



AN OPPORTUNITY LOST

Pensions, the amendment that never was

JULY, 2021

SIGNOS VITALES
EL PULSO DE MÉXICO

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SUMMARY

The Social Security and Retirement Savings laws amendments are filled with chiaroscuro. They tackle relevant issues like the replacement rate, the high contribution weeks, and the high commissions charged by the administrators; nevertheless, it leaves aside issues of greater significance like labor informality, the care system (linked primarily to women) and, the access to public health.

The law's amendments only strengthen the labor market duality in Mexico (formal and informal). In the best-case scenario, the amendments will manage the evil better (which will still be present), but they are not designed to fill Mexico's economic and social gaps. From a macroeconomic view, it must be stressed that resources from the economy will be reassigned and will raise the weight of the pensions in the Mexican financial system.

THE CONTEXT

On July 22nd, 2020, the federal executive announced the amendment proposal of the Social Security and Retirement Savings laws (SHCP, The Secretariat of Finance and Public Credit for its acronym in Spanish, 2020). Such a proposal was approved by congress months later. The aforementioned laws amendments were published in the Official Journal of the Federation by December 16th, 2020 (DOF, for its acronym in Spanish, 2020).

Said amendments were given in the middle of the sanitary crisis, the first Afore generation (GA, for its acronym in Spanish), which is about to be retired. In a time where Mexico is going through the worst economic crisis in recent history. The amendments to the corresponding laws were approved without setbacks (like many others). At least two reasons enabled their approval: (i) the federal executive has the majority in congress, which allows him to perform modifications as needed; and (ii) the current regulatory framework requires an urgent reform.

A broad consensus among specialists exists pertaining to the urgency to perform adjustments to the regulatory framework since it is of vital significance in the improvement of people's quality of life; however, the reach of the adjustments is far away from the desired goal, improve people's quality of life and, in particular the underprivileged.

A profound amendment poses several challenges for it to have the desired results. I.e., in Mexico, labor status (formal and informal) greatly determines ac-

cess to social security conditions, like health care, nurseries, unemployment benefits and (under certain conditions) pension. Likewise, the labor market in the different country regions have their peculiarities, and much more so when we are talking about labor conditions by sex.



Imagen: Tasa de informalidad en *La voz de Jalisco* en: <https://tinyurl.com/tfhzupf>

The idea is simple, informality leaves you out of the social protection system in Mexico, with all of its weaknesses, but sex and the region you are born to fertilize the differences. Moreover, the amendments to the aforementioned laws perpetuate said conditions.

LABOR CONDITIONS IN MEXICO

According to ENOE (the National Survey on Occupation and Employment for its acronym in Spanish), by the fourth quarter of 2020, only 38.7% of the employed population in Mexico (20.61 million people) had access to health institutions (private or public). This access implies that 61 out of every 100 employed people in the Mexican economy lack this benefit.

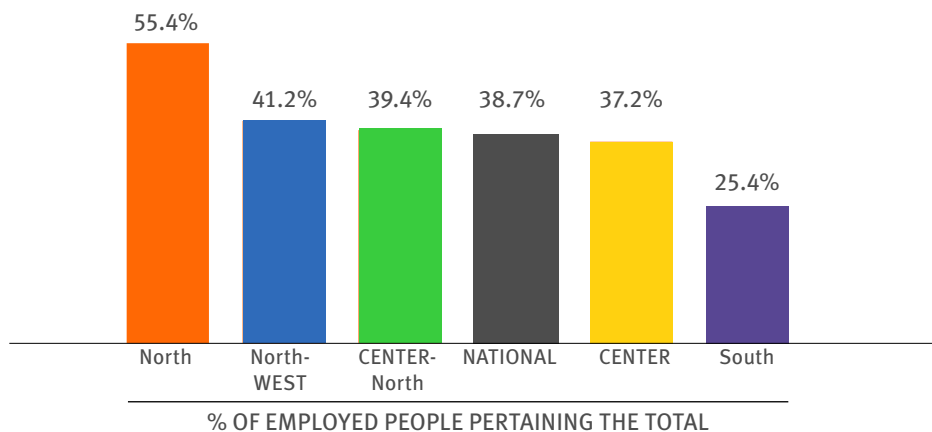
Out of 20.61 million Jobs, 63.1% are condensed in the northern and central regions, while the country's South only clusters 14.7% of the previously mentioned jobs. While in the country's northern region, 55 out of 100 employed people have access to health services, in the south of the country, only 25 out of 100 people are in the same condition.

For the regionalization, the Centro de Estudios Espinosa Yglesias classification is used (Ceey, Espinosa Yglesias Study Center, for its acronym in Spanish)¹.

39.7% of employment coupled with health services in the south of the country is dependent on only three economic activities: educational services, health services, and social assistance and, government activities. The cases of Chiapas, Oaxaca and, Guerrero (the entities with the higher level of poverty in the

¹ North: Baja California, Sonora, Chihuahua, Coahuila, Nuevo León and Tamaulipas;
Northwest: Baja California Sur, Sinaloa, Nayarit, Durango and Zacatecas;
Center-North: Jalisco, Aguascalientes, Colima, Michoacán and San Luis Potosí;
Center: Guanajuato, Querétaro, Hidalgo, Mexico state, Morelos, Tlaxcala, Mexico City and Puebla;
South: Guerrero, Oaxaca, Chiapas, Veracruz, Tabasco, Campeche, Yucatán and Quintana Roo.

GRAPH 1. EMPLOYED POPULATION WITH ACCESS TO HEALTH INSTITUTIONS PER REGION OF THE COUNTRY (%)



Source: In-house elaboration with data from the fourth quarter of 2020 of ENOE.

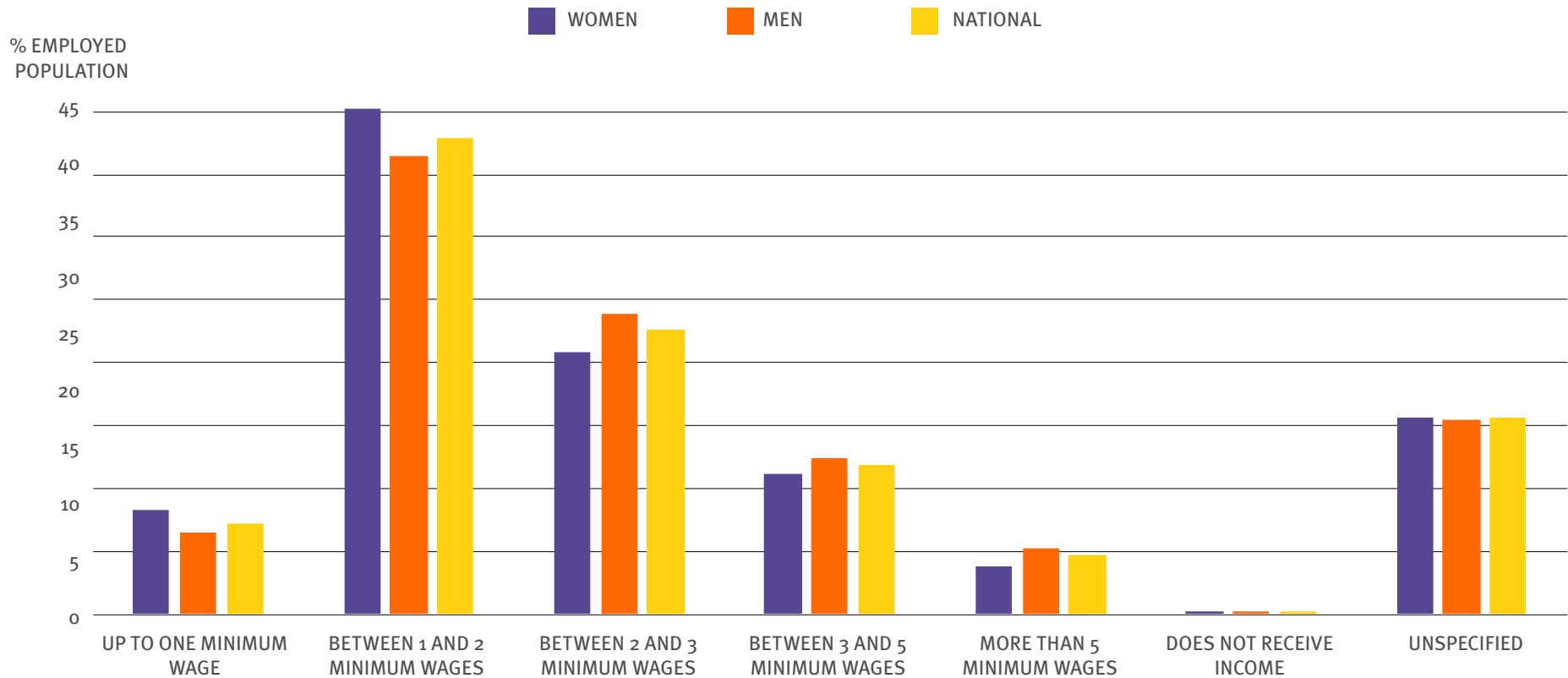
country) are highlighted, which reliance on the aforementioned activities is at least half of the employment with such benefit (52.5%, 51.9% and, 49.9% respectively).

In the north of the country said activities only add 18.2% of the employments with that benefit, in contrast to the secondary level of the economy (transformation) which adds 42.5%. Nationally 26.9% of employed people with access to health services are employed in the three aforementioned activities.

In turn, 6 out of 10 employments in the country with health benefits are given to men. Albeit, pertaining to the employed population, 40 out of 100 women have

the benefit compared to 38 out of 100 men in the country. The northern and southern contrast is noted among women, too; 57 out of 100 women working in the North have access to health institutions, while, in the southern region, only 27 out of 100.

GRAPH 2. PERCENTAGE OF EMPLOYED POPULATION WITH ACCESS TO HEALTH SERVICES BY INCOME LEVEL AND SEX, FOURTH QUARTER 2020



Source: In-house elaboration with information from ENOE, 2020.

In the last quarter of 2020, 45.1% of the employed population with access to health services in the country disclosed having incomes of up to 2 minimum wages. In the case of women, said ratio is 48.5% of the total employed population and in the case of men is 42.9%. Only 4.7% of the national population (936.6 thousand people) with the same benefit has more than five minimum wages.

The job insecurity conditions in which most of the Mexican population is found are not the result of the current sanitary crisis in spite of its havoc (which there is, as previously pointed out in the last Vital Signals report), but they have primarily been a part of a constant erosion process in the Mexican labor conditions.

Based on ENOE's data, we know that between the last quarter of 2005 and 2020, only three regions have increased employment with health benefits, regarding the employed population total: North, Northwest, and central-North, but labor conditions in the center and south of the country have been going towards the detriment to the workers.

As is pointed by Acción Ciudadana Frente a la Pobreza (Citizen Action Facing Poverty, 2020):

for years and decades labor conditions detriment has risen, wages lost value, pseudo lawful measures and practices to avoid social security and permanent recruitment multiplied and, the means to prevent an authentic union organization with the appropriate collective wage negotiation and working conditions. There are structures in the world of employment that are poverty factories (p.4).

According to the same organization, 78% of the population was not found in dignified working conditions by the last quarter of 2019, 51% did not have a

stable contract. In brief, the employed population with adequate social benefits is minimal (4 out of 10), and from this population, only a tiny percentage has dignified working conditions (22%).

THE ROAD TOWARDS THE PENSION

For the purpose of counting with the Mexican Pension system, it is vital to access formal employment (being enrolled in the Social Security Mexican Institute) and fulfill two requirements: a minimum of contributed weeks (1,250 weeks before the amendment to the aforementioned laws) and having 65 years of age. That is to say, in Mexico, access to health services and a pension by the end of the working life is determined to the access to formal employment during a set timeframe; otherwise, employees are excluded from the social protection system.

According to the Labor Market Trajectories Module (2015) from INEGI (The National Institute of Statistics and Geography, for its acronym in Spanish), only 39.9% of people between 18 and 54 years of age in Mexico have had access to social security during their whole working trajectory. While 41.5% of the previously mentioned group never had access to a social security institution. Meaning, at least 42 of every 100 Mexicans are not candidates to be a part of the social security system.

Thus, it is equal to the timeframe people are employed in the formal labor market about their whole working trajectory (Contribution Density) than the very

own pension system. Contribution density (DC, for its acronym in Spanish)² is 42.9% in Mexico, but men have a DC of 53.7% compared to 46.1% of women.³

The aforementioned implies that Mexican starting their working life traverse between informal and formal employment and that women stay the longest in the path of informal employment. While they stay in informality (almost 54% of the time), they do not increase their savings on retirement accounts (registered or assigned) despite the added value to the economy.

It bears mentioning that while the employees contribute, they add to their retirement savings account, otherwise known as contributory pensions. The sum of the savings plus the interest generated (minus the commissions charged by the banks) on the accounts of each employee is the amount they withdraw at the end of their working life.

To scope the severity of the situation, let us suppose the case of a person that started his working life at 25 years old, and so far, has worked for 40 years (65 years of age). The 1,250 weeks requirement implies that 60% of its working trajectory (1250 contributing weeks/2080 working weeks) has been employed in the formal employment market (roughly 24 of 40 years). Hence, with the current DC a great deal of Mexicans will not have access to a pension.

² It was calculated as the ratio of the contributed time to the Retirement Saving System (SAR, for its acronym in Spanish) between the total time in the labor market.

³ All employees affiliated with the Mexican Institute of Social Security (IMSS, for its acronym in Spanish) contribute to the SAR. However, two subsets are differentiated: registered employees (those who signed a contract with an Afore, so it manages their resources); and assigned employees (those who never entered an agreement to select an Afore are assigned to an administrator or service provider).

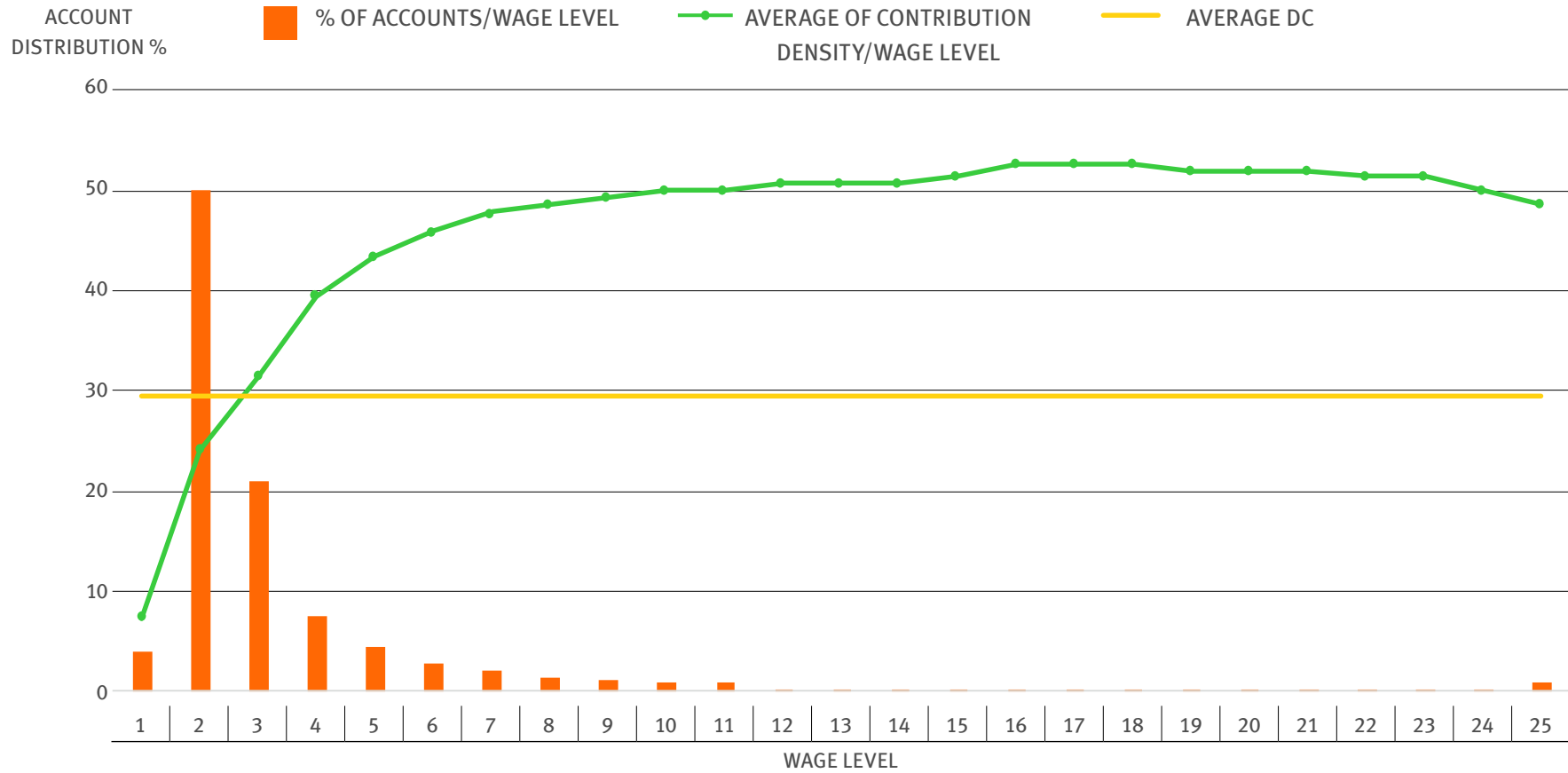
Likewise, employees with incomes up to 3 UMA (Update and Measure Unit, for its acronym in Spanish) focus 75% of the GA accounts. At these income levels is the lowest DC. Only the employees with incomes of 2 UMA focus roughly 50% of accounts, but their DC is 36% on average. Just 25% of the population (4 UMA ahead) has a DC between 59% and 79%; this implies that, on average, those with a higher probability of success to access a pension have equal or higher income to 10,897.8 pesos a month.⁴

In other words, –keeping everything else constant– the people with incomes of 2 UMA –which have a 36% DC– on average will have to labor for 3472.2 weeks in their work-life (66.8 years) to comply with 1,250 weeks of contribution. Assuming they started their work-life at 20 years old, they could access a pension by the time they are, on average, 87 years old.

Mexican starting their working life traverse between informal and formal employment; women stay the longest in the path of informal employment and cannot increase their savings on retirement accounts.

⁴ The UMA value is 89.62 pesos to date during 2021. The monthly value is calculated by multiplying the daily rate by 30.4. For the annual calculation, the previously mentioned is multiplied by 12.

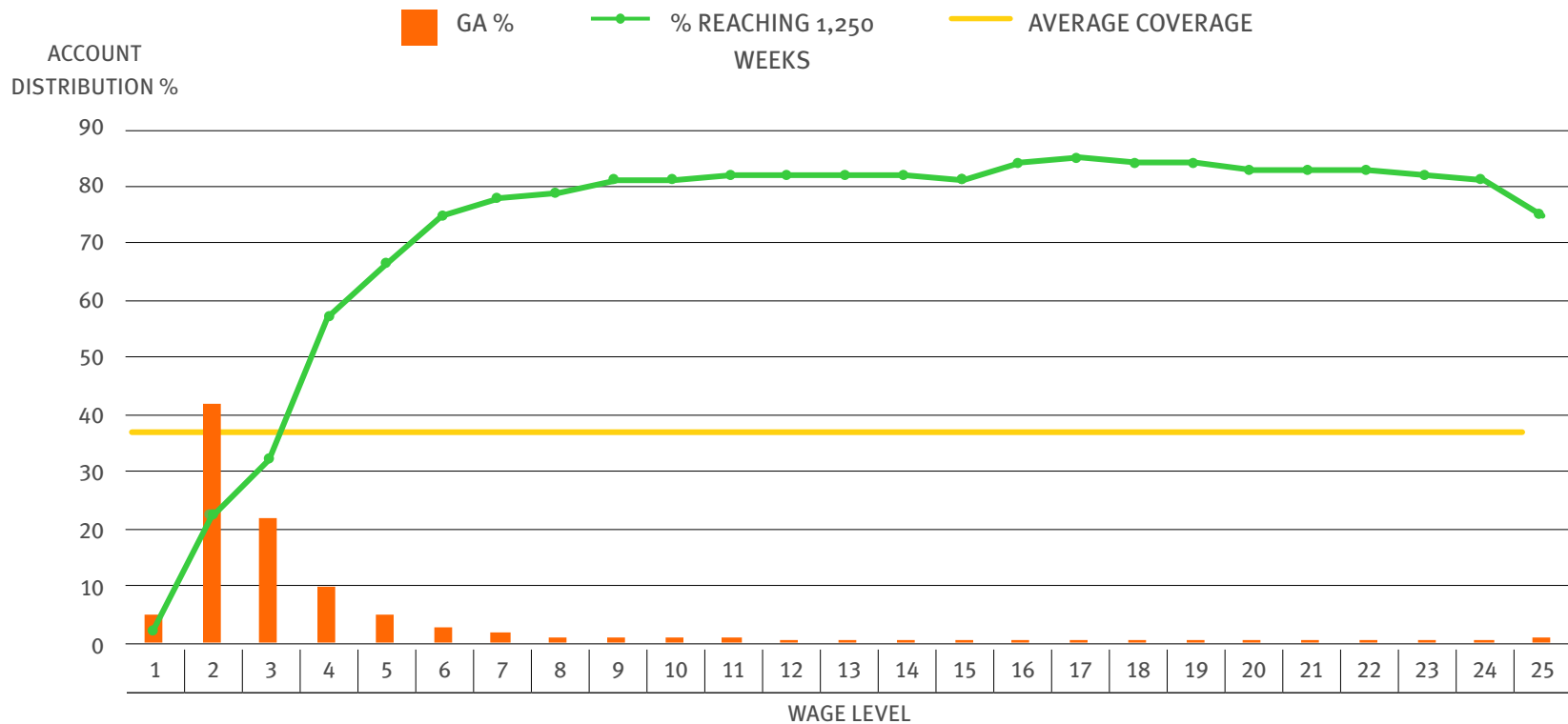
**GRAPH 3. CONTRIBUTION DENSITY AND ACCOUNT DISTRIBUTION OF SAR ACCOUNTS
PER WAGE LEVEL, 2018**



Source: CONSAR. (2018). Wage level “1” corresponds to an SM. For higher than 1 level, it refers to the amount of UMA times.

According to the National Commission for Retirement Savings (CON SAR, for its acronym in Spanish) information, only 24% of employees that are part of the GA will be in condition to fulfill the contribution time required by law, which enables them to access a pension by turning 65 years old. The rest of the population (76%) would be left without a pension (will receive a Denial of Pension).

GRAPH 4. PENSION COVERAGE AND SAR ACCOUNT PERCENTUAL STRUCTURE OF REGISTERED EMPLOYEES THAT WILL REACH A PENSION, 2018



Source: CON SAR. (2018). Wage level “1” corresponds to an SM; for higher than 1 level, it refers to the amount of UMA times.



Likewise, from the total registered workers, 43% of men will comply with the 1,250 contribution weeks required by law; conversely, 30% of women will have access to a pension. This information clarifies the notable differences between men and women and income level since barely 2% of employees that receive minimum wage (SM, for its acronym in Spanish) will have the right to a pension. At least 75% of employees with incomes equal to or higher than six UMA will have access to the same right.

The reduced DC explains that only 22% of the employees with two UMA wages (where the bulk of the population is found) may Access a pension by the end of their working trajectory. Meaning, regardless of the time people work, the possibility to have access to social security in Mexico is minimal.

OFFICIAL DIAGNOSIS

The amendments made to the Social Security and Retirement Savings laws approved by congress come from three assumptions, which provide a glimpse of the main issues to tumble:

1. Low replacement rates⁵
2. A high number of contribution weeks
3. Elevated commissions charged by Afores

On the other hand, the tripartite nature of contributions is recognized: employee, employer and, government. Furthermore, this identifies the aimed population of the aforementioned policy, hoping it is more progressive than the previous one; that is, it expects that the lowest incomes are the most benefitted, at least from the federal executive's perspective.

For the purpose to improve retirement conditions of the workers, the following is propound:

1. Reduction of contribution weeks. The weeks change from 1,250 to 750 to gradually increase –within ten years– to up to 1,000 weeks of contributions.
2. Commissions charged by afores will be decreased from .9% to .7%—a 22.2% reduction.

⁵ Represented percentage of the worker's pension pertaining to the income received before retirement.

3. Increase employer contributions to pensions from 5.15% to 13.87% within an 8-year timeframe. The contributions will result in a 15% by adding the employee contribution (which remains the same).
4. The Minimum Guaranteed Pension (PMG, for its acronym in Spanish) goes from 3,289 to 4,345 Mexican pesos, on average.
5. Government contributions are focused on those workers which wage range from one to four SM.

IMPLICATIONS OF THE MEASURE

As shown, 6 out of 10 employed Mexicans in the Mexican economy do not have health services and will not have the right to a pension as a contribution to their work. Their working condition (Informal) excludes them. The differences among men and women and between regions are evident, even between the same sexes by region. The bulk of the aforementioned population (around 45 of each 100) obtains from their work up to 2 SM. The vast majority of them cannot reach a DC (about 60%) that ensures access to a pension by the end of their working trajectory.

In principle, the law's amendments are aimed at 4 out of 10 working-age Mexicans, meaning, the other 6 out of 10 are still left out of access to a pension as well as other benefits as a fruit of their labor, within them access to health institutions and unemployment insurance. Hence the policy is only aimed at employees contributing to IMSS through the private industry (20 million by March

2021). Yet, from this universe, 14 million are the aim of the proposal due to the amendments to the regulatory framework on the law that came into effect in the middle of 1997.⁶

Thereupon, taking into account the gaged employees that will receive a denial of pension from the CONSAR (76%). We know that without the amendments to the regulatory framework, approximately 10.6 million people –that partook in the formal work market– will not receive a pension and could only withdraw the accrued balance on their savings account. The situation is overly critical.

By reducing the contribution weeks, a lower DC is required to reach a pension. According to specialists in the field, with the new pension regime, around 1.7 million workers will be favored from such reduction (Levy, 2020). But in spite of those 8.9 million employees (10.6 – 1.7) still will not have the right to a pension. The failure of the pension system in Mexico is and will be evident.

For their part, costs of formal recruitment are on their own elevated for private companies. State and federal taxes are disincentives towards the creation of formal employment. The proposal does precisely that, increase the cost of recruitment, mainly to those collecting lower wages.

Likewise, the recruitment, as mentioned earlier, cost increment will have repercussions on the informal employment market due to the displacement of formal employees that the measure may cause, which will increase labor informality (rise in offer) and will drive wages down.

⁶ The other 6 million contribute by the 1973 promulgated law; at the retirement moment, they can choose between the 1973 or 1997 law; nevertheless, employees usually select the 1973's law pension scheme.

In Mexico, the informal employment wage level is 10% lower than formal employment due to IMMSS and Invoavit (Workers' National Housing Fund Institute, for its acronym in Spanish) contributions (Antón, 2012). In other words, the proposal spawns certain conditions that allow the differences between formal and informal workers to intensify.

Suppose we are talking about financial viability. It is important to clarify that, during the last five years, the approved federal budget pertaining to the exercise of the social quota is more significant on average by 3.9%. By 2019 the under-spending was 12%, and in spite of that, by the 2020 fiscal exercise, the approved budget was increased by (17%). In other words, the account with which the social quota is paid to the workers is receiving more budget than needed.

According to CIEP (Economic and Budgetary Investigation Center, for its acronym in Spanish), the cost of the social quota with the current law would require 41,205 million pesos; meanwhile, with the reassignment proposal, the amount would rise to 43,573 million pesos (CIEP, 2020). Hence is considered probable that it will be covered with the Statutory Contributions program; that is to say, it will not require extraordinary resources.

Likewise, the same phenomenon is replicated to those workers that receive the PMG. In 2020 the number of workers with that benefit was 18,230, which received on averages 3,289 pesos. The disbursed amount was 720 million pesos; nevertheless, the assigned budget to the PMG program was 5,204.76 million pesos. In other words, the fiscal cost of the measure would be covered at least until 2021, and if the said budgetary program is abided, it will not require more than the incurred spending.

On its part, the decrease in commissions collection will allow to increase workers' savings. According to CONSAR, a 50% reduction in commissions collection would increase an average of 12% of workers' savings. The aggregate will allow asset reassignment in the Mexican financial system, meaning it will have more savings that could be destined for long-term investments. The workers' financial savings will have more relevance pertaining to the total assets in the financial system.



Image: laboral informality in El pulso laboral at <https://tinyurl.com/ysn3nvau>



Image: laboral formality in Capital Humano at <https://tinyurl.com/39srfwvr>

PENSIONS, PERPETUATING TWO MEXICO'S

The amendments to the regulatory framework in pension matters cater to the disease symptoms but do not address the structural factors that cause it. Therefore, the issue will be better managed in the best-case scenario, but the patient will not get better; the disease will remain there, and it will worsen.

With the law's amendments, the dual work system is strengthened (formal and informal). Moreover, in the search for better labor conditions in the formal market, decisions are taken to temper the crisis that will be faced by a significant part of Mexican workers at the end of their working life. Thereafter, instead of boosting formal work, creation does the opposite by increasing its cost. Hence the measures are not only insufficient to solve the issue but also conflicting.

In turn, the law's aforementioned changes will cause severe distortions in the labor market. The formal work market sensitivity enables us to think that informality will remain one of the biggest challenges of the Mexican economy. Nevertheless, economic resources will be reassigned at a macroeconomic level, given the transference of private incomes (banks). They will release them into the financial system for investments with a long-term horizon, although the possible impacts on economic competence are unknown.

As well as it was proven in a recent Vital Signals study, women have the most significant burden with home care and explain that why they remain outside the economically active population. Labor conditions and the time they can be inside the labor market exclude them from the social protection system in Mexico.

On its part, formal work in the south of the country, mainly in the poorest entities, will remain hooked to economic activities related to health and education –without undermining them– and will be some of the few ways to motivate social mobility in the region, since they ensure better living conditions through working benefits like pension access. Meaning, there are no incentives for people to take risks in other knowledge and working areas.

Consequently, from the law's amendments, at least four fundamental aspects are decoupled: care (strongly related to women), health, employment, and the peculiarities of each entity in the country are left aside. In sum, the federal executive gambles on continuity for the formal and informal Mexico, widening the gaps between North and South. Tagging differences between men and women, which intensified by the effects of the sanitary crisis. The two Mexico's option was taken, despite having the institutional scaffolding strengthened by the amendments on the fourth Constitutional article, which could have led to a more profound reform.

In sum, the federal executive gambles on continuity for the formal and informal Mexico, widening the gaps between North and South, and tagging differences between men and women.



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