by now, policymakers in several countries of Eastern Europe and the Former Soviet Union have introduced private old-age provision on a mandatory basis, while at the same time downsizing the public tier. 20 The recent move towards pension privatisation implied the adoption of a ‘worker-choice model’ (Lindeman, Rutkowski and Sluchynskyy 2000: 32). This system of individual retirement savings accounts, managed by competing pension funds, has also been dubbed ‘mandatory, forced saving program’ (Hemming 1998: 22).

36. An increasing amount of contemporary policy change is affected by policy transfer and the global diffusion of models (Dolowitz and Marsh 2000). Conservative critics of the welfare state had long prepared the ground for a paradigm change in old-age security, as described by Hirschman (1991). Yet, the cognitive availability of the Latin American precedents was pivotal to turn pension privatisation from a theoretical concept into a political reality (Weyland 2001). 21 It was in the wake of the end of the cold war

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20. The only transition country where the public scheme was closed altogether was Kazakhstan (Andrews 2001).

that the terms of the prevailing discourse in old-age protection shifted, interacting with the rise of neoliberalism as the dominant paradigm in economic policymaking, particularly in developing and transition countries. Today, a dominant epistemic community\(^{22}\) can clearly be identified: a new pension orthodoxy has been giving major impulses to pension privatisation, arguing that such paradigm change in old-age security would lead to both a rise in saving and to efficiency improvements in financial and labour markets, thereby resulting in an increase in long-term growth (e.g., Corsetti and Schmidt-Hebbel 1997).\(^{23}\)

37. The recent wave of full or partial pension privatisation, \(i.e.\) the adoption of similar blueprints across countries, suggests a common international transmission mechanism of ideas. Although individual Latin American reformers passed their experiences on to East European policymakers, in person or via their writing\(^{24}\), direct diffusion effects from Chile and other Latin American reform precedents were rather weak in the post-socialist region, with the exception of Croatia and Kazakhstan. Latin America carried the stigma of being a less developed region (Orenstein 2000), making it unsuitable as a benchmark case. However, Latin American-style pension privatisation was recommended as a major reform option by the IFIs, most notably the World Bank (World Bank 1994; Vittas 1997). While originally not contained in the so-called ‘Washington Consensus’ (Williamson 1990, 2000), pension privatisation has since become part and parcel of the neoliberal reform package. To provide first-hand information on Latin American pension reforms, the World Bank and USAID also sponsored trips to Argentina and Chile for Polish and Bulgarian MPs, social security experts and journalists.

38. Hence, in Central and Eastern Europe, where the connotations of the ‘Chilean model’ were more likely to refer to the Pinochet regime than to a regional example of economic success, the IFIs played an important though mostly low-key role as agents of transmission, helping to enhance the low status of the Latin American precedents (Nelson 2000; Müller 2001a).\(^{25}\) Apart from the ubiquitous conditionalities, channels to support pension privatisation include loans and an expert-based knowledge transfer - a potentially attractive assistance package for local policymakers. Although the IMF and USAID have taken part in relevant cross-conditionalities with the Bank, as well as other forms of co-operation, overall they play a less outstanding role.

Political actors and the policy context in pension reform

39. While the privatisation of old-age security was clearly a major policy recommendation from abroad facing any pension reformer in Central and Eastern Europe, it was the domestic political process that eventually resulted in the adoption or rejection of radical pension reform, as the above case studies have made clear. The following analysis includes the identification of relevant political actors in the

\(^{22}\) An epistemic community is a network of professionals in a particular domain and with a common policy enterprise, who may come from different professional backgrounds. They share faith in specific truths and in a set of normative and causal beliefs, have shared patterns of reasoning and use shared discursive practices (Adler and Haas 1992; Haas 1992).


\(^{25}\) In this context it is interesting to note that ‘adopters eventually become source countries themselves’ (Kay 1998: 47). Argentina, that set out to replicate the ‘Chilean model’ and ended up with a mixed variant, later exported its model to the transition countries. Later, partial pension privatisation in Poland and Hungary seems to have triggered another regional contagion effect from the Baltics to the Balkans.
pension reform arena and the consideration of the policy context that shaped their room for manoeuvre, influenced by political factors and economic conditions.

40. Scholars of the political economy of policy reform have stressed the importance of political leadership – courageous, committed individuals, often market-oriented economists – and their ability to communicate a coherent vision (Harberger 1993; Sachs 1994). Pension privatisation amounts to a paradigm shift that may be greatly facilitated by such committed policymakers famous for the radical economic reforms they pushed through, such as Bokros in Hungary. In Poland, there is unanimity that radical pension reform would have been impossible without the initial push by Baczkowski. Rutkowski and Anusic, World Bank economists on leave, played an important role in Poland and Croatia. However, the existence of such agenda setters can certainly not be considered sufficient to guarantee success against powerful interest groups (Williamson and Haggard 1994; Tommasi and Velasco 1996). This is particularly highlighted by the Slovene case, in which one of the most influential individual policymakers could not impose pension privatisation against the unions and the Finance Ministry.

41. Bresser Pereira, Maravall and Przeworski (1993: 208) have pointed out that policy reform has been pursued in four distinct styles: while decretism (reliance on presidential rule by decree) and mandatism (executive use of a legislative majority to short-cut legislation) are two exclusive, technocratic policy styles, parliamentarism and corporatism/concertation involve extensive negotiations with opposing forces in the legislature and beyond. The ‘technocratization of decision-making’ (Silva 1999: 58) has been criticised, as it weakens democratic institutions and rules out consensus building required for political sustainability (Bresser Pereira, Maravall and Przeworski 1993; Stiglitz 2000). A parliamentarist and/or corporatist policy style was chosen in Bulgaria, Poland and Slovenia. Pension privatisation was pushed through by mandatism in Croatia. Corporatism was combined with mandatism in Hungary; a case highlighting that insufficient consensus building can lead to severe alterations in reform design by subsequent governments and ultimately threaten the sustainability of the move.

42. When it comes to institutional or individual actors that have been relevant in the pension reform arena, most of the above cases of pension privatisation have witnessed the Ministry of Finance as a key player. This Ministry is often staffed with neoliberally trained economists who feel that pension privatisation perfectly matches their overall efforts to decrease the role of the state in the economy. The role of the Minister of Finance was especially pronounced in Poland, Hungary and Croatia. This actor, for whom pension privatisation was a means to achieve macroeconomic rather than social objectives, was supported by local interest groups, such as business organisations and the financial sector, as well as the IFIs.

43. Contrary to this, the Ministries of Labour or Welfare, responsible for the existing old-age security schemes, were often reluctant to engage in structural pension reform, thus reflecting the existing Bismarckian traditions in Central and Eastern Europe. In Poland and Hungary, these Ministries objected to the radical paradigm shift, but - given the predominance of the Finance Ministry in the cabinet - proved too weak to prevent it. In many cases of pension privatisation, the Labour Ministry’s influence on reform design was deliberately limited by the setting up of small task forces that worked out the draft legislation and served to bypass the Labour Ministry’s pension-related competences (Müller 1999; Nelson 2001). This policy pattern confirms the technocratization of decision-making and the key role of ‘insulated policy-making elites’ in pension privatisation (Schamis 1999: 265). In Poland and Bulgaria, Labour Ministers that had rejected the shift to funding were replaced with new ones with an ex ante commitment to a mandatory funded tier, in order to facilitate the iconoclastic move. In Slovenia, the ideational distinctions between

both Ministries proved to be less clear-cut: the Minister of Labour, an economist, was the principal advocate of partial pension privatisation, but was vetoed by the Minister of Finance and the trade unions.

44. In many countries, social security employees, pensioners’ associations and/or special interest groups with privileged pension schemes have opposed pension privatisation. In the post-socialist world, trade unions have also been dubbed ‘pensioners’ parties’ since many of their members are retired. In the Czech Republic and Slovenia plans to reform old-age security triggered the largest political rallies since independence. It is interesting to note that the Czech unions voiced strong opposition against the 1995 pension reform law, but started to advocate parametric reforms when pension privatisation appeared on the political agenda. The Pensioners’ Party failed to enter Parliament in the Czech Republic, yet it even formed part of the governing coalition in Slovenia at the time of the 1999 reform. Contrary to this, Poland’s Solidarity trade union even participated in the conceptual debate on systemic pension reform with an early proposal in support of a partial shift to funding. In Croatia most trade unions voiced opposition against pension privatisation, except for the union of state employees, that considered setting up a second-tier pension fund. Interestingly, the retired persons’ trade union also agreed with the move to funding. Trade unions in Bulgaria also supported partial pension privatisation, given their business interests in this industry.

45. Left-wing parties did not always join the ranks of the opponents of a shift to funding either. There have been many cases where market-friendly reforms have not been carried out by conservative free marketeers, but rather by left-wing governments - a phenomenon called the ‘Nixon-in-China syndrome’ (Rodrik 1994). Among the above case studies, the post-socialist governments in Poland and Hungary are among the ‘unlikely’ administrations involved in pension privatisation. It has been argued here that in a context of high indebtedness, these left-wing governments were under a stronger pressure from international creditors to demonstrate their commitment to market-oriented reforms. Moreover, they were better suited to handle opposition from trade unions. In both Hungary and Poland, the governing parties had traditional ties with the unions and used them to ease resistance. On the other side of the coin, these ties implied that pension reformers were forced to negotiate with reform opponents and to make concessions.

46. The specific policy context may provide reformers or reform opponents with action resources. The executive’s degree of control of the legislature amounts to an important institutional variable. In Bulgaria and Hungary, the large parliamentary majority enjoyed by the governing coalition allowed for a swift passing of structural pension reform. Contrary to this, in the Czech Republic and Slovenia the political conditions in the second half of the 1990s may have been less than propitious for pursuing radical reform. Due to the broad character of the coalition in Slovenia, the need to embark on consensus-building prevailed, while successive minority governments in the Czech Republic seemed to allow for very little leeway in policymaking. Yet, strong governments do not always embark on radical reform either, as concentrated authority is tantamount to concentrated responsibility, providing little chance of blame avoidance (Pierson 1996). Pension privatisation in Croatia - the outlier in terms of the Freedom House country rating during the Tudjman era - was by no means faster or more radical than in the other cases. A closer look reveals a wavering commitment of the president and the ruling party to the iconoclastic paradigm shift. Clearly, in a context of concentrated authority, leadership in policy reform initiatives is key.

47. Economic factors and considerations have had a substantial impact on the choice of reform model. As noted above, pension privatisation has been primarily proposed for macroeconomic motives, seeking to embark on a virtuous circle leading to economic growth. Madrid (1998) and James and Brooks (2001) have pointed to increased international capital mobility and the recent experiences of capital market crises, that may have induced policymakers to seek to reduce the vulnerability to capital outflows by
boosting domestic savings and the local capital market.\textsuperscript{27} Moreover, scholars of the political economy of policy reform have highlighted that a preceding crisis may induce radical change - the so-called ‘benefit of crises’ hypothesis (Drazen and Grilli 1993).\textsuperscript{28} Crises may enable policy reform because they can change the relevant constellation of actors. In the pension reform arena, they tend to reinforce the ‘privatisation faction’. Fiscal crises turn the Ministry of Finance into a potential actor in the pension reform arena. More specifically, when pension financing goes into deficit, the resulting dependence on budgetary subsidies grant this likely advocate of the ‘new pension orthodoxy’ an important stake in reforming old-age security (Müller 1999). Furthermore, a persistent financial crisis may severely erode public confidence in the public pension systems, thus facilitating fundamental reform. Almost all countries reviewed above experienced a sizeable fiscal deficit and/or high pension expenditure prior to reform. Croatia’s fiscal deficits were low, but public pension spending and system dependency ratios soared. Hungary and Bulgaria witnessed a grave economic crisis before embarking on pension privatisation. In Bulgaria, the need for fiscal restraint was heightened by the adoption of a currency board shortly before preparations for pension reform began.

48. The cases of the Czech Republic and Slovenia show that there is a flip side to the economic factors and considerations that potently pushed pension privatisation elsewhere. In both countries, policymakers were fully aware that pension privatisation would have resulted in substantial fiscal costs in the short and medium run, thus complicating future compliance with the Maastricht criteria. Particularly in a context of high implicit pension debt, this concern may render Ministers of Finance potentially ambivalent allies of the new pension orthodoxy.\textsuperscript{29} Moreover, while the development of the local capital market was a frequently mentioned motive for pension privatisation elsewhere, policymakers in the two countries reviewed here explicitly pointed to the nascent stage of Slovenia’s capital market and the crisis-ridden financial sector in the Czech Republic when cautioning against radical pension privatisation. In Croatia and Bulgaria, similar concerns led policymakers to postpone, albeit not abandon, the introduction of the mandatory funded tiers.

49. Yet another economic context factor needs to be considered. When external debt is high, governments tend to stress their general commitment to market-oriented reform. The announcement of pension privatisation can be interpreted as a ‘signalling’ strategy (Rodrik 1998), as rating agencies include radical pension reform as a point in favour in their country-risk assessments, in spite of its fiscal impact. Critical indebtedness also increases the likelihood of the involvement of the IFIs in the local pension reform arena (Brooks 1998). Their leverage is partially determined by their stakes as important creditors in many transition countries. However, their impact is not limited to binding conditionalities resulting from their own financial involvement. Rather, it is the general level of external indebtedness that matters, as the IMF and the World Bank ‘may signal that a developing country has embraced sound policies and hence boost its credibility’ (Stiglitz 1998: 27). When their recommendations are disregarded by local governments, alternative sources of market financing are often hard to obtain. As noted by Kay (1999), policymakers were well aware that financial and/or technical support from the IFIs was only available for a pension reform that included a privatisation component.

\textsuperscript{27} Yet, contrary to these high hopes, the Chilean evidence suggests that pension privatisation actually had a negative impact on national saving (Mesa-Lago 1998).

\textsuperscript{28} Situations of perceived emergency can induce contending political groups to agree upon unpopular, painful measures and facilitate the destruction of political coalitions that had blocked reform, breaking a previously existing stalemate (Williamson 1994). However, the ‘benefit of crises’ hypothesis has not met with unanimity among scholars of the political economy of policy reform.

\textsuperscript{29} In this context, it is interesting to note that the IFIs have recently modified their stance on fiscal deficits stemming from a shift to funding. In the Hungarian case the World Bank (1999a: 44) argued that ‘the transitional deficit is not a fiscal deficit in the usual sense’, while the IMF (1998: 62) followed a similar line of reasoning with regard to Croatia.
Bulgaria and Poland were classified as severely indebted at the time of pension privatisation, while Hungary was characterised by moderate indebtedness (World Bank 1996; 2001b). The cases of the Czech Republic and Slovenia indicate that the IFIs’ leeway as advocates of multi-pillar schemes may be constrained by contextual factors. Slovenia and the Czech Republic are very advanced transition countries, characterised by a low level of external debt. In this context, both the potential leverage and the interest of the IFIs to spend resources on the promotion of pension privatisation is severely limited. Croatia’s indebtedness was also classified as low, yet Croatia’s political isolation under Tudjman still rendered the IFIs important international allies. Thus, the ‘global politics of attention’ (Orenstein 2001; Orenstein and Haas 2002) needs careful differentiation.

The importance of reform design

It is widely observed that parametric reforms, although moderate in the light of paradigmatic alternatives, are politically sensitive. They easily allow the identification of individual losses and are perceived as a mere cutback of acquired entitlements – without anything in exchange (Holzmann 1994; Müller 1999). The obstacles to parametric pension reform in the Czech Republic only highlight the potential that such reforms may hold to engender sizeable blame. In several of the above country cases, reformers attached great importance to reform design, with a view of lowering the political resistance to pension reform. The relevance of tactical sequencing, strategic bundling, packaging and compensation has been stressed by scholars of the political economy of policy reform (Haggard and Webb 1993; Sturzenegger and Tommasi 1998).

The Hungarian and Polish reformers resorted to tactical packaging when they distanced themselves from the Latin American models and stressed the originality of local reform efforts (e.g. Rutkowski 1998). In spite of the obvious conceptual parallels that indicate a de facto inclination to the Latin American models, policymakers decided to avoid all reference to these precedents, as soon as they found out about the inconvenient connotations among the Central European public (Müller 1999; Orenstein 2000). To mitigate resistance to reform, reformers resorted to direct compensation by granting compensatory pensions to those who switched to the newly established funded tier, even though for fiscal reasons acquired pension entitlements were rarely recognised completely. With the exception of Hungary and Croatia, where the new pension system is truly universal, reformers opted for a strategy of exclusionary compensation and division of potential opponents by exempting powerful pressure groups from structural pension reform.

Full or partial pension privatisation enables policymakers to hand out potentially attractive stakes to potential opponents, thus creating constituencies (Graham 1997). ‘Shifting to a funded scheme … allows for arguments that all can win, thus abandoning intractable zero-sum games’ (Holzmann 1997: 3). In a number of countries reformers granted trade unions the right to run their own pension funds, thus

30. As pointed out in World Bank (2001a: 13), the Czech Republic even has a net creditor position vis-à-vis the outside world. In turn, Slovenia is classified as high income and will soon graduate from World Bank financial and technical assistance altogether (World Bank 2000b). International country ratings indicate that Slovenia and the Czech Republic currently enjoy the best evaluation of all transition countries in terms of investment risk and credit rating.


32. James and Brooks (2001) distinguish between four types of compensation: Exclusionary compensation exempts powerful groups from reform, direct financial compensation tackles groups adversely affected, indirect and cross-compensation imply trading off one policy for another or linking reforms, and political compensation exchanges broader political rewards for support on a specific issue.
converting them into stakeholders of pension privatisation. In Bulgaria, the trade unions’ business interests in the private pension industry even preceded plans to establish a mandatory funded tier, thus facilitating a broad consensus on partial pension privatisation. Contrary to this, neither the Czech nor the Slovene unions were interested in reaping economic benefits from the setting up of their own pension fund in a mandatory tier, contrary to a part of organised labour elsewhere. The Slovene unions were in close contact with their German counterparts, staunch opponents of pension privatisation. In the case of the Czech unions, their reluctance may be connected with the fact that their early involvement within the voluntary pension funds tier remained unsuccessful.

54. Polish policymakers intended to embark on strategic bundling by linking enterprise privatisation with systemic pension reform. However, they eventually decided to use privatisation proceeds to cover transition costs by supplying them to the state budget. While helping to solve the fiscal consequences of a partial shift to funding, this use of privatisation proceeds completely lacks visibility (Gesell-Schmidt, Müller and Süß 1999). In Bulgaria, reformers thought that private pension funds could transform privatisation vouchers into tangible benefits, but met with a lack of enthusiasm among private pension fund administrators to convert vouchers into old-age pensions.

55. As stressed by Pierson (1994), the political costs of reform can be lowered by increasing its complexity. In several East European countries, the reformers’ strategy amounted to bundling up some unavoidable, yet politically sensitive reforms of the public PAYG tier with the more visible introduction of individual pension fund accounts (Holzmann 2000). This ‘obfuscation strategy’ in Pierson’s terms (1994: 21) entails the potential to lower the visibility of the envisaged cutbacks and to draw public attention to the granting of individualised ownership claims. The introduction of the individual pension fund accounts tended to be perceived as the creation of a monitorable track record of individual property rights over time, that the political system would be less likely to take away. In contrast to the unfavourable public perception of parametric reforms, the drawbacks related to pension privatisation are often easier to conceal (Müller 1999).

56. In most East European countries, the scope and financing of transition costs – a major fiscal and distributional issue when it comes to a shift to funding – were successfully shielded from public debate. Hence, the public perception of the strengths and weaknesses of pension privatisation was biased towards its advantages, while the concomitant fiscal burdens were ignored. This asymmetry of perception may explain the observable fact that policymakers have legislated structural pension reform in pre-electoral periods (e.g. in Hungary, Poland), contrary to the conventional notion that retrenchment as well as radical reforms are unlikely to be tackled when the hazards of accountability are high. This suggests that the perceived attractiveness of pension privatisation may outweigh its blame-generating potential, thereby differing markedly from the politico-economic potential of parametric reforms. However, the prospect of new privately-run pension funds was received less enthusiastically in countries where memories of fraudulent pyramid schemes and failing banks were fresh, such as Croatia and Bulgaria.

57. When it comes to sequencing, a fiscally motivated strategy was chosen in Croatia and Bulgaria, that started with a downsizing of the public scheme and introduced an funded tier only three years later. However, as the different components of pension reform were legislated as parts of an overall package and by the same government, an underlying bundling strategy can still be observed. Contrary to this, Polish policymakers resorted to deliberate unbundling in the legislative process, mainly driven by the political business cycle. Pension privatisation was legislated by the outgoing government, while the restructuring of the public tier was left to the new government. Pension reform was then bundled up with three other structural reforms, that were to come into force simultaneously. The latter turned out to be a very costly strategy. Pension reform preparations, most notably the IT system, were not ready on time, but the reform ‘had to’ start anyway, resulting in substantial implementation problems that persist until the present day.
This example highlights that the reformers’ desire to exploit a political window of opportunity to pass and implement pension privatisation may clash with optimal reform preparations and existing state capacities.

**Concluding Remarks**

58. Unlike the bulk of pensions-related research, this paper did not discuss the desirability of alternative pension reform paths.\(^{33}\) Instead, it sought to explain how different pension reform choices came to be made in six post-socialist countries, by analysing the behaviour of individual and collective actors under economic, political and institutional constraints. While strongly encouraged by the IFIs, the radical paradigm change in old-age security was mainly advocated by the Ministry of Finance, staffed with neoliberally trained economists. Pension privatisation perfectly matched their overall efforts to decrease the role of the state in both regions. These important allies of the new pension orthodoxy often faced intra-government opposition from the Ministry of Labour, committed to the Bismarckian traditions in both regions. Partial pension privatisation became feasible when powerful actors inclined towards pension privatisation - the Ministry of Finance and the World Bank - had stakes and leverage in the local reform process. By comparison, radical pension reform did not proceed when the Welfare Ministry was the only relevant pension reform actor. Trade unions played a variety of roles: while staunchly defending the PAYG scheme in some countries, which they often helped to administer through tripartite bodies, they turned into stakeholders of partial pension privatisation elsewhere. Most notably in Croatia and Poland, a seemingly successful defence of the the *status quo* in old-age security in the courts backfired, leading to a shift to funding, as the alternative reform path, based on parametric changes, was effectively blocked. The cases analysed here indicate that, contrary to conventional wisdom in social policy research, far-reaching pension reform is possible in a democratic context. Yet, more comparative research is needed to account for the emerging diversity of patterns in the political economy of pension reform.

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\(^{33}\) For an evaluation of the recent pension reforms in Eastern Europe see, e.g., Müller (2001b, 2002b).
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