

Unions' Role in Argentine and Chilean Pension Reform

Teresa Ghilarducci
Patricia Ledesma Liébana
Department of Economics
University of Notre Dame

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Please address all correspondence to Teresa Ghilarducci, Department of Economics, University of Notre Dame, Notre Dame, IN 46556-5639; phone: (219) 631-7581; fax: (219) 232-3086; e-mail: ghilarducci.1@nd.edu.

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SUMMARY

The 1981 privatization of Chilean pensions created immediate winners and observable benefits. It also created a model for Latin American pension reform. This study compares the Chilean and Argentine experiences by using political economy models of social welfare development as a framework for discussion. We suggest privatizing pensions could divide workers or create opportunities for unions to garner control over financial capital investments. The Argentine pension reform may diverge substantially if unions increase their participation in the pension fund management and worker education.

Keywords: Latin America, Chile, Argentina, pensions, unions, political economy

The wave of pension reform in Latin America in the 1990s is part of economic structural adjustment policies that strive to liberalize markets throughout the region. The World Bank's 1994 pension report fits into this agenda, encouraging individual private pension plans and less government-sponsored social insurance. The report argues that creating a fully funded private pension system as the main pillar in an old-age security system would encourage more work and shorter retirements, increase private savings, promote economic growth, and pay better pensions. The exemplar model is Chile's 1981 pension reform. José Piñera — Chile's Labor minister under Pinochet — has called the Chilean model “a solution that empowers all workers” (Piñera, 1998).

This study shows that pension privatization does not necessarily “empower” workers. Rather, it focuses on the unique problems individualizing social insurance entails: problems of evasion and non compliance, unproductive competition between pension fund companies, high administrative costs and increasing industry concentration. These problems could be tempered by allowing group decisions, for which unions can serve as a channel. Unions seek particular goals in a pension system, many of which are present in a pay-as-you-go (PAYG) system, but some are only found when unions share control of advance-funded pensions. By emphasizing the role of unions and their shortcomings, we address an area the World Bank (1994) report's lead author admits was under-examined (James, 1995).

A review of the Latin American experience reveals that while economic conditions trigger pension reforms, they do not entirely explain them. A comparison of the Argentine and Chilean experiences highlights the importance of a democratic environment and the strength and strategies of the actors, especially workers, in determining the shape of pension privatization. We use secondary sources, government data, interviews and models of social-welfare formation to describe how unions and democratic processes affect pension reform such as Chile's in 1981.

One dominant theory of social welfare development are class-based theories, which posit that workers and unions initiate social insurance programs in order to gain economic security. The neo-Marxist variant argues that capitalists initiate social welfare programs in order to make unions complicit and to quell labor revolt (Pampel and Williamson, 1993).

1981 Chile and 1993 Argentina faced financial problems in their PAYG systems — worsening ratios of workers to retirees and an impending financial collapse of their publicly-managed pension system. But these problems could have been solved within a PAYG structure¹. Therefore, although the reform of a nation's retirement system depends on technical considerations about what nations can afford without hindering economic growth, they are also dependent on the relative power of labor and capital and non class interest groups (Kay, 1995; Pampel and Williamson, 1993). We are addressing the second set of variables that determine pension reform.

The first section argues how pension reform becomes capital market reform, while greatly altering the economic security of workers. It briefly examines the arguments that privatizing pensions improves capital markets and economic growth. It also examines worker and union goals for a pension system. Sections two and three compare the Argentine and Chilean cases. Section four discusses how union control and ownership of funds and participation in pension reforms could help mitigate problems of an individual capitalization pension scheme. The final section summarizes the study's main arguments.

1. THE POLITICAL ECONOMY OF PENSION REFORM

(a) Capital markets

The World Bank proposal for mandatory funded pension systems managed by private institutions assumes that savings determine investment and that the private sector allocates resources to their most productive uses, compared to the public sector. Thus funding retirement, rather than taxing current workers, increases savings available for investing².

Feldstein (1996) shares this view and argues that PAYG systems distort individual savings behavior by inducing people to save less because government transfers will solve retirement needs. This diminishes funds available in equity markets and economic growth is compromised.

Despite these arguments in favor of deepening capital markets, critiques of modern finance

markets point to the following problems: imperfect and asymmetric information (Stiglitz, 1989), short-termism and speculation (Singh, 1996; Lazonick, 1992), and agency problems (Jacobs, 1994).

The market for corporate control, as well as shareholder rights movements in the U.S. and Europe, have been viewed as solutions for classic agency problems — that is, where the managers of the companies do not represent the interests of the owners. Instead they pursue their own objectives. In developed economies elaborate regulations allow investors to know and investigate the companies they own. Shareholders vote proxies, go to shareholder meetings, and hire and fire boards of directors

Imperfect and asymmetric information in financial markets causes restricted and high cost borrowing (Stiglitz, 1989; Jacob, 1994). As a result, financial markets can be extremely inefficient in directing capital to productive uses, especially, ventures with medium to long-term time horizons. Government provisions of information, subsidies for housing, local economic development, and venture capital are most often required.

Only in neoclassical theory does savings axiomatically equal investment. Yet, savings only allow investment; its mere supply does not determine the demand for investment goods. Even the most developed capital markets require sophisticated regulation and monitoring; they change unpredictably, rapidly, and are prone to speculative bubbles and crises.

In sum, increasing savings does not generate efficient capital markets. Efficiency requires transparent information about ownership, active and involved owners, and a trusted supervisor to make financial institutions and corporations accountable.

(b) Worker and union goals for pension reform

In industrialized democratic market economies, unions routinely control and influence pension funds. Unions have joint control over worker pension fund investments in the Netherlands, the U.K., France, Australia, and through worker co-determination in Germany. Eight percent of funds in the U.S. are jointly controlled union-management funds and over 50%

of company sponsored pension funds are negotiated by unions. The American federation of labor unions, the AFL-CIO, uses sophisticated corporate campaigns by asserting shareholder rights to question the broad policies of corporate management (Ghilarducci *et. al.*, 1997; AFL-CIO, 1996). Even more unions and government agencies are targeting pension funds toward investments that earn market rates of return and yield economic development goals — such as job creation and housing.

Unions also support pension systems that balance six incongruous goals: adequacy, redistribution, individual and horizontal equity, efficiency, and finally, social and economic stability (Steurerle and Bakija, 1994). Economic stability refers to the Keynesian notion of maintaining consumption during recessions and social stability refers to the ability of social insurance programs to quell working class “revolt” (Pampel and Williamson, 1993). Their relevance for the Chilean and Argentine case is described in the next section.

First, an old-age pension system helps redistribute income, through minimum pensions, progressive taxes financing, and high replacement rates for low earners. Second, individual equity goals ensure individuals obtain a “fair” return from individual effort — higher income workers receive higher pensions. Third, horizontal equity is met when workers in similar work situations receive similar pensions. Individual capitalized plans violate this goal because rates of return differ. Efficiency matters. High administrative costs and perverse incentives, like encouraging retirement at a very early age or requiring a very small number of years for eligibility, diminish the amount of pensions paid.

Workers and unions want social insurance in order to reduce risk. In market economies, most income comes from work. Disability and superannuation are always present risks. Workers saving for pensions face a number of risks: (a) “Longevity risk” — the risk of outliving retirement accounts; (b) Financial risks of market failure and bad investment decisions; (c) Inflation; (d) Non compliance risks — the risk that the worker does not save steadily and the account is too small (Turner, 1997; McGillivray, 1998). Adverse selection is a problem for insurance companies selling guaranteed streams of income. Private insurance companies know

workers can assess their longevity better than the company and long-livers will be more likely to buy the guarantee. Thus, every insurance company expects a high-priced group and charges higher fees to make up for the increased risk. Social insurance plans avoid adverse selection by making participation mandatory and universal. All workers take an annuity, not just those who perceive they will live a long time. Also, mandatory participation bypasses myopia — the tendency for humans to be shortsighted and not foresee substantial future income needs. Social insurance schemes pay, most often indexed, annuities and base pensions on years worked and wages — thus avoiding all financial, longevity, inflation, and non-compliance risks. However, workers in government systems face the risk that politicians can change the benefits — the political risk — and mismanage the system (Diamond, 1994).

In these systems the financial health of the universal social insurance program is based on the financial health of the labor force. For example, half of the projected U.S. Social Security deficit would not exist if U.S. wages had kept up with productivity in the 1980's.

With privatization, retirees and workers no longer gain unambiguously when wages and productivity rise. In fact, workers could be torn between wanting sharp rises in share values even if they are fueled by deep wage cuts and employment.

2. WORKERS' ROLE IN PENSION REFORM: LESSONS FROM CHILE

After the Pinochet coup in 1973, the *junta* undertook a massive reevaluation of the social security system. Chile was the first country in Latin America to implement a PAYG comprehensive social insurance system. The system became very generous in the 1950s. It was inflation indexed and groups were made eligible for full benefits after having paid less than a full career of contributions. Diamond and Valdés-Prieto (1994) conclude that although the pension system “fell short of performing its insurance functions adequately, this does not mean that its finances were out of control.” It was in balance in 1976 and its ratio of workers to retirees was stabilized at about the average OECD ratio.

But, the system had low benefits and the values declined over time. The contribution rates

for pensions were high. In 1979, blue-collar workers paid 22.95% and white-collar workers paid 24.91% of payroll (Cheyre, 1988). In 1973, just before the coup, economists circulated a large report (called the *ladrillo*, “brick”) that suggested ways to fix problems of excessive rates and discrimination in benefits.

Often lost in discussing Chile’s reform are the enormous government outlays required in the transition. The Diamond-Valdés-Prieto (1994) study notes “a fiscal saving program was only feasible because the Chile of 1979-80 was under military control, with the military accessible to radical proposals from its economists.” The surplus in 1980 was necessary to pay for liabilities already accrued by people who would leave the system and to finance the tax cuts of 11% to induce people to leave the system. The Pinochet *junta* did not implement drastic bank reforms until the pension system was privatized. The intent was for the new system to buy the bonds of the rescued banks. The magnitude of the transition’s costs is such that it has called into question the reform’s net impact on savings (Holzmann, 1996).³

René Cortázar, labor secretary under the first democratically elected president, agrees that the old system had no political curbs on overspending for some groups and that populist tendencies in governments gave too much privilege to some interest groups — white collar workers, copper miners, etc., which violated horizontal equity (Cortázar, 1995). Cortázar emphasizes the economic benefits of reducing the political risk. He feels the current system is fairer because pensions no longer depend on particular issues of relative bargaining power. The other political risks avoided are, one, promising future benefits that the government system cannot afford and, two, the state using reserves in national budget politics. He laments that workers’ representatives were not consulted and have a limited role in the administration of the funds. This may be inefficient as well as politically unstable for reasons discussed in the last section.

In sum, in the early 1980s, the military government wanted to sell its state-owned industries, reduce government spending, lower labor costs for employers, and quell worker resistance. The new Chilean social security system that went into effect on Labor Day, May 1,

1981, substituted privately managed funds for the nation's Social Security system and helped effect these political goals. Chilean workers entering the labor force after 1983 were required to enter the individual privatized system, older workers could choose and were given a 17% pay raise if they joined the new system. The armed forces did not join the new system — they remained in their own PAYG plan.

Employers pay nothing. All Chilean workers (who report employment), after 1981, must contribute 10% of their income to an individual pension plan. Workers must also pay an additional 2.2% for administrative costs and an additional 0.8% for disability and survivor insurance for a total of 13%. Commissions out of taxable wages are around 3% — down from a high of 8.7% in 1984. Therefore, for every \$100 of wages, workers must pay approximately \$18 for pension administration expenses (Kay, 1999).

With these high fees, the profits of the private companies that administer the funds, the “*Administradoras de Fondos de Pensiones*” (AFPs), have been high, over 22% per year until 1994. Recently, the structure of the industry competition that relies on sales forces encouraging workers to switch funds is forcing up costs and imposing losses. In 1995, seven of the 15 AFPs reported losses. Profitability has since recovered, recording 17.5% and 20.5% in 1997 and 1998, respectively (SAFP, 1999).

Strict competition, theoretically, is the only regulating influence designed to keep these fees low, but after a wave of mergers in 1998, the four largest AFPs controlled 81% of the market (SAFP, 1999). One of the main incentives for competition in this industry should be the transfer of members between AFPs in response to higher returns and lower fees. Instead of forcing fees to fall, competition has increased costs as AFPs hire more sales staff to lure workers from fund to fund. Between 1992 and 1997, the number of sales persons leaped from 4,000 to over 18,000 (Kandell, 1997), with the ensuing increase in wage and salaries expenses. The driving forces behind the transfer industry have been “transfer wars” among the AFPs to gain market share and “bribes” offered by sales representatives (Quijano, 1998).

There has been considerable consolidation — in 1994 there were 21 AFPs; at the end of

1998 there were nine. Regulations prohibit the AFPs from branching to other services, yet, some AFPs such as Provida, Habitat, and Santa María, are establishing branches in Argentina, Peru, Bolivia, Colombia, and Costa Rica. The portfolios are very similar because AFPs must pay insurance in case they diverge from the average annual return. Therefore, returns, and products are similar. It was hoped that since the AFPs cannot compete on the basis of performance, they might have competed on the basis of fees, service, and education. But, advertising and foreign operations have become the AFPs major strategies to improve rates of return for the AFPs owners, not for the workers whose funds they manage. These are classic monopolistic competitive inefficiencies; barriers to entry are high, the products are similar, competition gives way to consolidation but competitors still must furiously advertise.

If union-based plans existed some of these problems could be tempered. First, unions could encourage groups of workers to join and bargain over fees. This would help minimize the now expensive way the system is regulated — through advertising and exit. Second, unions could subsidize information for low-income workers. The few Chilean union AFPs, Magister and Aporta, are indistinguishable from the other AFPs because groups cannot join an AFP. Unions have no comparative advantage in attracting (and keeping) members. Periodically, there are proposals in Congress to allow groups to negotiate fees and terms and conditions of entering and exiting an AFP, but the industry opposes them.

Though the owners of the AFPs suffered lackluster returns, the workers' funds managed by the AFPs fared worse in the mid- to late 1990s. Chilean funds earned, on average, 11.8% per annum in real terms between 1981 and 1997, but this return does not include administrative costs (Shah, 1997). These rates were unsustainable and are falling. In 1995, the rate of return was negative (-2.5%); performance in 1996 and 1997 was mediocre: 3.5% in 1996 and 4.7% in 1997. In 1998, pension funds lost an average of 1.1% (SAFP, 1999). Chilean workers could have earned more in bank savings deposits between 1995 and 1998 (Mark, 1996; Banco Central de Chile, 1997).

Among the worst problems are gaps in coverage. Almost 6 million workers (excluding the

military, which is 10% of the work force) had an AFP account in December 1998. But, over 2.6 million do not contribute because of unemployment, undeclared wages, and irregular work (SAFP, 1999). Also, in December 1995, over 35% of contributors had accumulated less than \$500 in their accounts (Shah, 1997). If the pension is not up to 75% of the poverty standard the government eventually has to pay the difference for contributors. Aporta, a bank worker union AFP, has the highest contribution rate (active contributors as a ratio of members) at 73%, while Magister (owned by the teachers' association) ranks fifth out of nine.

Unlike gaps in coverage, the potential liability to the government is not explicitly dealt with and recognized. The government guarantees a minimum pension to anyone who contributed 20 years. This guarantee means that a woman contributing all her life with a 1% annual real wage growth, a five-year break for child rearing, and retiring at the mandatory age of 60, would have to earn an estimated 7% (net) on her pension account to earn just as much as the minimum pension guarantees. In the absence of high returns, low-paid workers will likely fall back on the government welfare system (Barrientos and Firinguetti, 1995). This projected liability is not booked and it is likely to be larger if workers avoid working in the formal economy after 20 years because they will get no return from the contributions. Workers are guaranteed the same pensions without the extra contributions. This situation violates individual equity and efficiency. These were the stated most important goals for the reformers.

The AFPs also own the insurance companies that provide the disability and survivor insurance. The extent of cross ownership is undetermined. Anecdotes suggest it is significant. Julio Bustamante, the superintendent of pensions, in 1995 ordered greater transparency through the reporting of cross ownership, but no significant progress has been made. Just four funds own approximately 55% of all corporate bonds. In the U.S. and Europe, there are well-organized shareholder activists and corporate monitoring; there is no such organization in Chile. Union-controlled AFPs would presumably help make the ownership linkages transparent— making the system more politically stable.

In sum, the inherent inefficiencies of an individual-based system may doom the Chilean

economy. The system's administrative costs are large, people in like situations may have different pensions depending on market performance, over half of the population will need government subsidies to meet poverty standards, and private savings were not significantly increased by the system. These developments may disrupt capital markets. Workers face longevity risks, market risks, timing risks, and inflation risks (Turner and Watanabe, 1995). The only benefit agreed upon is that political risks are reduced. However, transparency of benefits may be replaced by the opaqueness of the implications for new corporate ownership.

3. ARGENTINE UNIONS AND MODIFYING THE CHILEAN PENSION MODEL

In March of 1991, Argentina enforced a stabilization program mainly based on U.S. dollar convertibility and elimination of the fiscal deficit. The PAYG Argentine social security system was near collapse when it was reformed in 1994 for two main reasons. The politicization of the system created pockets of privilege for some groups — very similar to the Chilean problem (and to some extent inevitable in all public schemes with a short contribution requirement). Some workers could get a very high replacement rate with very few years of contributions. Furthermore, as the Argentine population aged, the system became more expensive. Retirement values fell by half during the 1980s although the government promised some indexation. Court cases upheld the pensioners right to larger pensions but the government could not afford to pay them.

Despite this crisis, the Chilean model was not adopted. Pressure from the Labor Federation, the CGT, influenced the modification of the Chilean model. Many variants were debated. The reform eventually created a three-tiered system where people voluntarily chose the individual capitalization or the guaranteed state system. Under the capitalization system, the first tier is a small universal basic pension. The second tier consists of a workers capitalization plan (a defined contribution scheme). A third tier is the supplementary, voluntary, savings tier for workers who choose the individual accounts system. In Argentina, workers were offered a (dubious) government promise to pay current credits under the old system and there was no mechanism to

raise wages if one switched to the new system as was the case in Chile. During the first year, the new system was a bust. With pressure the state modified the rules so that workers once choosing the new system would still have a temporary option of switching back to the old system. Yet, in 1996, over half of workers were in the new system and voluntarily joined an “*Administradora de Fondos de Jubilaciones y Pensiones*” (AFJP). The contribution rate is 11%.

In Chile, the state is not allowed to administer any pension funds; however, in Argentina, the national bank owns an AFJP, Nación AFJP, that had 8% of the participants in 1998 (SAFJP, 1999). Nación AFJP guarantees a minimum return to its affiliates, albeit in pesos. The other major difference is that Argentine labor unions own a broad range of businesses including worker resorts and health care centers. Yet, at the end of 1998, only one AFJP (out of 15), Futura, is owned and controlled by the light and power workers, municipal employees and social security workers union. Another large union AFJP, the construction and sanitation workers’ Claridad, was acquired by the largest AFJP (Orígenes) in 1998⁴. Futura and Nación are among the few Argentine-based AFJPs. The four largest AFJPs (Consolidar, Máxima, Siembra, and Orígenes) account for 69% of assets and are majority owned by foreign financial firms — mostly Spanish and American and to a lesser extent, German and Italian. The fifth largest AFJP is 90% owned by the Bank of Boston (Salomon Smith Barney, 1998).

Just as in the Chilean case, the “transfer industry,” the amount of advertising and effort to encourage people to switch AFJPs, concerns regulators. The percentage of worker contributors changing AFJPs every year almost doubled in two years — increasing from 14.9% in 1995 to 28.9% in the year ending September 1997 (Quijano, 1998.) Like Chile, the portfolios of the AFJPs are highly regulated and become similar, as are the commissions. When contributors switch it is likely to be due to advertising rather than a significant difference between funds.

Argentina’s compliance rates are low and falling, as is the case in Chile. Of the over seven million workers affiliated with AFJPs at the end of December 1998, only 3.5 million contributed. The compliance rate varies by AFJP. The union-owned Futura AFJP has the second-to-the-highest ratio of workers paying on a current basis to those in the system (the contribution rate) at

57%. The largest AFJPs drive down the contribution rates — their average is only 49.3%. Argentina's rate started at 62%, while Chile's initial rates were around 75%.

The problem of increasing concentration and less vigorous competition will also occur in Argentina. The four largest AFJPs have 70% of affiliates; the first eight have 92%, while the remaining 8% is distributed among 7 AFJPs. From the 25 AFJPs at the start of the system, only 15 remain. Many forecast a continuation of mergers and takeovers. Again, like in Chile, there is no corporate monitoring; yet the problem is less severe since the holdings are, by far, in government debt and cash.

4. THE ROLE OF UNIONS IN PENSION PRIVATIZATION

Workers and unions in Argentina and Chile had very different roles in pension reform; the fact that the military imposed reform in Chile is not the main difference. Both nations are now democracies with very different labor movements. Yet, both the Argentine union AFJPs and their Chilean counterparts are losing active affiliates.

Privatizing pensions has greatly increased workers' exposure to risk and channeled billions of dollars into private hands. The need for joint management is particularly important since pension fund regulation is loosening significantly in Chile over time — and will likely do so in Argentina. Foreign issues were allowed in the portfolios for the first time in 1991 in Chile, but funds have yet to reach the 12% ceiling. There is pressure to allow more investment into infrastructure investing, equities, and public works financing.

The management of these savings and the uncertainty has led to other anxieties about a growing concentration of economic wealth and power. Since there is no data on cross shareholding we cannot analyze how the growth of the AFPs and AFJPs have affected the concentration of ownership and control in these nations.

The pre-1981 pension system in Chile was viewed as biased in favor of politically powerful groups and some deemed the system unaffordable. The 1981 pension reforms were meant to correct this. However, Chile has found that regulating workers' moneys flowing

monthly into the hands of private, global money-managers is expensive, can create islands of power and elite control, and is ripe for corruption (Paul, 1991).

Just as crucial, financial money managers may not have local economic regional development as an objective. Most of the AFJP and AFP investments are in government debt or corporate equities (Salomon Smith Barney, 1998). There are very little mortgages, real estate, local development, and venture capital. Some capital-worthy projects do not obtain credit because of asymmetric and imperfect information — barriers that also appear in developed nations. Though in Argentina and Chile there are very few economically targeted investments, we expect more in Argentina for two reasons. First, there is a stronger labor movement in Argentina. In 1990, 46.2% of the Argentine labor force was unionized (Lamadrid, 1990), compared to only 13.6% in Chile (Frías, 1993). International experience with union involvement in the management of pension funds in Denmark, the Netherlands, the U.S., the U.K., and Australia show that union-managed pension plans attempt to fill capital gaps and target economic development (Ghilarducci, 1995).

Second, there are union initiatives under way that address information problems. In February 1999, the Inter-American Development Bank (IDB) funded a joint Argentine/Chilean project to train union educators about pension funds and social insurance. These union educators will, in turn, train workers.

In all privatized pension systems in Latin America, much of the finance capital is owned by workers and controlled by others. In Argentina, the IDB and labor movement initiative could encourage more union involvement in pension management and policy reform. Chile's model — which spread — seemed to decidedly exclude unions by prohibiting groups of workers from negotiating terms and conditions of belonging to an AFP. Ironically, this exclusion appears to have been mistake — the labor movement didn't demand it. Involving unions could have alleviated some of the problems of individual capitalization schemes. Unions could reduce the transfer industry by sponsoring non-profit pension management firms and encouraging workers to stay with a fund as group. Furthermore, worker-directed pension funds could be used to

develop communities, create jobs, and enter into public-private partnerships for various domestic infrastructure projects. As workers own more companies through their pension plans, unions could help the public scrutinize and influence corporate policies (Ghilarducci *et. al.*, 1997).

In nations where unions are weak, pension systems are being evaluated in terms of only one of five social insurance goals — individual equity — and ignoring the other four — horizontal equity, redistribution, efficiency, social and economic stability (Reynaud, 1996).

5. SUMMARY

We have outlined the feared and hoped-for consequences of pension systems on capital markets and workers. There is the possibility that under privatized, individual-based pensions, the interests of the working class can be divided.

Marxist scholars have criticized PAYG systems because they redistribute payroll contributions between workers and do not fundamentally alter the balance of power between capital and labor (Katz Olson, 1982). Yet, in PAYG systems, retired workers are aligned with the interests of current workers because the strength of the pension depends on payroll growth and union political strength. Anti-Marxists in Chile praised the new system because of its anti-solidarity effects. Actually, it is José Piñera (1988) who explains the political economy purpose of the pension reform succinctly:

“The new system establishes a necessary connection between efforts and benefits. We do not harbor a single doubt that this capitalization system will benefit the silent majorities, which were systematically fooled by the PAYG system. The reform will have profound political consequences as well: a dramatic increase in individual freedom, which with the participation in social life and economic progress will constitute an insurmountable barrier against communism... establishing benefits proportional to effort, a huge source of state power and discretion disappears [...] Just as with the Labor Plan, we have the certainty of

giving another mortal blast to the politicization of social life and to Marxism, and particularly to poverty and injustice.” [Authors' translation]

This quote clearly emphasizes the reform’s purported advantages in promoting individual equity and avoiding the political risk that governments might default on pension promises. Just as clearly, Piñera (1988) argues that the reform’s goal was to neutralize class conflict.

Privatization creates winners and losers. The winners, when the private sector takes over a government function are, first and obviously, the vendors — the pension administration industry. Employers also gain because they are exempted from paying pensions. Nevertheless, employers lose long-term relationships with workers encouraged to accrue pension benefits. This may have detrimental consequences for the economy depending on the lost productivity effects of employers’ pension programs. Certain workers gain — those who do not live long, are savvy or lucky in investing and do not have dropout years when they are not contributing regularly in the formal sector. Losers include disabled workers, workers outside formal labor markets, and long lived. Women are likely losers because of culture, biology, and economics — they raise children, live longer, and are paid less (Barrientos and Firingueti, 1996; Arenas de Mesa and Bertranou, 1997).

High-income workers may have better investment advice and have longer careers. The state wins, at first, by leaving the pension “business.” However, if pensions are inadequate, the government, or, more accurately taxpayers, lose by paying more welfare benefits in the future. The state, also, incurs the expense of regulating and monitoring the “private” system for malfeasance and fraud. Unions may participate more, especially if legislation allows group affiliation. However union success will depend on whether unions in Argentina and Chile can organize more workers in an era of flexible labor arrangements and high unemployment. They also have to catch up and acquire professional financial management skills. Argentine union leaders may have a head start.

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NOTES

- ¹ See the discussion in Arellano (1980), and Diamond and Valdés-Prieto (1994) for the Chilean system.
- ² These arguments are supported by economists such as Boeker (1995), at the Inter-American Development Bank.
- ³ Reviewing empirical evidence from the start of the system until 1994, Holzmann (1996, pp. 31-32) concludes that “the empirical findings suggest that the direct contribution of financial market developments to private saving was negative.” He suggests a reverse causality, from growth and productivity increase to savings and from increased public savings to private savings.
- ⁴ Milk industry workers own 2% of Unidos AFJP. San José, under the control of the restaurant workers’ union and eight other unions, was reported to have sold 100% of its stock to Banco Hipotecario. The transaction was approved by the SAJP in September 1998 (SAFJP, 1999). Banco Hipotecario also has a 40% share in the holding that controls Prorenta AFJP (Bermudez, 1998).