OECD
BETTER POLICIES FOR BETTER LIVES

MEXICO

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- **Move towards a truly national pension system: make public- and private-sector schemes converge; eliminate special regimes in public firms and universities; condition part of the transfers to local governments to the adoption of the national scheme; unify non-contributory safety nets and integrate them better with the first-tier contributory pension**

- Increase the mandatory contribution rate to the funded DC system

The current pension system will deliver low replacement rates. In 1997, the mandatory pension system for private-sector workers was transformed from a public PAYGO DB into a private funded DC scheme. Contributions of 6.5% of earnings go to individual DC accounts. In addition, the government contributes a social fee (*cuota social*) for wages below 3.6 times the average wage (in 2018). Upon retirement, the accumulated account balance is used to acquire a price-indexed annuity or a programmed withdrawal. Annuity rates take into account gender-specific life expectancy, implying a lower pension for women with the same pension assets as men. Based on OECD projections, this leads to a net replacement rate of 28.6% for men (26.7% for women) after a full career at the average wage. Moreover, full-career low-wage earners will have the second lowest replacement rate among OECD countries. Employers make an additional 5% contribution to an individual housing sub-account, which reverts to the DC account when it is not used. Including the housing sub-account increases the projected replacement rates to 48.9%, which is still low by OECD comparison. People who are older than 65 years at the time of retirement are eligible to the minimum pension (PMG) in the new DC scheme provided that they have contributed for at least 1,250 weeks (24 years). The same programme is available in the old scheme for those who have 500 weeks of contributions.

Key indicators: Mexico and OECD average

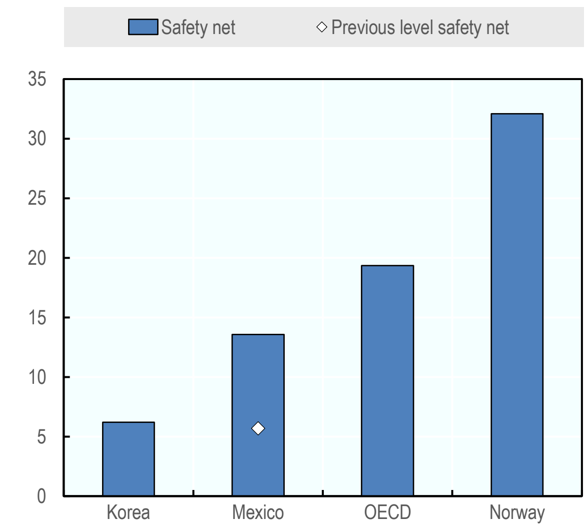
	Mid-1980s	Mid-1990s	Mid-2000s	latest available	latest OECD	long-term	long-term OECD
Normal retirement age for a full-time career starting at age 22	65.0	65.0	65 (60)	65.0	64.2 (63.5)	65.0	66.1 (65.7)
Statutory retirement age	65.0	65.0	65 (60)	65.0	64.5 (63.8)	65.0	66.5 (66)
Net replacement rate, avg earner						28.6 (26.7)	58.6 (57.6)
Effective contribution rate (average earner)				6.3	18.4		
Total pension spending, % of GDP	0.2	0.7	1.0	2.2	10.0		
Public pension spending, % of GDP	0.2	0.7	1.0	2.2	8.5		
Public debt, % of GDP	0	0	0	0	80		
Employment rate 55-64, %		75.7 (25.7)	78.2 (31.1)	76.2 (37.1)	68.5 (54.8)		
Labour-market exit age	78.5 (77.2)	71.2 (73.6)	73.2 (72.8)	71.3 (66.5)	65.4 (63.7)		
Old-age poverty rate, %	28.0	32.7	28.0	24.7	13.5		
Life expectancy at 65, years	15.5 (17.3)	16.6 (18.2)	17.0 (18.9)	16.6 (18.5)	18.1 (21.3)	20.2 (22.1)	22.5 (25.2)
Old-age to working-age ratio	0.09	0.10	0.11	0.13	0.31	0.40	0.58
Fertility rate	3.8	2.9	2.4	2.1	1.7	1.7	1.7

Note. The figures for women appear in parenthesis where they differ from those for men.
Long term: Around 2065 based on all legislated reforms up to mid-2019.

A new universal old-age safety net (*Programa Pensión para el Bienestar de las Personas Adultas Mayores*) for those aged 68 or older was introduced in 2019. The relative old-age poverty rate among people over 65 is very high, above 30%. The new programme replaces the targeted social assistance programme (*Programa Pensión para Adultos Mayores*, PPAM) for people aged 65 or above with a contributory pension below a certain threshold (about 12% of the average wage). Those currently aged 65-67 who were getting the PPAM will automatically receive the new universal pension. Compared with PPAM, the benefit level is much higher - almost 2.2 times higher, 14% of average wage instead of 6% - and is no longer means-tested against pension income. The objective is to reach everyone above 68 years old (8.5 million people in 2019) against 5.5 million with PPAM in 2018. In terms of coverage, the elimination of means testing is offset by the increase in the eligibility age. People who have limited cumulated contributions but are eligible to the PMG might still have poor incentives to participate further in the formal labour market as additional contributions do not generate more pension entitlements. The disconnection between non-contributory pensions and the PMG creates substantial differences as a function of contribution periods and perverse incentives once eligibility conditions for the PMG are met.

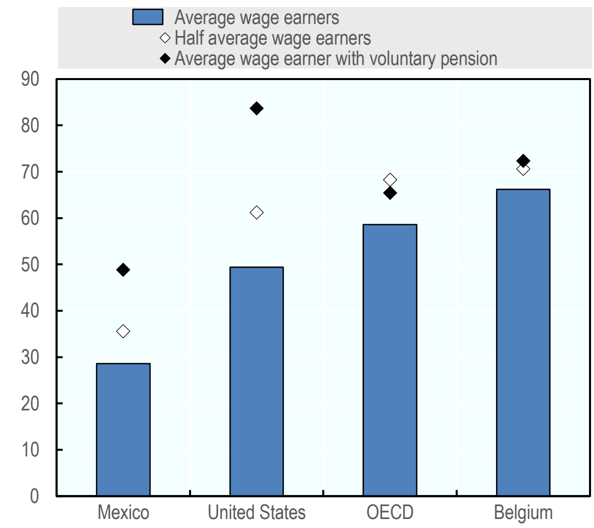
There are large differences in pension treatment within the country. "Transition workers" who contributed to the system at least once before 1997 can opt to have their pension computed according to the heavily subsidised PAYGO DB scheme. Hence, an individual who had contributed to the pension system one month before the introduction of the new system will receive a pension benefit much larger than that of an individual who entered the system one month later and contributed the same with the same work experience. Moreover, the pension system is highly fragmented, far beyond the different treatment of private- and public-sector workers. Some states, local authorities, public universities, other public entities and various professions run independent pension systems. There are also different non-contributory schemes run by federal and local governments. There is coordination neither across the various plans nor across the federal and local levels, even for non-contributory schemes. This generates opacity, duplication and inefficient management, and is a source of large inequalities. The lack of portability of entitlements between schemes and entities also harms labour mobility.

Old-age safety net (% of average wage)



Source: OECD Pensions at a Glance (2019).

Long-term net pension replacement rates from mandatory pensions in the private sector



Source: OECD pension models.

The transition to the new DC system should be smoothed, the fragmentation of the pension system reduced, contributions to the DC system raised and first-tier pensions better integrated. A pro-rated mechanism should be introduced to address the transition from the old to the new system. All the rights acquired by workers in the old DB system would be guaranteed, while new contributions would accrue entitlements in the new DC system. Moreover, the rules for all pension plans should be harmonised, with the ultimate goal of establishing a truly national pension system equal for all. This harmonisation should include the pension plans for private- and public-sector workers, as well as the special regimes (for states, municipalities and universities, among others). To increase retirement income, mandatory contribution rates should be gradually increased and extended to the self-employed. The old-age safety net and the PMG should be better coordinated to ensure that each additional year of contribution results in a higher benefit. Moreover, the minimum contribution period of 1,250 weeks required for the PMG should be lowered, adjusting the benefit level in line with the period contributed. The coordination of safety net programmes run by different levels of government should also be enhanced, for example by making part of the transfers to local governments conditional on the adoption of the national scheme.

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