

Chilean Pension Reform: Coverage Facts and Policy Alternatives

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Abstract

As opposed to defined benefit pension schemes, which are showing sustainability problems around the world, individual capitalization systems are seen as financially solvent. However, there has been some controversy during the last years with respect to this system's ability to provide adequate pensions. Nevertheless, in any contributory system, defined benefit or defined contribution, the performance of labor markets is crucial. The lack of contributions in the first case would imply financial problems (or exclusion) and lower pensions in the second. This article presents an analysis of how different variables affect the pension level in an individual capitalization scheme, assessing their relative importance. Then, individual level administrative data combined with survey information, is used to project pension benefits. The results show that a considerable percentage of the population would not be able to self-finance an old age pension higher than the level of the minimum pension guarantee, in expected terms. Moreover, most of them would not be entitled to get state funding to obtain a pension of that amount. However, the heterogeneity of individuals implies that there are very different situations and that not all of those who receive a low pension are vulnerable when old. There are cases in which individuals have other types of savings or, in the case of women; they might live of their husband's pension or widow pension benefit if diseased. Additionally, two possible reforms are explored, and their potential impact is evaluated—the default contribution for self-employed and the extension of the minimum pension guarantee for a broader range of contribution periods, not just 20 years.