Betting on the risks of the poor: The World Bank's approach to social security

The World Bank has demonstrated peculiar persistence in promoting privatized social security systems. Even when studies carried out by the Bank itself indicate that it is not possible to prove the success of these reforms, privatization policies for old age pension systems have been consistently implemented since the 1980s. This approach, currently labelled 'social risk management', claims to complement existing social protection systems. However the role of governments is limited to compensating for the market's failings.

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Since the 1980s, World Bank-driven structural reforms have systematically shifted the balance of social risk away from state institutions and onto the shoulders of the individual. For example, the World Bank's policy objective of prioritizing financial system restructuring and development has increasingly targeted the reform of public social security institutions, involving the privatization of old age pension systems. This significantly heightens the longevity risks faced by individuals, in particular by reducing the role of risk pooling and by making individuals increasingly responsible for having sufficient personal savings to cover consumption needs for the duration of retirement.

In 12 Latin American countries, beginning with Chile in 1981, purely defined-benefit, 'pay as you go' public pension systems – in which the pensions paid to the elderly are financed by contributions paid by current workers – have been substantially downsized, and mandatory individual savings accounts and voluntary pension plans have been added in a process known as the 'multi-pillar approach' to pension reform.

The single-mindedness of the World Bank in promoting privatized systems has been peculiar, since the evidence – including data in World Bank publications – has indicated that well-run public sector systems, like the social security system in the United States, are far more efficient than privatized systems. As a matter of fact, the extra administrative expenses of privatized systems comes directly out of the money that retirees would otherwise receive, lowering their retirement benefits by as much as one third, compared with a well-run public social security system.

The administrative expenses that are drained out of workers' savings in a privatized system are the fees and commissions of the financial industry, which explains its interest in promoting privatization in the United States and elsewhere. For instance, US firms like Merrill Lynch have been some of the biggest beneficiaries of social security privatization in developing nations such as Chile.

The World Bank has been quite successful in promoting this neoliberal approach in the field of social policy, thus entering a field of public action largely dominated until the mid-1990s by a UN specialized agency, the International Labour Organization (ILO). The opportunity was offered by the critical evaluation of the continuing universal appropriateness of ILO Convention 102 on minimum standards in social security, signed in 1952.

Specifically, conventional contributory approaches to social security provision, as defined by this Convention, are inherently unsatisfactory mechanisms for the financing and delivery of social protection to the large majority in the least-developed countries. In particular, low levels of population coverage – around 10% against 80% in industrialized countries – continue to undermine the legitimacy of mandatory contributory schemes. It is estimated that the problems of chronic poverty, and the insecurity which this brings, affect more than three quarters of the world's population who have no access to formal social security programmes, including more than one third of the world's population who currently remain without any form of social protection at all.

The attack on public social security

The World Bank's rapid displacement of the ILO from its traditional role as the institutional repository of knowledge in the field of social protection policy, and in particular old age pension provision, is actually rather ironic. It should not be overlooked that a contributory factor in the failure of conventional social security mechanisms to provide more adequate levels of coverage in the developing world has been the detrimental impact that the neoliberal-inspired, anti-state policy agendas of World Bank structural adjustment programmes (SAPs) have had upon levels of formal sector employment in adjusting and transition economies.

The World Bank's attack on public sector social security systems around the world has been both direct and indirect. The indirect attacks have been most important for industrialized countries like the United States. The World Bank has vigorously promoted the notion that social security systems, such as the one in the United States, are unsustainable. This was done most clearly in a decisive World Bank book on pension reform published in 1994, *Averting the Old Age Crisis*.[1] The title implies that longer life spans, due to increasing wealth and improved medical technology, are going to impose an unbearable burden on nations, unless their social security systems are radically altered.

This basic premise of the book has been widely criticized.[2] Life spans have been increasing rapidly in the industrialized nations for more than a century. In most industrialized countries – including the United States – the increase in spending on social security programs in the past 30 to 40 years was actually larger (measured relative to the size of the economy) than it is projected to be in the next 30 to 40 years. In other words, the World Bank could have more appropriately written *Averting the Old Age Crisis* in 1960 than in 1994.

The lack of evidence to support its basic premise has not prevented *Averting the Old Age Crisis* from being extremely useful to political groups with an interest in privatizing social security systems around the world. It is worth noting that Estelle James, who led the research team that authored *Averting the Old Age Crisis*, is now a member of George W. Bush's presidential commission for privatizing social security, although not in her capacity as a World Bank employee.

The World Bank's role in promoting the privatization and structural reforms of social security systems in the developing world has been far more direct. In addition to providing rhetorical support to the ideological and financial interests who advocate privatization, the World Bank has also provided loans and technical assistance to nations that have privatized their social security systems, particularly in Latin America and the Caribbean, and also later in Eastern European countries.[3]

However, in 1999 the first critical voices started emerging within the Bank concerning its ideological approach to structural reform of pension systems. In particular, the World Bank chief economist at the time, Joseph Stiglitz, sought to alter the Bank's single-minded support for privatized social security systems, co-authoring a paper which pointed out that many of the reasons given for preferring privatized social security systems are not supported by evidence. He openly encouraged the institution to rethink its approach on the subject

1 World Bank (1994). *Averting the Old Age Crisis: Policies to Protect the Old and Promote Growth.* Washington DC: Oxford University Press.

2 Baker, D. (2001). *The World Bank's Attack on Social Security.* Washington DC: Center for Economic and Policy Research.

3 See chapter about World Bank policies in Central-Eastern Europe developed by the BGRF and BEPA in this Report.

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by critically dismantling ten myths about social security systems.[4]

While acknowledging that the problems that had motivated pension reforms across the globe were real, Stiglitz noted that the arguments most frequently used to promote individual retirement accounts are often not substantiated in either theory or practice. The study therefore concluded that "policymakers must adopt a much more nuanced approach to pension reform than that offered by the common interpretation of *Averting the Old Age Crisis*." Furthermore, Stiglitz made it clear that the one-size-fits-all approach promoted by the Bank until then could not fit the very different contexts and situations in so many countries around the world.

The new 'social risk management'

In order to react to these criticisms and address concerns about the coverage limitations of formal and semi-formal contributory social protection systems, the World Bank conceptualized its new approach to social protection, the so-called social risk management (SRM) approach. In 2000, the World Bank's World Development Report presented its new policy framework for "attacking poverty" (which was also the title of the report). Significantly, at the time of the definition of the Millennium Development Goals[5] in the UN Millennium Declaration, the Bank clearly stated its intent to reconceptualize social policy as social risk management.

Framed conceptually using the common shared terminology of risk management and commercial insurance, and drawing upon assets-based approaches to welfare, the stated core policy goal of SRM is the alleviation of hard-core poverty through the better management of risks, defined in an inclusive sense to cover social, economic, political, environmental, labour market and non-labour market hazards or risk events.

Social risk management has been presented as having dual roles: protecting basic livelihood and promoting risk taking. As such, the SRM approach to social protection clearly differs from conventional social policy approaches, under which the rationale for social policy intervention is explained by issues as varied as market failure, solidarity and mutual obligation. In short, through emphasizing the double role of risk management instruments, SRM aims to empower the chronic poor with a greater ability to mitigate predicted labour market and non-labour market risks through increased access to a diversified range of assets, while simultaneously encouraging greater (entrepreneurial) risk-taking behaviour.

Once again, SRM aims at reducing the role of risk-pooling state provision while encouraging a greater role for private sector delivery of individual risk mitigating instruments. The significance of this element of the SRM approach is that, by prioritizing the private sector delivery of individual risk mitigating instruments, those individuals without sufficient financial means to purchase commercial insurance products are more likely to have to tolerate greater degrees of risk. Therefore the overall aim of the new approach is the lessening of risk, not the meeting of needs.

In general, the concern with the SRM approach, and in particular its explicit desire to further limit the scope of formal social security, is that a greater number of individuals are likely to become increasingly reliant upon public 'safety net' coping mechanisms, albeit complemented by additional informal, and potentially illegal, coping strategies. Surely, an effective system of social risk management should reduce the need for coping strategies, and not enhance it. Such a situation is clearly undesirable, and in fact runs contrary to the neoliberal mantra of increasing individual empowerment by reducing dependence on state institutions.

A similar degree of uncertainty remains with regards to the SRM expectation that asset ownership will encourage successful risk taking. Within the SRM framework, the assumption is made that if the poor could engage in riskier and thus potentially higher-return activities, then this would enable these individuals to graduate out of chronic poverty. Suggesting that the poorest, for lack of assets and social capital, shy away from "engaging in riskier but also higher return activities"[6] seems rather inappropriate and overgeneralized.

What is the state's role in fighting poverty then?

A key problem encountered in analyzing SRM lies with the difficulty in delimiting the parameters of state action. In general, and despite the stated intent of SRM to complement existing social protection systems, the 'repositioned' social protection role of government is presented in a somewhat prescriptive and limited fashion as a means only to compensate for market failure. For instance, Holzmann and Jørgensen[7] refer to the role of government as "providing risk management instruments where the private sector fails" or as "enacting income redistribution if market outcomes are considered unacceptable from a societal welfare point of view." However, the Bank's limited expectations regarding the desired role for governments in social protection provision is presented most clearly when they suggest that the state should provide "social safety nets for risk coping."

The emphasis placed by the Bank on coping strategies suggests that the SRM framework is built upon two premises. First, there is a premise that state institutions in developing countries will never be in a position to provide anything other than the most limited forms of social protection. Problematically, this perspective appears to deny the possibility of social progress. Second, the SRM framework appears to have been built upon the premise that developing countries should actively seek to implement social protection strategies which limit state action to the delivery of targeted social expenditure only.

These assumptions have serious implications for the most vulnerable groups in society. For the elderly poor, SRM may prove to be doubly problematic. On the one hand, poor elderly people, especially in the least-developed countries (LDCs), are progressively more likely to become marginal players in labour markets and household economies as they age. On the other hand, they are also progressively less likely to have access to 'assets' which can be used to mitigate against predicted or unpredicted risks. Accordingly, part of the solution to the problem of poor levels of social protection coverage for older people in the LDCs in particular must lie with the universal provision of tax-financed cash benefits – something which has been highly criticized by the Bank.

Providing for the elderly in developing countries should be seen as something of strategic importance within social and economic development programmes. It is increasingly recognized that older people have an important role to play within extended family groups in helping to reduce the destabilizing outcomes of increasing urbanization, labour force migration and, in Southern Africa in particular, the debilitating impacts of HIV/AIDS. This is because the family has traditionally been the most important, and sometimes only, social protection mechanism available to many people in the developing world. Therefore, providing older people with 'assets' in the form of cash benefits will guarantee that they have a continuing value as caregivers for family and community members.

Finally, it remains to be seen whether SRM approaches to social protection can provide a framework to lift people out of poverty in the longer term. From a conceptual perspective, the SRM framework relies too heavily upon the need for coping strategies for it to satisfactorily fulfil its self-proclaimed role in the management of social risk. For marginalized,

4 Orszag, P. (Sebago Associates, Inc.) and Stiglitz, J. (World Bank) (1999). "Rethinking Pension Reform: Ten Myths About Social Security Systems". Presented at the conference on "New Ideas about Old Age Security", 14-15 September. Washington DC: World Bank.

5 See details of the MDGs in Joyce Haarbrink's article in this Report.

6 Holzmann R. and Jørgensen S. (2000). "Social risk management: a new conceptual framework for social protection, and beyond". Social Protection Discussion Paper No. 0006. Washington DC: World Bank.

7 *Ibid.*

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poor older people, with no access to either labour market opportunities or alternative risk mitigating assets, the only feasible institutional mechanism for social protection remains the state. Therefore, the development of policies prioritizing a strategic role for tax-financed universal pension provision in LDCs would provide a more immediate mechanism to help mitigate life-cycle risks and to help lift older people out of poverty.[8]

The facts speak: the failure to extend pension coverage

Ten years after theorizing its extreme approach to pension reform in *Averting the Old Age Crisis*, the World Bank carried out a preliminary review of its experience in pension reform in Latin America, with some surprising findings.[9]

According to the Bank, Latin American governments that had undertaken structural overhauls to their national pension systems had improved their budget position, made public pensions more equitable, and encouraged savings and investment. But Guillermo Perry, World Bank chief economist for Latin America and the Caribbean, openly admitted that "...the failure to extend coverage to a broader segment of society makes it premature to call the reforms a success. Old age poverty remains a significant risk for the region's citizens."[10] Furthermore, the World Bank study pointed out that "more than half of all workers [are excluded] from even a semblance of a safety net during their old age."

In the specific case of Chile,[11] it was found that the investment accounts of retirees were much smaller than originally predicted – so low that 41% of those eligible to collect pensions continued to work. Voracious commissions and other administrative costs had swallowed up large shares of those accounts (up to 50%), and the transition costs of shifting to a privatized system were far higher than originally projected, in part because the government was obligated to provide subsidies for workers failing to accumulate enough money in their accounts to earn a minimum pension.

PRIVATIZING SOUTHERN EXTERNAL DEBT

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The external debt of many countries in the South, and notably some of the poorest in the world, has held back development, the fight against poverty and the financing of social security in those nations for more than 30 years.

Northern governments and international financial institutions like the World Bank and the International Monetary Fund (IMF), which are primarily responsible for this unsustainable situation, have repeatedly declared their willingness to free the poorest countries from the burden of this debt and the need to find a proper solution. Up until now, however, the declarations made and initiatives formulated, such as those arising from the G8 Summit in Gleneagles in 2005, have yielded poor results, if any.

Now the poor and highly indebted countries are facing a new threat, as they are obliged to deal with new creditors that pay even less attention to their needs and requests: private financial institutions.

In the last few years, an increasing part of the external debt owned by export credit agencies (ECAs), private banks and in some cases even Northern countries has been sold onto secondary financial markets, and is now controlled by highly speculative institutions such as private equity funds and hedge funds.

The mechanism by which this debt has flown from publicly controlled institutions like ECAs to speculative markets is called securitization, an instrument by which one financial institution sells risky credits at a discounted price to another financial company or to the secondary financial market.

After this process has taken place, it is now very difficult, and in some cases almost impossible, to know who controls a significant part of some of the poorest countries' external debt. As a result, any future initiatives undertaken at the international level to eliminate a part of this debt could be seriously thwarted by these new financial mechanisms.

Many countries in the South must now contend with this new threat to the fulfilment of fundamental social and human rights. The securitization and privatization of debt is just one of the financial mechanisms generating severely adverse impacts on the poorest inhabitants of the planet. There is an urgent need to draw up and enforce adequate national and international rules to regulate and control financial and economic powers, in order to bring them back to their original role: helping people to improve their lives, instead of seriously threatening them. ■

However, the Bank limited its self-criticism to the need to improve market-based mechanisms in order to fix outstanding problems in a privatized system, and in particular to pay more attention to ensuring that privately administered pension plans are efficient by offering affiliated workers and their families the best possible coverage at competitive prices. By doing this, the Bank avoided answering the original question which drove it into the social security reform business in the first place: the question of how to extend coverage to the elderly poor. Nevertheless, it finally recognized after a decade that governments should be paying much more attention to the poverty-prevention function of national pension systems.

The World Bank's controversial new health strategy

The SRM framework and its flawed assumptions are also at the heart of the World Bank's approach in the case of the 10-year Health, Nutrition and Population Strategy elaborated in 2006, which consequently presents an incorrect diagnosis and therefore an incorrect prescription for reform.[12]

Once again – as in the case of social security policy and the ILO – the Bank cooperated very little with the World Health Organization (WHO) and neglected most of the research, policy advice and technical assistance already offered by this institution to developing countries' governments. The biased selection of research and analysis that underpins the proposed new health strategy is moving the Bank to further exacerbate existing shortages of health workers, to further undermine public health systems, particularly in low-income countries, and to entrench two-tiered systems where the poor will continue to be denied access.

8 McKinnon, R. (2004). "Social risk management and the World Bank: resetting the 'standards' for social security?", Journal of Risk Research 7 (3), April. Carfax Publishing.

9 Gill, I., Packard, T. and Yermo, J. (2004). *Keeping the Promise of Social Security in Latin America*. World Bank and Stanford University Press.

10 World Bank (2004). "Keeping the Promise of Old Age Income Security in Latin America". Press release, 13 December. Available from: <wbln1018.worldbank.org/LAC/LAC.nsf/PrintView2ndLanguage/146EBBA3371508E785256CBB005C29B4?Opendocument>.

11 Anrig Jr., G. and Wasow, B. (2004). "Twelve Reasons Why Privatising Social Security is a Bad Idea". The Century Foundation.

12 Oxfam Great Britain (2007). "World Bank Health Strategy and the Need for More Balanced Research and Analysis Across the Bank". Briefing prepared by Oxfam for Civil Society Organizations. EU World Bank Executive Directors meeting, Brussels, 6 February.

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The analysis that has been done by Bank staff for the new health strategy assumes that existing levels of out-of-pocket payment are an indication of ability and willingness to pay for services. This is despite research quoted in the very same document which demonstrates that these existing payments have driven millions of marginalized people into deep poverty.

The analysis further proposes an increase in the contracting-out of health services to the private sector and the promotion of social insurance systems. This diagnosis takes the current situation as a given for the future and does not look for ways to improve public system capacity. For example, it does not address the acute shortage of health workers overall – according to WHO, 4.2 million more physicians, nurses and support workers are needed around the world. Nor does it address public sector capacity to coordinate, regulate, and harmonize sustainable and robust health care systems. By doing this, the Bank approach ignores a large, if not overwhelming, body of evidence that low-income countries with weak state capacity are not able to effectively regulate and incentivize private health providers to offer equitable access to services for all. Instead, they need precisely the opposite approach: increased investment in public institutions which provide services directly, financed from national revenue. This is in fact the only way that countries – including developed countries – have succeeded in providing health services based on need rather than ability to pay.

Apparently, such ideological bias in World Bank research is not the exception. A recent independent audit of World Bank research, which examined over 4,000 World Bank activities between 1998 and 2005, found that rather than policy being formulated on the basis of a balanced analysis of a wide range of research, policies were often formulated on the basis of historical preference, and then backed up by selective research and biased analysis.[13]

The panel that carried out the evaluation, made up of distinguished academic figures, had substantial criticisms of the way that World Bank research was used to proselytize on behalf of World Bank policy, often without taking a balanced view of the evidence, to the point that "the degree of self-reference rises almost to the level of parody." These conclusions are also supported by recent research commissioned by the Norwegian government regarding World Bank and International Monetary Fund (IMF) economic policy conditionality: "The most serious weakness of the IFI [international financial institution] reports is their quite narrow methodological and disciplinary starting points."[14]

The assumptions behind the SRM approach are also at the core of the market-based solutions advanced by the Bank to extend access to social protection in the health sector. In particular, the Bank proposes systematizing existing levels of payments into formal, insurance-based systems. In low-income countries where the majority of the population lives on less than USD 2 a day, there is no evidence that this approach helps to build equitable health systems. On the contrary, there is evidence that publicly financed systems are better able to provide universal, equitable access to services in low-income situations.

By choosing this questionable solution, the Bank once again deliberately reduces the role of the state and public intervention on the basis of the ideological and unproven assumption that private health providers are more accountable, of higher quality and more efficient than public providers. Public sector workers are presented as corrupt, with no analysis of why corruption thus defined occurs among this group, and no comparative analysis of how and why massive corruption also occurs in private provider contracts. The Bank's strategy ignores the evidence of successful reforms to strengthen the training, recruitment and retention of more highly motivated and better-compensated public sector health care workers, and proposes only to bypass the public sector in favour of a falsely valorized private sector. In promoting private service provision, the strategy is practically promoting internal migration from the public to the private sector and therefore further fragmentation of public health systems.

Undue constraints on fiscal space for health and social policies

It should be noted that the new health strategy aims only to advise low-income countries on reforms within their fiscal and absorptive capacity constraints. The World Bank should, instead, aim to assist recipient countries to overcome those constraints, rather than viewing them as a given. In particular, the Bank should not push low-income countries to be "selective and realistic" about which results they can achieve in this field, but should, on the contrary, help these countries to deliver a comprehensive package of health services to the whole population. In this regard, the strategy fails to acknowledge the impact of IMF policies on countries' ability to adequately address their human resource crisis and provide universal access to quality health care for all.

In July 2007 the Centre for Global Development's working group examining the IMF and health spending – which was chaired by ex-IMF staffer David Goldsbrough and included officials, academics and representatives of civil society – found that the Fund has unduly constrained countries' policy choices. The group analysed in detail the specific cases of Mozambique, Rwanda and Zambia and concluded that "IMF-supported fiscal programs have often been too conservative or risk-averse. In many cases, they have unduly narrowed policy space by not investigating sufficiently more ambitious, but still potentially feasible, fiscal options for higher spending and aid."[15] The working group advanced a series of recommendations to international financial institutions, including the need to help countries explore a broader range of options for the fiscal deficit and public spending and to drop wage bill ceilings from nearly all social programmes.

An individual fight against poverty?

The element of the SRM framework aimed at refocusing social policy towards encouraging individual risk taking is potentially problematic in a more general sense. On the one hand, the failure of conventional approaches to public social policy to satisfactorily reduce poverty in developing countries and, on the other hand, their much debated contribution, predominantly through labour-market distortions, to the creation of a welfare-dependent underclass in developed economies, are often portrayed as being indicative of 'state failure'. Following this approach to the problem, it must be assumed, therefore, that the stress placed by SRM upon the need for an increasingly proactive and inherently risky role for the individual in a personalized fight against poverty will permit poverty to be increasingly defined, from a neoliberal perspective at least, as 'individual failure'.

Consequently, in some cases the SRM approach to social protection may actually contribute further to the social and economic exclusion of the poor, and those individuals who remain in poverty, for whatever reason, are likely to face a greater degree of stigmatization to the point of being seen as living in a "pathological condition."[16] Accordingly, with the possible exception of the truly indigent, the chronic poor may come to be regarded as not only undeserving but beyond help. Such an unacceptable view structurally undermines the belief that social protection is a fundamental right of all citizens.

Given that riskier activities, by definition, promise the potential of higher returns when successful and also the likelihood of severe, and potentially catastrophic, losses when they fail, in principle it may be deemed inappropriate for an international organization such as the World Bank to encourage individuals to engage in activities which hold the inherent potential for encountering such losses.[17] ■

13 Banerjee, A. *et al* (2006). "An Evaluation of World Bank Research, 1998-2005".

14 Norwegian Ministry of Foreign Affairs (2006). "The World Bank's and the IMF's use of Conditionality to Encourage Privatization and Liberalization: Current Issues and Practices".

15 Center for Global Development (2007). "Does the IMF Constrain Health Spending in Poor Countries? Evidence and an Agenda for Action". Report of the Working Group on IMF Programs and Health Spending.

16 Vilas, C. (1996). "Neoliberal social policy: managing poverty (somehow)". *NACLA Report on the Americas*, Vol. 29, No. 6.

17 See footnote 10.

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