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Government Hopes Overhaul of Social Security System will Encourage Savings

by LADB Staff

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In early November, President Ernesto Zedillo's administration announced a massive overhaul of the country's social security system. The changes attempt primarily to encourage increased domestic savings, but also propose changes in the structure of the social security institute (Instituto Mexicano del Seguro Social, IMSS) to encourage efficiency and to improve the level of medical service provided to members.

In a press conference explaining the changes, Zedillo said the overhaul of the IMSS was necessary to prevent the collapse of the system. In addition, he said the changes provided his government with the opportunity to create a more equitable and efficient pension system for Mexicans. "We will strengthen the system to provide increased protection, offer greater coverage, and improve the quality of services," Zedillo said. Among the changes proposed by the Zedillo administration is the creation of a program that gives private citizens the choice of remaining with the current IMSS pension program or to create individual retirement accounts.

The President suggested that given more choices, workers are likely to set aside money for retirement. The new pool of money, said Zedillo, will be used to replace some of the short-term foreign capital that has left Mexico due to the devaluation of the peso in January of 1994. According to some estimates, foreigners have withdrawn about US\$30 billion in capital from Mexico. "More domestic savings will mean more investment and more growth," Zedillo said in a press conference explaining the changes. "That economic growth, in turn, will create more jobs, which would translate to more security for our society.

Indeed the past, many economists have criticized Mexico for focusing too much on attracting foreign capital to fuel the economy instead of promoting a pool of domestic savings. In recent years, Mexico's domestic savings rate has fallen from 22% of GDP in 1988 to less than 16% of GDP in 1995. According to the daily newspaper Excelsior, the Zedillo administration's objective is to boost Mexico's domestic savings rate to 24% of GDP by the year 2000. "You will not see much difference in the first year, said one official familiar with the plan. "But in two or three years you will see a major increase in the amount of savings."

In his speech, Zedillo emphasized that 30% and 40% of the new funds obtained from the retirement and disability pension contributions will be used to provide business loans, especially to small- and medium-sized enterprises. Companies of all sizes with strong possibilities of success in the areas of construction, infrastructure, and technology will also receive preference for loans from this new pool of money. Under the proposal, the federal government would assume 7.143% of the business sector's total annual contributions to the system. To meet this commitment, Zedillo said his administration has pledged annual appropriations of more than 3.6 billion nuevo pesos (US\$482

million) to various retirement programs. Each participant in the new program would also make daily contributions of one nuevo peso (US\$0.13 cents).

One of the features of the plan proposed by the Zedillo administration is to provide workers with the choice of remaining in the existing retirement system or to open individual retirement accounts. The individual accounts would be structured to offer a higher return than the existing system, which in theory would encourage workers to save more. According to the Mexico City daily newspaper *Excelsior*, the individual retirement accounts could attract a percentage of the workers who are not currently in the formal economy and who currently do not save any money for retirement. A rough estimate released recently by the Zedillo administration is that as much as 50% of Mexico's economically active population (EAP) of 36 million persons is part of the informal economy.

Among other changes, Zedillo's plan proposes to broaden medical coverage and reduce costs of medical care. The IMSS system currently covers 39 million Mexicans with salaried jobs. The changes propose to extend at least some coverage to 53 million other Mexicans who are self-employed or part of the informal economy. Additionally, participants who receive medical coverage under the IMSS will now receive the choice of continuing in IMSS-run clinics or to select their own doctors at health maintenance organizations. The proposal to restructure the IMSS has received endorsements by business and union leaders, but has been strongly opposed by IMSS employees, who fear the legislation will lead to a comprehensive downsizing of the IMSS system.

In addition to managing retirement funds, the IMSS includes nearly all of Mexico's clinics and hospitals, 155 day-care centers, 38 theaters, 149 discount stores, four recreation resorts and 16 funeral parlors. Indeed, according to some economists, Zedillo's proposal would in effect end subsidies for the money-losing operation of the system, such as the theaters and the day-care centers. The IMSS employees, aware that the Zedillo administration is adamant about enacting the IMSS restructuring, are instead focusing on attempting to influence Congress.

The Chamber of Deputies must still approve Zedillo's proposed changes to 26 articles in Mexico's social security legislation. In their arguments to Mexican legislators, the IMSS employees suggest that transferring management of the national pension fund to private parties could create corruption. "We believe with all certainty that if legislators authorize these initiatives, inefficiency and ineptitude will be rewarded," the workers said in advertisements placed in several newspapers in Mexico City. "That will have negative repercussions for most Mexicans."

On the other hand, economists from Grupo Financiero Banacci suggest that private managers of the pension funds, would have to adhere to strict regulations and restrictions. Indeed, the government is expected to turn over the administration of the pension funds only to investment societies that specialize in investment of retirement funds. Most of the retirement money is expected to be placed in "safe investments," such as municipal bonds and other government- issued securities.

However, the fund managers will be given the flexibility to invest up to 15% of the pool of retirement funds stocks and other high-yielding instruments, as long as these are "qualified" investments that do not surpass a certain "risk" rating. IMSS secretary general Juan Moises Calleja told reporters that the proposed changes will protect retirement funds against any future economic crisis in Mexico,

especially the "impact of inflation and devaluations." [Note: Peso-dollar conversions in this article are based on the Interbank rate in effect on Nov. 7, reported at 7.47 nuevo pesos per US\$1.00] (Sources: New York Times, Notimex, 11/02/95; Excelsior, La Jornada, 11/02/95, 11/03/95; Reforma, 11/02/95, 11/06/95; El Diario de Yucatan, 11/06/95)

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