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*Institutional Legacies in Post-Communist Pension Reform:
Global Perspectives and Prospects for Consolidation*

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In the last quarter of a century, governments around the world began to revise the terms on which the risk of income loss in old age is insured within and across generations. Whereas most governments have coped with rising demographic and economic pressures on state pension systems by making modest changes in the retirement age and generosity of benefits, an increasing number of governments have undertaken a more fundamental transformation in the basic structure and function of risk protection through some degree of privatization of old age pension institutions. Privatization entails a shift from the principles of risk pooling to individual savings by linking individuals' retirement income directly to lifetime contributions, which are invested and managed by private sector firms. In doing so, this reform transfers to individuals of the risks and costs of saving for old age that were previously shared broadly within and across generations.

The first pension privatization was enacted in Chile by a decree of the Pinochet dictatorship in 1980. Since then, more than 25 countries around the world from Scandinavia to Central Asia have implemented some degree of privatization within statutory old age pension systems. In most cases, such reforms have been adopted in the context of competitive democracy, and even more strikingly, have in some instances been approved often by wide legislative majorities and with broad public support. Although Latin America led the world in pension privatizations adopted in the 1990s, by the end of 2005, the post-communist nations of Central Eastern Europe to Central Asia were home to the greatest number of countries that had adopted some degree of market-oriented pension reform (see Table 1 for a list of such countries).

The location, number, and depth of pension privatizations adopted around the world present striking puzzles for scholarly research. In particular, this reform offers a critical opportunity to re-examine the nature and role of policy legacies in the renegotiation of this basic structure of intergenerational social contracts. Policy legacies have long been shown to influence powerfully the goals and options available for institutional reform.¹ But how and to what limit these effects are felt remains the subject of considerable debate. Indeed, the remarkable stability

of state social welfare institutions throughout the second half of the twentieth century spawned a prolific body of research demonstrating an array of forceful policy feedback mechanisms that stabilize and reinforce a given ‘path’ of institutional development over time.² As vital as this research has been, it has one critical lacuna: it has great difficulty in accounting for instances where qualitative changes in the structure and ends of state welfare systems do take place, such as in the privatization of old age pensions. A prima facie inspection of the depth and location of pension privatizations in the last quarter century raises certain doubts about the predominance of policy ‘lock-in’ forces in foreclosing the option of fundamental institutional transformation in large and mature welfare states.³ Yet, closer inspection of the design of reformed pension systems also fails to substantiate the view that private pension systems are being constructed upon a ‘tabula rasa.’ Most privatized pension systems bear a heavy imprint of their institutional progenitors, combining a scaled-back version of the old public social insurance system with newly-created individual retirement accounts that are placed under private management. The tabula rasa perspective is also thrown into question by inspection of the broader ‘second generation’ of social policy reforms in Latin America and Central and Eastern Europe, which reveal considerably more modest institutional restructuring efforts in areas as such health care and education reform.⁴ How, then, can we understand the role of institutional legacies in the structural transformation of old age pensions?

Analysis of structural pension reform must begin with recognition of the overwhelming ‘stickiness’ of old age pension systems.⁵ Such resilience has justified a view of old age pensions as the archetype of path-dependent institutional processes. In particular, pensions have been shown to be subject to the forces of ‘increasing returns,’ through which every step along a given institutional ‘path’ makes subsequent departures ever more unlikely.⁶ But such a view is unsatisfactory from the perspective of understanding the role of institutional legacies in structural reform, for it suggests that an institutional inheritance exerts a powerful, if not deterministic effect on the prospects for institutional change only until such forces are overwhelmed or

disrupted by exogenous pressures. The weight of causal explanations of institutional change thus rests heavily on the force of external pressures. This paper takes a different view, which seeks to connect the processes of institutional stability and fundamental, path-departing change. To do so, I first re-examine the concept of institutional legacy, arguing that in addition to the conventional emphasis on the structural features of an institution, such as its maturity, scope and generosity, relevant policy legacies reside within the set of shared normative principles (concepts of what is ‘fair’) and performance expectations (of what the institution can or should provide) that develop over time with the institution. These elements of an institutional inheritance, which I call its ‘living legacy,’ may long provide a foundation for behaviors and attitudes that reproduce a given institution, but as recent research has shown, may also become a lever for institutional change. I lay out a causal argument connecting the institution’s living legacy to the strategic political context and macroeconomic landscape, which mediate the causal effect of institutional legacies on the adoption of pension privatization. I evaluate this more contingent view of path-dependent reform in a global data set of structural pension reforms adopted between 1980 and 2002. The quantitative analysis reveals that the effect of a pension system’s financial legacy on the likelihood of privatization is not linear, and that the government’s financial situation at the time of reform intervenes systematically in shaping the viability of privatization efforts. The prospects for building democratic majorities around pension privatization, moreover, depend not simply on the breath of formal legislative authority claimed by the government, but on the partisan stripe of governing party, wherein left parties enjoy systematic advantages in the adoption of this reform. Pension privatization adopted by left governments, however, is systematically less extensive in market orientation than that adopted by non-left governments.

The last part of the paper asks whether analysis of the broader global can provide any analytic leverage into explanation of the dramatic institutional transformations occurring among the post-communist social protection systems. A vignette of the pension privatization in Poland provides a context in which the causal process and long-term prospects for consolidation of

market-oriented pension institutions are explored. This discussion also returns to the question of policy legacies in the process of institutional reform. The implication of my argument about living legacies suggests that the more critical force of inherited beliefs and expectations are likely to be felt in the consolidation of the new liberal social bargains. Although this process has only just begun, evidence to date suggests that the political sustainability of market-based pension systems is far from assured, but may depend heavily on the interaction between the institution's living legacy and the ways in which reformers have navigated political conflicts over structural pension reform.

Pension Privatization and Path-Dependent Change

The concept of path dependence has been central to the study of the post-war welfare state. In its most basic formulation, path dependence suggests merely that events and policy choices in the past systematically shape later options and goals of institutional development. The precise nature and effect of institutional legacies on subsequent developments, however, vary markedly throughout this literature.⁷ For Myles and Pierson, old age pension systems represent the 'classic case' of path dependent processes. Once in place, Pierson has shown, social security institutions become a central part of the political landscape, delimiting social rights and benefits, giving program beneficiaries something for which to fight.⁸ More specifically, he has shown that pensions are subject to the institutional processes of 'increasing returns,' which tend to 'lock-in' a given institutional design and make significant institutional ever more unlikely over time.⁹

As a case of institutional *path departure*, pension privatization offers a critical opportunity to assess the causal role of institutional feedback mechanisms and legacies on the process of institutional change.¹⁰ Before proceeding with this argument, it is important to highlight the aspect of this reform that makes pension privatization such a fundamental path departure. Although much attention has been focused on the transfer of pension fund management from the public to private sector, it is not the 'privateness' of the new institution that marks it as a fundamental structural shift in the welfare state. Rather, it is shift from risk pooling to self-

insurance that classifies pension privatization that represents a fundamental break with the established path of institutional development. While social programs manage risk differently in across nations and policy areas, most social welfare systems rest upon some objective of reapportioning social risks broadly across society.¹¹ For Esping-Andersen, then, differences across welfare regimes reside not in *whether* there is pooling, but in the *way* that risks are pooled.¹² The replacement of risk pooling mechanisms with those of individual savings thus transforms the very ends and essence of the welfare state, signaling that a structural shift in this social institution has occurred.¹³ Thus while new forms of private savings opportunities, ownership and property rights are created, and with them the possibilities for some considerable individual gains, pension privatization also imposes meaningful losses on the beneficiaries of redistribution in traditional social insurance programs.

For scholars of social welfare reform, the enormous electoral hazards of loss imposition have long been shown to make fundamental reform of such institutions politically difficult, if not unviable. The beneficiaries of existing social policies, as Pierson has shown, are not only loathe to accept cuts their current benefits (even where commensurate gains are promised), but these concentrated interests are also advantaged in political mobilization relative to the dispersed interests of potential beneficiaries of reform.¹⁴ Retrenchment politics in mature welfare states thus are said to be governed by the logic of ‘blame avoidance,’ through which politicians face strong incentives to obfuscate or avoid the imposition of losses to current beneficiaries.¹⁵ The magnitude of political obstacles to reform, in this view, is proxied by the size of a welfare state’s clientele, which are understood not only to be strongly attached to the welfare state, but are also disposed to punish any politician that threatens these benefits.¹⁶ While the political unpopularity of benefit cuts remains beyond question, recent evidence that governments have won popular *support* for welfare state restructuring demands that we reconsider the conventional view of social security reform as a strictly politically-deadly endeavor.¹⁷ Recent research, however, provides reason to

question whether an individual's status as beneficiary of a pension system necessarily disposes her to unequivocal support and defense of the status quo.

A second critical mechanism that has been long understood to impede significant reforms of the welfare state is the financial legacy of these institutions. For old age pension systems in particular, the costs of 'exit' rise steadily over time, making fundamental reforms such as privatization ever more unlikely as such institutions mature.¹⁸ Such costs emerge in the privatization process as governments must continue to honor pension promises in the old system just as current workers' payroll contributions, which are typically used to finance such costs, are diverted (in all or part) to privately-managed pension funds.¹⁹ Substantial evidence indeed suggests that where implicit pension costs are very high, deep privatization becomes ever more difficult. But the increasing returns perspective, which views financial costs as an inexorably-rising barrier to privatization, encounters certain limitations in its empirical and theoretical force. First, a simple comparison of the average financial inheritance of privatizing countries, measured as the implicit pension debt (IPD), reveals that among the set of countries examined in this study, the inherited financial costs embedded in the institutions that were privatized is higher than that in non-privatizers (see Table 2). At the same time, an increasing number of exceptional cases of pension privatization, such as in Sweden, Latvia, Poland and Uruguay, challenge the view that even partial privatization is financially unviable where pension systems are large and mature.²⁰

From a theoretical standpoint, theories of increasing returns are forced to rely heavily on the causal force of exogenous shocks to explain cases of significant institutional reform. Measures such as pension privatization, in this view, emerge only where external pressures become so great as to disrupt or overwhelm the reinforcing effects of rising transitional costs of reform, allowing a new institutional process altogether to be established.²¹ As Thelen has shown for incremental institutional change, however, such a sharp line need not be drawn between the processes of path-dependent continuity and change.²² The challenge for this study is to probe

whether the processes of institutional reproduction and change can also be linked for instances of fundamental, path-departing reform such as pension privatization.

Contingencies in Institutional Path Departure

As a starting point for analysis linking path-dependent stability and change, I seek to extend the concept of policy legacy to include those elements of an institutional inheritance that reside beyond the formal rules, sanctions and benefit promises. Two such elements in particular may be worthy of emphasis. The first is the set of shared norms, or local conceptions of what is fair, that provide a normative legitimation for established social welfare institutions in a given context. The second is the set of performance expectations – about what functions the institution performs and what constitutes an adequate institutional output – that develop through individuals' long-term experiences with an institution. I call these the institution's 'living' legacy, for these emerge from and stabilize along with an institution, but also are changeable rather than fixed over time. Shared norms of fairness, whether they are grounded in concepts of solidarity, reciprocity or earned rights, have been shown to be critical stanchions of the welfare state and important byproducts of it.²³ Expectations about institutional performance, for their part, emerge over time with citizens' experiences of the institution or through socially-transmitted knowledge of it.²⁴ These performance expectations may be said to be part of what Pierson has called 'adapted expectations' that tend to be quite resilient, and also to reinforce behavior associated with the existing institution over time.²⁵ While such beliefs and expectations are generally stable and may long underpin behavior that reproduces the institution, they may also have negative implications – either where the institution itself diverges from long-established standards, or where these underlying beliefs and expectations themselves become subject to contestation and change.

Beliefs and expectations thus may be part of two distinct processes of institutional change. As mechanisms of institutional reproduction, norms and expectations establish a 'bar' or standard against which ongoing institutional performance is gauged. At any given time, then, citizens also hold a set of attitudes toward the institution that are derived from a comparison of the institutional

outputs (including the behavior of other participants and managers, and the institution's products, such as pensions themselves) to their prior beliefs about what is fair and expectations of institutional performance. As Grief and Laitin have shown, where individuals compare institutional outputs with expectations and find the former to fall short, beliefs about the institution may change, leading once-reinforcing behavior to give way to actions that undermine the institution.²⁶ For Margaret Levi, shared norms also provide a crucial mechanism through which the erosion of support for a given institution may emerge. When institutional outputs are perceived to be no longer consistent with norms of fairness and where perceptions of gains from compliance erode, consent to a given institutional bargain may be withdrawn and the institution weakened.²⁷ Thus, while expectations and beliefs associated with an institution may help to stabilize and reproduce it over the long term, these may also become mechanisms through which declines in satisfaction emerge, and with it, behavior or beliefs that undermine the existing institution.

Although these theories point to a causal process through which *some* form of institutional change may occur, they point most directly to reform that brings the existing institutions back in line with prevailing normative beliefs and performance expectations – that is, for a ‘fix’ of the institution. But pension privatization goes far beyond a restoration of the prior institutional standards and expected performance. Rather, privatization fundamentally transforms those very standards, altering the basic social bargain implied by old age income programs in a given country.²⁸ Of course, reformers can, and often do, seek public support for pension privatization on the illusory claims of restoring or ‘saving’ the national pension system. Such strategies are exceedingly short-sighted, however, as they set up the possibility for later protests when institutional outputs diverge from expectations and tightly-held norms.

But the normative principles and expectations that long upheld a given institution may also change, either prior to or in the course of political conflict over institutional reform. Such processes of belief and expectation change imply transformations in the basic bargain or social

foundations of the institution. Such renegotiations may occur in reform processes where politicians challenge traditional concepts of fairness that long upheld a given institution (such as those of mutualism and collective responsibility) by introducing liberal norms such as individual responsibility and freedom.²⁹ Where ideas become the central to political conflict over pension privatization, debates are likely to take on an ideological tone as reformers assail the old system as unjust, and tout the new one as more equitable. Reformers may also win public support for reform by raising the ‘bar’ for performance expectations, such as by arguing that citizens are entitled *more* than they currently receive from their pension system. In such instances, the potential benefits to be won through new private savings instruments, such as expanded ownership, choice, higher rates of return, and the like, become the foundations of consent to the new social bargain. Support for reform in the latter case will rest heavily on expected material gains. While politically quite saleable, these terms of consent may establish a shaky foundation for the long-term sustainability of the new market-based institutions, as I will argue in the final part of the paper.

The beliefs and expectations associated with a given institution thus may become a mechanism severing citizens’ attachments to the status quo on the basis of perceived divergence of the institution from these established standards. These principles and expectations also may be challenged and subject to revision themselves. When beliefs about what is fair and expectations about what the institution can or should do are renegotiated in ways consistent with the principles and outputs of private pension systems, then a durable social foundation for the new institution is likely to be established. Debate over principles of individual versus collective responsibility, and specification of the likely costs and risks associated with private investment need not occur for radical institutional change to be enacted, however. Although most reformers spend considerable time and energy seeking public support for private pension reform, political incentives point more clearly toward the obfuscation of the costs of reform, and to the portrayal of this measure as an unequivocal material benefit for citizens. In other words, it is possible to change a law without

renegotiating the basic social bargain that underpins it. The final section of this paper returns to the implications of this argument for the process of consolidation of reformed pension systems. As minimum requirements for the legislation of pension privatization in democratic contexts, however, reformers need only to win the sanction of these measures by elected legislatures; privatization must also be financially viable.

Legislative Sanction. The electoral hazards of imposing losses on organized beneficiaries of a given institution have long been shown to prevent major reform of the welfare state.³⁰ Although the imposition of losses is an ineluctable feature of pension privatization, this reform is not simply an extension of politics of retrenchment, or benefit cuts alone. For in addition to the rollback of risk-pooling structures, privatization involves important *creative* processes that center on the establishment of new forms of property rights and investment options. These potential distributive benefits delimit critical opportunities for politicians to obfuscate the attendant losses and risks associated with the reform, and thus to potentially neutralize the electoral hazards of privatization.³¹ To the extent that the salience of losses are diminished, potential veto actors may fail to be activated and politicians may face strong electoral incentives to support this reform in order to claim political credit for providing new benefits or for resolving apparent institutional problems. Where such a distributive logic dominates the legislative process, pension privatization may be approved by large – if not over-sized – legislative coalitions.

The emergence of a credit-claiming logic around pension privatization is far from assured, however. Claims that privatization will improve citizens' material conditions or that such reforms are equity-enhancing may easily ring hollow where reformers lack credibility on social welfare issues. Moreover, where credible social or political actors (e.g., traditional defenders of the welfare state such as labor unions, retirees or left parties) oppose privatization, the loss-imposing elements of the reform are likely to gain political salience. In such cases, a veto dynamic may be activated, and the electoral costs of support for such a reform elevated as well.

Recent scholarship on social welfare reforms suggest that partisan cues provide a critical short-cut for voters seeking to navigate complex issues such as old age pension privatization. In particular, left parties may effectively draw upon their traditional association with the defense of the welfare state and interests of the working class to credibly portray social welfare reforms as necessary, rather than ideologically-motivated, and even as beneficial for workers.³² Left parties, moreover, are more likely to gain the support of labor unions and retirees for privatization initiatives, since leaders of these groups may prefer to negotiate concessions within reform led by a left party than to risk surrendering such opportunities under subsequent governments.³³ Citizens also may view welfare state reform by the left as a ‘lesser evil’ compared to that of a right-wing party, as Kitschelt has argued.³⁴ The electoral costs of loss imposition thus may be attenuated, if not supplanted altogether by political credit-claiming, where such measures are initiated by a left party government and supported by credible social actors such as labor unions and retirees.

Financial viability. The conventional view of path-dependent change suggests that the viability of pension privatization diminishes strictly as an institution becomes more mature.³⁵ Such a view, however, overlooks the ways in which strategic government actors can reduce or postpone the transitional costs of reform. Rather than being an exogenous parameter that delimits the opportunities for reform, the cost of pension privatization is endogenous to the degree of structural reform that is adopted and to the design of transitional rules. While some governments have used discretionary income such as privatization revenue to offset the costs of pension reform, others have redesigned the transitional rules in such a way that reduces or postpones the financial toll exacted of governments through this reform.³⁶

The financial viability of this reform also is likely to depend heavily on the resources that are *effectively* available to the government to finance this cost. Governments may fund the transition to a private pension system in several ways, such as through increased taxation, by making spending cuts elsewhere in the budget, or through increased sovereign borrowing. The first two options are politically quite difficult, however, making the use of government debt the

principal means of absorbing the transitional cost of privatization. But most governments also face formal and informal constraints on sovereign borrowing. For governments that rely on international credit to finance their budget deficits or for those seeking membership in communities such as the European Union, these international political or financial actors may threaten to *punish* them for overstepping the acceptable limits on sovereign debt-to-GDP ratios.³⁷ Two governments that inherit similar implicit costs from their old pension systems, but which differ with regard to extant debt burdens, thus face very different effective financial constraints on the adoption of pension privatization initiatives. For the more heavily indebted government, even a modest increase in the sovereign debt-to-GDP ratio may threaten international punishment. Where such penalties are meted out by financial market actors, the cost may entail higher interest rates on existing and future borrowing, or even capital flight. The implication of this argument is that while the pension system's implicit financial legacy is important, it is far from absolute in itself as a determinant of the prospects for fundamental reform. Rather, these possibilities may be mediated powerfully by the fiscal context in which the pension reform is proposed, and by strategic choices made by the government in the reform process.

Empirical Analysis

The arguments in the previous section suggests that the possibilities for radical institutional restructuring may be contingent and context-dependent, rather than determined strictly by the structure and maturity of an institution. I expect that the likelihood of privatization will be greater where governing coalitions are led by left parties; however, such governments should be more likely to adopt much less private reforms, as a concession to their core constituents. Although the correspondence between a pension institution and prevailing norms and performance expectations is difficult to capture in quantitative terms, following Levi, I take compliance with a given institution as a proxy for the broad level of consent, or perceptions that the institution is fair and effective.³⁸ Where such consent erodes, active compliance rates are likely to decline; with them, falling political opposition to privatization should make such a reform more likely, all else being equal. I

test the effect of the inherited pension liabilities on the possibilities for reform. In the conventional view, the likelihood of privatization should decline strictly as implicit pension costs rise. I expect that in addition to the endogenous costs of privatization, the financial leeway that governments enjoy to absorb the transitional cost through additional borrowing should also shape the likelihood of adopting some degree of pension privatization. As prior debt-to-GDP ratios rise, the likelihood of reform should fall, all else being equal.

I test these hypotheses in a data set encompassing 69 countries including the OECD member nations, Latin America and post-communist nations of Central and Eastern Europe and Central Asia (see the Appendix for a country list). The empirical analysis uses a two-step Heckman selection model; this estimator combines regression analysis of variation across nations on the degree of structural reform while taking into account the prior likelihood of privatization using a probit analysis of the broader set of countries. In this way, the Heckman model corrects for the effects of sample selection in analysis of degrees of variation in the reform outcome across privatizing governments.³⁹

Dependent Variable. The dependent variable of the analysis captures movements toward pension privatization along the two politically-relevant dimensions of structural reform discussed above. The first measures the cuts to risk pooling (defined benefit) programs, while the second captures the expansion of private property rights through the size of private benefits accrued to the average wage worker in the new private retirement accounts. The first dimension is measured as the share of the average-wage worker's pension that derives from her individual, privately-managed pension account (*Percent Private*), while the latter is the replacement rate, or percent of working income for the average wage worker, that derives from her privately-managed individual pension account (*Private Benefit*). Both measures are derived from simulations using the text of pension reform laws in the nations around the world that implemented structural pension reforms between 1980 and 2002.⁴⁰ Figure 1 illustrates the simulated private and total replacement rate in the reformed pension systems, while Figure 2 arrays the two dimensions of

structural pension reform. Without a theoretical basis for privileging one dimension over the other, I take the product of the two dimensions – private income replacement and the public private mix – as the dependent variable for the outcome equation in this analysis. This measure, in effect, weighs the private replacement rate by its share of the total pension benefit for the average wage worker.

Independent Variables. I use the following indicators to capture the main explanatory variables to explain movements toward market-oriented pension reform across nations. The Appendix provides a full list of definitions and sources. The force of *inherited pension liabilities* is measured by the size and generosity of state pension liabilities to existing pensioners and workers, or implicit pension debt (IPD).⁴¹ The partisan structure of legislative competition is captured first using the size of the *governing majority*, or share of seats held by the governing party or parties. I include a binary variable measuring *left party government* to indicate the partisan identity of the governing party. This is coded 1 if the largest governing party in the legislature is of the left and 0 otherwise. The level of fragmentation or competition among opposition parties is measured using the Herfindahl index of opposition parties, or sum of squared seat shares held by competing parties. A government's *financial leeway* to absorb the transitional cost of privatization is captured with by the ratio of central government debt to GDP. *Compliance* with state pension institution is measured as the ratio of active contributors to the social security system to working age population.

Control Variables. I control for demographic and economic pressures to adopt market-conforming pension reforms in three ways. First, demographic pressure is measured as the share of the population age 65 or older. The forces of globalization are captured through exposure to trade, or imports plus exports as a share of GDP, and through a nation's exposure to foreign capital flows, including direct, portfolio and other investment inflows and outflows for each country. The potential financial influence borne by the World Bank, which has advocated pension privatization, is operationalized as the sum of World Bank and IDA loans and credits as a percent of GDP for each country. I also control for the size of the economy as the natural log of gross domestic

product, and include the unemployment level to control for the effect of broader labor market trends on the level of compliance with the old age pension system. Political system controls take two forms. The first is a measure of whether the chief executive is a directly-elected president, indirectly elected president, or leader of a parliamentary government. The second is the level of democratic freedom, which is measured as the Freedom House index of political rights.

Empirical Estimation. The results of the empirical analysis are reported in Table 3. The cross-national analysis lends support to the contingent view of path dependent institutional change. In particular, the empirical model suggests that along with powerful demographic pressures, the political and financial context in which structural pension reform is brought to the agenda weigh heavily in shaping the likelihood and degree of institutional reform that governments enact.

Beginning with the political variables, the analysis reveals that winning support for pension privatization is not simply a question of how much legislative authority the governing party can command, but rather that such authority is mediated by *who governs* in the legislative assembly. This effect is evidenced in the variables for the size of the governing majority, and its interaction with the left party variable in the first and second model specifications of the selection equation. In the first specification, the size of the governing majority and the partisan stripe of the largest legislative party alone are not significant predictors of privatization. In the second specification, however, the interaction between the size of the governing majority and left party leadership is significant and positive. The coefficient suggests that whereas the size of the majority alone does not translate directly into effective capacity to privatize; when such authority is held by a left party, however, the potential political costs – of concentrated accountability for reform – may be reduced, if not neutralized by this credible partisan actor. This result supports the argument that parties of the left may enjoy significant advantages in advancing pension privatization in such a way that involves a credit-claiming dynamic, therein neutralizing the electoral incentives associated with the imposition of losses through this reform.⁴²

The coefficient on the measure of division among opposition parties in the second model specification is negative and statistically significant beyond the 1 percent level, indicating that as opposition parties become more divided, the likelihood of privatization increases. Where opposition parties are weak and highly fragmented, their ability to act collectively – here, to prevent extensive policy change – diminishes.⁴³ Efforts to mobilize against pension privatization by minority parties thus may be undermined where authority is divided broadly among a large number of opposition parties. Among privatizing governments, the outcome equations offer support to previous research that suggests that while left parties have joined or even led the movement toward market-oriented reform around the world, significant partisan differences are apparent in the nature and style of these reforms.⁴⁴ In this case, left governments systematically adopt less extensive market-oriented pension reforms compared to non-left governments. The size of the legislative majority, however, tells us little about the degree of structural reform that is adopted across privatizing governments.

The role of path-dependent forces in the privatization of old age pensions is captured first through the measure of the implicit pension debt (IPD). The IPD signals the political and financial inheritance of the existing public pension system. In order to capture the effect of the implicit pension debt at very high levels, I also include the square of the IPD in the likelihood equations. The coefficients on both IPD variables are statistically significant. The sign on the IPD variable is positive, while that on the coefficient for the square of IPD is negative. Together, these estimates signal that the effect of the pension system's financial inheritance on the likelihood of privatization is conditioned by the magnitude of those implicit liabilities: when the IPD is low and moderate, an increase in implicit pension costs raises the likelihood that governments will embrace pension privatization, while at very high levels the forces of policy 'lock-in' emerge, consistent with Pierson's account.

The compliance variable approaches the concept of a policy legacy from a different angle. To the extent that compliance with the pension system may be taken as a signal of citizens' consent

to the existing institution, then political obstacles to privatization may track roughly the scope of active compliance with the status quo design, controlling for broader labor market trends.⁴⁵ This relationship, of course, is likely to be strongest in countries where the state enforcement capacity is imperfect, and where a substantial shadow economy makes evasion of taxes and payroll contributions to social insurance programs a realistic option for many workers. The prevailing level of unemployment in the economy is included in both model specifications in order to control for broader labor market trends. The compliance rate in this set of countries varies from 9 percent in the Dominican Republic to 98 percent in Switzerland. The coefficient on this variable is negative and statistically significant at ten percent, offering qualified support for the expectation that as compliance falls, the likelihood of privatization will be greater. While this is a very rough proxy for the prevailing attitudes toward the fairness and efficacy of a pension institution, the analysis suggests that further inquiry into more dynamic concepts of institutional legacies that lie beyond structural attributes of an institution may be fruitful.

The coefficient on the level of government debt as a percent of GDP is negative and significant, consistent with expectations that government financial conditions will mediate the likelihood of adopting this reform, all else being equal. Although implicit and explicit pension debt are equivalent from an intertemporal budget perspective, the mere relabeling of implicit liabilities as explicit debt may be highly costly for reforming governments.⁴⁶ Thus while the inherited financial cost of a pension system remains important, it is not deterministic of the possibilities for privatization. Rather, the broader fiscal and international contexts in which governments seek to recognize those liabilities weigh heavily in the ability of governments in a globalized economy to adopt deep structural reform. Although exposure to foreign capital flows does not predict the likelihood of privatization, among governments that do privatize, those receiving a lower volume of international capital flows systematically take greater steps toward private pension provision. Globalization thus may act as both a constraint and a catalyst for the adoption of market-oriented reform in many countries.

The controls for demographic pressure reveal a significant and strong effect on the adoption of pension privatization. The coefficient on World Bank loans also is positive across both model specifications. This effect is not surprising given that almost every privatizing nation in Latin America and the post-communist region, where the bulk of the pension privatizations have been located, has also received financial support from the World Bank in the 1990s. But it is not clear from such an analysis whether this correlation reveals the effect of financial coercion, through which the Bank would use conditions on development loans to impose privatization, or whether government actors that were anyway resolved to privatize are more disposed to accept World Bank support for structural reform. Closer case-based research is required in order to sort out the precise causal mechanisms underlying this observed correlation.⁴⁷

The coefficient on the political system variable indicates that pension privatization is significantly more likely in direct presidential systems than in parliamentary systems of government. The negative and statistically significant coefficients on the democracy variable in both model specifications indicate that pension privatization is more likely in democratic than in non-democratic countries, all else being equal.⁴⁸ The Latin America variable is not significant, suggesting that pension privatization is neither more nor less likely in Latin America than in other regions of the world due to unmeasured factors in this equation. With the rapid diffusion of this reform among post-communist nations in the 1990s, pension privatization can no longer be considered a predominantly Latin American phenomenon. The coefficient on the size of the economy, the natural log of gross domestic product, is negative, but is not a statistically significant as a predictor of the likelihood of pension privatization.

Overall, the quantitative analysis provides a useful roadmap for inquiry into where and under what conditions this dramatic institutional reconfiguration in social protection is likely to occur. Such analysis offers less insight, however, into the question of how the observed correlations came about, or whether such reforms are likely to be sustained. While it is possible for reformers to enact privatization laws without renegotiating the basic principles and expectations that

have long upheld the traditional social insurance systems, the long-term prospects for these institutions to become stable and self-reinforcing in the absence of such debates is not guaranteed. The next section considers briefly the process and long-term prospects of structural pension reform. Using the vignette of pension privatization in Poland, I ask whether these broader global trends can inform our understanding in any way of the dramatic institutional transformations occurring in post-communist social protection systems.

Process and Prospects for Structural Pension Reform

The design and enactment of market-oriented pension systems represents only one, albeit vital, step in the long-term process of institutional transformation of social protection. Although private pension systems rest upon very different normative foundations and imply very different functions and evaluative standards than traditional social insurance systems do, modern private pension systems may be put in place even where these basic elements of intergenerational social bargains are not explicitly debated or renegotiated within the political process. Of course, the traditional beliefs and expectations that long sustained traditional social protection system may be changed well in advance of pension reform laws. In the past two decades, liberal ideas and norms have disseminated throughout the post-communist world, stimulated both by the collapse of communism and the expansion of cross-border channels of communication. But norms are not binary concepts, and to the extent that traditional principles of solidarity or mutualism, and expectations of state guarantees of old age income remain in place, then certain frictions may emerge in the consolidation of market-based social policy designs. In other words, like the broader process of democratization, the transformation of social and intergenerational bargains such as old age pension institutions cannot be assumed to be a teleological process.⁴⁹

The implication of this legacy argument is that a new institutional ‘path’ is more likely to become stable and self-reinforcing where it rests upon a social foundation of beliefs that the new bargain is fair and effective.⁵⁰ The process of reform, the terms on which privatization is ‘sold’ to political constituents, and strategic decisions made by reforming governments thus may have

powerful long-term consequences for the sustainability of reforms. In formal conflicts over institutional change, therefore, we may observe more than simply the mechanisms of formal institutional change, but also the laying of the groundwork for a new social bargain. While their full implications will only be apparent in the medium to long term, analysis of the interaction of strategic politicians and inherited beliefs and expectations in the political process may yield insight into whether the new institutions will be stable and self-reinforcing, or weak and ultimately self-undermining.⁵¹

The emergence of reinforcing beliefs and behaviors associated with the new social institutions is a particularly difficult challenge for private pension institutions. This is because private pension systems only yield evidence of their effectiveness after three to four decades, when the first working generation begins to retire fully under the rules of the new system. Traditional pay-as-you-go pension systems, by contrast, faced considerably lower performance-based obstacles to consolidation. This is because in most cases state pension institutions began to offer benefits directly to pensioners that were not tied to individual contributions. Societies thus immediately observed evidence of benefits associated with the new social insurance institutions. Not only will such evidence not be forthcoming immediately with the private pension systems, but to the extent that public support for such programs rested heavily on the potential material gains to be won, such as high rates of return and rapid accumulation of wealth, the early years of operation may threaten to betray such high expectations. Where confidence in the fairness and efficacy of new private pension systems erodes, the new market-based institutions may become vulnerable to similar declines in support or compliance that plagued the old state-run pension institutions in many countries.

Pension Reform in Poland. For scholars exploring the transformation of social protection in Eastern Europe, there is little doubt that social insurance reforms were not designed upon a blank slate. Rather, these were more accurately ‘re-built’ within a dense landscape of enduring financial and institutional obligations and public expectations of a strong state

commitment to social welfare.⁵² Avatars of the Bismarckian-style pension systems established throughout Eastern Europe at the end of the 19th century have persisted not only throughout the communist era, but remain an important foundation within partially privatized pension systems.⁵³ The communist legacy, nevertheless, is profound. There were almost no voluntary private pension schemes in the post-communist nations in 1990, and in most cases, pensions were financed from general revenue and were often subsidized with transfers from state-owned firms.⁵⁴ Retirement benefits in most cases were highly redistributive; they were either based on a flat replacement rate or were calculated as a defined percentage of a subset of salary years. Retirement ages were also quite low in the post-communist nations, averaging 60 years for males, and 55 for females.⁵⁵ Despite communist efforts toward homogenization of benefits, however, certain privileges for special occupational categories remained in place in countries such as Poland and Hungary.⁵⁶

The pension privatizations adopted across the post-communist region generally have been designed around a scaled-back public defined-benefit pension tier and a newly-created system of privately-managed individual pension accounts. Notable exceptions to this trend are the radical fully-private pension system in Kazakhstan and the more recent trend toward the adoption of notional defined-contribution (NDC) pension accounts. The NDC model mimics certain aspects of privatization by linking pension benefits directly to individual contributions through individual pension accounts. Such accounts remain under public management, however, and are not funded, although risk pooling and intragenerational redistribution are largely removed from the system.⁵⁷ In countries such as Latvia and Poland, the adoption of an NDC reform within the public tier of the pension system was combined with a partial privatization to virtually eliminate intragenerational redistribution from both pillars of pension system.

Many post-communist pension systems came under significant financial strain in the 1990s during the transition from planned to market economies. In many cases, retirement and disability pensions were used to buffer the social impact of this transition and to shed excess labor

from privatized enterprises.⁵⁸ Pension system dependency ratios thus jumped sharply in the 1990s, well ahead of old age dependency rates. Adding to the strain on these pension systems were sharp declines in compliance rates during the transition, which opened wide gaps in the finances of state social budgets.⁵⁹ In countries such as Hungary and the Czech Republic, post-communist governments coped with rising pension costs and declining system revenue by allowing pension values to erode through under-indexation.⁶⁰ In Poland, by contrast, pensions served as a critical means of compensation for well-organized workers and unions in the process of transition; over the course of the 1990s, the real value of pensions *rose* by 8.8 percent in Poland.⁶¹ As a result, state pension outlays in Poland jumped to over 14 percent of GDP by mid-decade.⁶² Critically, public satisfaction with Poland's pension system did not closely track this surge in spending. Public opinion surveys in Poland reveal broadly negative, and diminishing, perceptions of the state pension system in the mid-1990s.⁶³ Conversely, the real decline in state pension values in the Czech Republic failed to sever the strong and broad public ties to the state pension system in the 1990s; not only was the Czech pension system broadly considered viable, but citizens mobilized massive demonstrations in defense of the system.⁶⁴

In 1998, the government of Poland enacted a deep structural reform of that nation's old age pension system. The new 'mixed' (public and private) pension system, which began to operate in 1999, is organized around a multi-pillar system of individual accounts. The first tier is a mandatory public system of notional individual accounts based on the defined-contribution principle, while the second tier is a mandatory system of privately-managed and funded defined-contribution pension accounts. The third tier is a voluntary system of individual savings accounts also managed by the private sector. Retirement benefits in both the public and private components of the reformed Polish pension system are thus based fundamentally workers' lifetime contributions, which are divided between their public and private individual accounts.⁶⁵ Only the private account, however, is invested in financial markets, while contributions to the notional account are credited with a notional interest rate and used by the government to finance

current pension costs. Poland's reformed pension system thus transfers the overwhelming cost and risks of savings for old age to individuals, although only about half of the average wage earner's retirement income is placed under private sector management.⁶⁶

Despite the depth and strong liberal orientation of Poland's pension reform, it is notable that this measure was not enacted by neoliberal Finance Minister Balcerowicz. Although the issue of pension privatization was raised in the early 1990s, it was dismissed as politically unviable in Poland at that time.⁶⁷ In the Czech Republic as well, Prime Minister Vaclav Klaus, who was famous for his vow to create a 'market economy without adjectives,' was unable to overcome broad and stern public opposition to pension privatization, although he was able to defend rapid and extensive privatization effort as necessary and inevitable for the revitalization of the economy.⁶⁸ Although subsequent governments in the Czech Republic also failed to advance pension privatization measures, Polish citizens would later give broad support to the deep structural reform initiated by the communist successor SLD-PSL coalition (1993-1997.) Neoliberal reformers in both countries thus could gain public support for market-oriented macroeconomic restructuring, but not for old age pension reform. Credibility, these cases suggest, may be highly issue-specific for distinct partisan actors.

Of course, more than simply the partisan stripe of the governing coalition changed in Poland between the early and mid-1990s when the issue of pension privatization was raised again. The SLD-PSL government enjoyed the benefits of a strong economic recovery by mid-decade, while Balcerowicz had raised the issue in the context of deep economic contraction.⁶⁹ At the same time, political debates surrounding pension reform in Poland were considerably less divisive than in other countries. Economic issues in general, and old age pensions in particular, were not the most dominant issue cleavage organizing political competition.⁷⁰ Indeed, the Christian-nationalist Solidarity Electoral Action (AWS), which was in the opposition when the SLD-PSL launched its pension reform effort, had drawn up its own privatization proposals in the early 1990s, and thus raised few serious objections to the SLD-PSL proposal. Following the 1997 national election that

saw the defeat of the SLD-PSL, AWS came to office in alliance with the liberal Freedom Union (UW) and oversaw the design and enactment the final pieces of pension reform legislation that had been initiated by the previous coalition government. While the Polish case lends modest support for the hypothesis about left-party credibility in pension privatization, the reform in fact was carried out by two distinct governments – one with more neoliberal, but important Christian-nationalist credentials, and the other a coalition of communist successor parties.⁷¹

The proposal to privatize the old age pension system in Poland was initiated by technocrats in the Ministry of Finance in response to the sharp rise in pension costs in the early 1990s. The government economists viewed this measure fundamentally as a way to diminish the Polish government's long-term pension costs – a goal that was encouraged by the government's desire to gain accession to the European Union.⁷² Reformers also drew heavily from international policy models such as Chile's privatization, and from extensive consultations with and active participation of the World Bank.

Although finance ministry officials typically work within highly-insulated government ministries focused attention strictly on questions of financial and technical viability, Polish technocrats also paid close attention to the political feasibility of their proposed reform.⁷³ Such concerns were well founded; in Poland, economic reforms were contested by powerful organized social actors such as unions that emerged from and helped to catalyze the end of communism.⁷⁴ Public dialogue over the pension reform lasted for a year and a half in Poland, and included extensive negotiation with labor unions in the context of a Tripartite Council. Polish Labor unions were divided, however, over the issue of pension privatization. Whereas the Solidarity unions supported this measure, the more traditional OPZZ remained opposed to the final measures associated with the reform.⁷⁵ The government made several concessions to labor leaders in exchange for agreement by union leaders (and affiliated parliamentary deputies) to support the reform, and thus neutralized the potential veto of this critical political actor.

In order to gauge the scope of public tolerance for their anticipated pension privatization, the Polish Office of the Government Plenipotentiary for Social Security Reform, which took the lead in the design and implementation of this reform, commissioned public opinion surveys between 1995 and 1997.⁷⁶ These polls reveal considerable dissatisfaction with Poland's old pension system, which grew steadily more negative over these years. They also suggested that a substantial portion of Polish citizens supported the principle that pension benefits should be linked in some way to individual contributions.⁷⁷ However, respondents were given only two options when asked to choose between preferred benefit rules; since there are many ways to link contributions and benefits within a risk pooling system, it is difficult to infer support for such a principle as an outright endorsement of the principle of privatization, *per se*.⁷⁸ Nevertheless, the survey results are suggestive of broad support among Polish citizens for principles that are consistent with a shift toward greater individualization of social protection. Either through public debate over economic reform, or through other channels, liberal ideas emphasizing greater individual responsibility had taken hold in Poland, signaling the existence of critical social foundations to legitimate a more individualized pension system.

After surveying public opinion, Polish reformers launched an ambitious public information campaign in May, 1997 to build support for the pension reform. A central pillar of this campaign, according to Chłoń, was to “talk about the reform as if it were already a fact, even if there were many hurdles still to overcome.” Creating such a perception of inevitability, reformers expected, would leave “very little room for opponents of reform to question the basic elements of the new system.”⁷⁹ The government's political rhetoric associated with the pension reform was also deeply infused with references to shared norms and Catholic social doctrine.⁸⁰ Polish technocrats framed the pension privatization both in terms of its preservation of the “social character” of the pension system as a whole – downplaying the fundamental shift toward individualization of pension savings – and in terms of “universally understandable and straightforward principles” such as full security, protection of acquired rights, and individual

prudence.⁸¹ Polish reformers thus sought at once to establish the reform as consistent with traditional Catholic social doctrine, and to situate it within the realm of new liberal norms of individual responsibility. As Müller points out, however, Polish reformers were less forthcoming about the losses associated with the pension reform, leaving citizens with an imbalanced perception of the relative strengths and weaknesses of this reform, and its implications.⁸² Thus while the normative foundations of the new social bargain were in place, the expectations regarding the associated costs of market-oriented reform may not have been so strong.

From Enactment to Consolidation

In many post-communist cases such as Poland, there was a widely-shared perception in the 1990s that the old state pension system was in need of reform.⁸³ But while this “negative consensus” provided reformers with a mandate to adopt some kind of revision to the ailing social insurance system, the emergence of a positive consensus behind the more dominant liberal social policy model is more difficult to ascertain in the short term. Will such a consensus establish itself over time as these systems take effect? For many economists, the answer is yes, as “good policy is good politics.” With the proper technical foundations, that is, well-designed reforms will function properly and over time will come to enjoy broad political support as a result.⁸⁴ But as mentioned above, the task of gaining broad public confidence based on the *performance* of privatized pension systems will be a considerable one. The challenge of recalibrating expectations and renegotiating the institution’s normative foundations will also be great, considering that in many post-communist nations the organizations of civil society that would normally participate in such debates were substantially weakened as such reforms were undertaken.⁸⁵

The first years of operation of the privatized pension systems in post-communist Europe have been difficult from an operational and financial perspective. Even in Poland the new private pension system began with a rough start as government pension agencies lacked the recordkeeping and systems infrastructure to collect and track individual payroll contributions, causing extensive delays in the transfer of funds to private pension accounts.⁸⁶ Economists also

cite the risk that low returns and high fees charged by private pension funds will under-perform citizens' expectations.⁸⁷ In Poland and Hungary, returns to net pension fund investments failed to exceed inflation in the first five years of operation, bringing about a real contraction in the value of workers' payroll contributions to the private pension fund managers.⁸⁸

Reformers in Poland went beyond their peers in launching widespread public information campaigns associated with pension privatization.⁸⁹ Such efforts, however, focused largely on persuading workers to join the new mixed pension system. Reformers thus concede that this campaign was not successful, since most citizens report paying closer attention to information provided through social networks and from the pension funds themselves, rather than from the government. What is more, the pension funds failed to incorporate deductions for administrative costs into projections of potential rewards for investing with them, and thus painted a highly optimistic portrait of the possibilities for wealth accumulation in their funds.⁹⁰ Indeed, surveys reveal broad confusion and lack of knowledge about the cost structure or rules of the private pension system.⁹¹ Given the complexity of issues and competing sources of information from pension fund managers and peers, the task of fully preparing citizens for the reality of market-based pension provision is a formidable one. Although Polish citizens expressed strong support for the reform shortly after its implementation, after five years of operation technocrats report that increasing dissatisfaction has been voiced by citizens in response to problems of implementation and by the realization of the magnitude of reductions in future benefits.⁹²

What are the prospects of consolidation of private pension systems? Despite initial difficulties, it is unlikely that new private pension systems will be subject to fundamental reversal of new private property rights. However, it is also far from assured that the present institutional equilibrium is the one that will stabilize over the long term in many cases. In Latin America, compliance with privatized pension systems has been low, and in many cases falling over the last decade, while the private pension system in Argentina was subject to partial renationalization and to political intervention in the invested funds. Even in Chile, which long stood as the model for

the ‘good policy makes good politics’ idea, fissures have emerged in the political foundations for this system. In the Chilean case, most ominously, objections to the private pension system are based not strictly on the failure of performance expectations, but rather on the potentially more threatening charge that the private pension system is “unfair.”⁹³

Are such threats to market-based pension systems likely to emerge in the post-communist cases? Data on compliance rates are very difficult to obtain for these countries, although anecdotal evidence provides a very mixed portrait of the political sustainability of private pension institutions. In Hungary, for instance, the private pension system has been subject to repeated changes that have tracked political turnover in the government. Indeed, unlike in Poland, the Hungarian pension reform was enacted without broad partisan consensus, as the majority Socialist Party excluded their major partisan rival, the Alliance of Young Democrats-Civic Party (Fidesz), from negotiations over the reform. Political debate over this measure, moreover, has been described as “elite,” and the measure framed largely in pragmatic terms, emphasizing its macroeconomic effects rather than social dimensions.⁹⁴ The Socialists were defeated by Fidesz shortly after implementation of the reform. Upon taking office in May 1998, Fidesz overturned a provision of the reformed pension system that called for contributions to the private pension system to grow from 6 to 8 percent of wages and even spoke of overturning the private pension system altogether.⁹⁵ Although such radical reversals were not attempted, Hungary’s new pension system has been subject to numerous revisions in the terms of the reform.⁹⁶ These changes are likely to have had strongly negative effects on public confidence in the system. Indeed, while enrollment in the private system grew rapidly following the reform, such growth has leveled off in recent years, while the pace at which eligible workers switching *back* to public pension system has increased dramatically between 1998 and 2002.⁹⁷ While revisions to the Hungarian pension system and to others in the post-communist region have been modest so far, they raise many questions from the standpoint of institutional legacies in the longer term process of institutional transformation.⁹⁸ They also point to a fertile

terrain in which to evaluate the role of political legacies within the processes of institutional change and consolidation.

Conclusion

This paper has approached pension privatization as a case of fundamental change in what had long endured as stable and even self-reinforcing institutions. From the perspective of understanding institutional legacies in this process, the theoretical and empirical challenge has been to trace not only the relevant elements of an institutional legacy that help to explain the location and depth of institutional transformation, but also to use this concept to bridge the theoretical gap between causal explanations of path-dependent continuity and fundamental, path-departing change. I have advanced two related arguments in this essay, and have raised several questions for further research. The first argument suggests that the elements of a policy legacy that are critical for understanding the process of market-oriented reform are not confined solely to formal rules defining the structure, cost and coverage of the institution. In addition to these, I have argued, relevant institutional legacies may reside within the set of normative beliefs (principles of fairness) and performance expectations that develop along with the institution, and which create a local standard, or 'bar' against which ongoing institutional outputs are gauged, allowing for both attitudes and behaviors supportive of institutional reproduction, and for change. The second argument positions this 'living' legacy in the process of institutional transformation. Where institutional outputs are perceived to have fallen short of these standards, then the institutional legacy itself becomes a lever inducing dissatisfaction with the status quo, and opening the door to some kind of institutional reform. Further, where such norms and expectations themselves are subject to contestation and revision, then the social bargain itself may be transformed, and the social foundation of a new and potentially self-reinforcing institution established.

There are several implications of this argument. First, the ability of political leaders to gather support for institutional change is likely to be constrained not simply by the structural features of the institution, or its objective performance, but also by the ways in which political

conflicts over reform are mediated along with conjunctural political and economic factors. Critical political obstacles to reform may be lowered where privatization is led and supported by actors with significant credibility on social policy issues such as left parties, labor leaders and retirees. The macroeconomic context also intervenes in shaping the viability of pension privatization in open and interdependent countries. Across a diverse set of countries and institutional contexts it is neither the case that structural features of an institution are deterministic of the possibilities for substantial reform, nor that such processes are fully pliant to the actions of strategic politicians. More generally, the analysis suggests that further inquiry into the intersection of institutional legacies and the 'modes' of transition may remain a relevant agenda for future research.

Table 1.
Structural Pension Reform in Post-Communist Nations

Year	Pension Privatizations Implemented	Pension Privatization in Process
1998	Hungary	Romania
1998	Kazakhstan	Lithuania
1999	Poland	Ukraine
2001	Latvia	
2002	Croatia	
2002	Estonia	
2002	Bulgaria	
2003	Russia	
2005	Macedonia	
2005	Slovakia	

Source: Chłoń-Domińczak 2004, Fenger 2005.

Table 2.

Implicit Pension Debt	N	Mean	Std. Dev.	Min	Max
Privatizers	23	146.1	84.3	8.7	297
Non-Privatizers	43	135.9	92.4	15.4	401

Figure 1.
Simulation of Structural Pension Reforms around the World
1980-2003

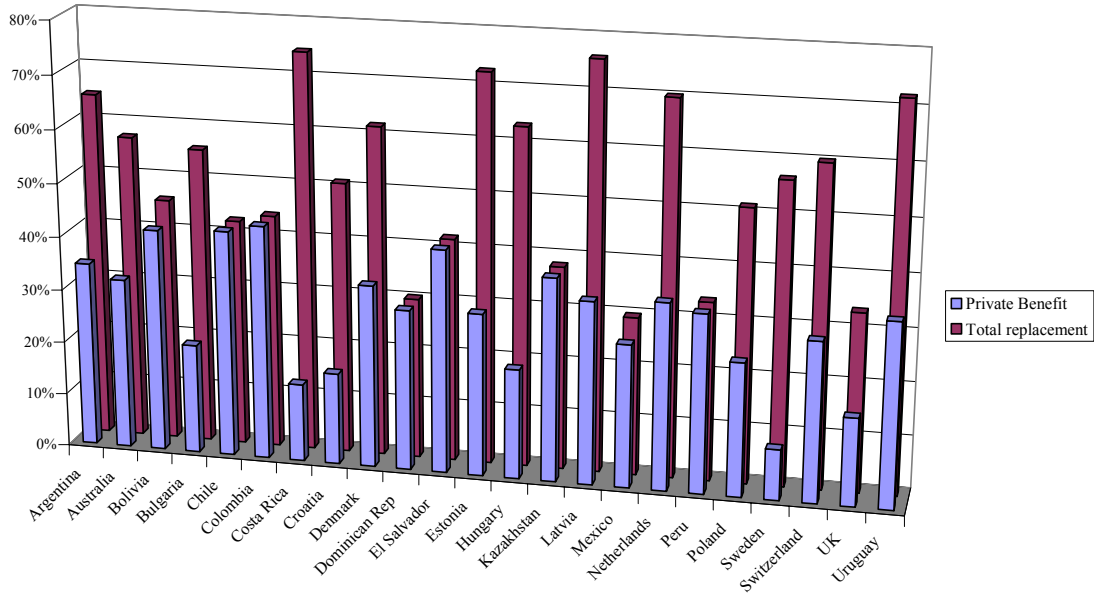


Figure 2.
Structural Pension Reform along Two Dimensions

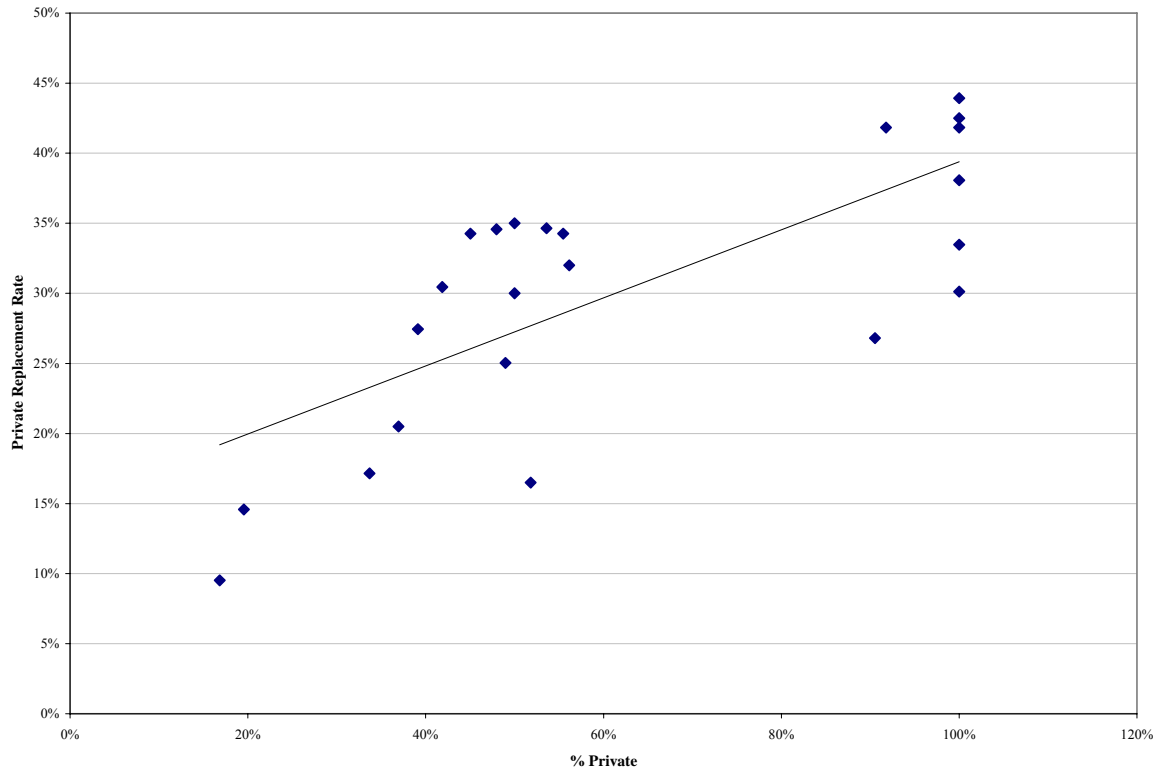


Table 3. Heckman Selection Model of Structural Pension Reform

DV: Structural Pension Reform	1	2
IPD	-0.062 **	-0.081 ***
	0.028	0.027
Capital Flows	-0.467 ***	-0.409 **
	0.155	0.172
Left Party	-8.761 *	-9.861 **
	4.566	4.073
Majority	13.254	-1.509
	13.494	14.290
Opposition Divide	-	-36.318 ***
		10.104
Const.	26.010 ***	54.220
	7.988	10.890
Selection: Likelihood of Privatization		
Left Party	-0.024	-6.911 **
	0.469	2.950
Majority	0.527	-7.255 **
	1.583	2.936
Majority*Left	-	12.946 **
		5.396
Opposition Divide	-	-1.667
		1.188
Parliamentary Govt.	-0.820 ***	-1.352 ***
	0.243	0.489
IPD	0.033	0.035 ***
	0.005	0.011
IPD*IPD	0.000	-0.00011 ***
	0.000	0.00003
Compliance	-0.041 ***	-0.059 *
	0.016	0.034
Unemployment	0.001	-0.004
	0.047	0.075
Population Age 65+ (share)	0.329 ***	0.444 ***
	0.101	0.173
Capital Flows	0.004	0.021
	0.015	0.024
World Bank loans	0.242 *	0.367 **
	0.128	0.185
Democracy	-0.643	-0.582 ***
	0.114	0.214
Latin America	1.151	0.498
	0.736	0.968
Debt (%GDP)	-0.012	-0.013 ***
	0.003	0.004
lnGDP	-0.019	-0.106
	0.071	0.165
Const.	-1.216	5.974 ***
	1.580	2.261
Number of Obs.	54	54
Censored	33	33
Uncensored	21	21
Log likelihood	-87.94059	-80.15289
Wald chi2	32.89	56.36

Appendix.

Countries Included in the Analysis

Latin America	Eastern Europe and Central Asia	OECD
Argentina	Albania	Australia
Bolivia	Armenia	Austria
Brazil	Azerbaijan	Belgium
Chile	Belarus	Canada
Colombia	Bulgaria	Denmark
Costa Rica	Croatia	Finland
Dominican Republic	Czech Republic	France
Ecuador	Estonia	Germany
El Salvador	Georgia	Greece
Guatemala	Hungary	Ireland
Honduras	Kazakhstan	Italy
Jamaica	Kyrgyz Republic	Japan
Mexico	Latvia	Netherlands
Nicaragua	Lithuania	New Zealand
Panama	Macedonia	Norway
Paraguay	Moldova	Portugal
Peru	Poland	Spain
Trinidad and Tobago	Romania	Sweden
Uruguay	Russian Federation	Switzerland
Venezuela	Slovak Republic	Turkey
	Slovenia	United Kingdom
	Tajikistan	United States
	Turkmenistan	
	Ukraine	
	Uzbekistan	

Variable Definitions and Data Sources

Variable	Definition	Source
Population Age 65	Population ages 65 and above is the percentage of the total population that is 65 or older.	World Bank (2005)
Debt	Government debt as a percent of GDP is the entire stock of direct, government, fixed term contractual obligations, including domestic debt and foreign debt, divided by gross domestic product.	World Bank (2005)
Natural Log of Gross Domestic Product	The natural log of GDP at purchaser's prices is the sum of gross value added by all resident producers in the economy. GDP data are in current local currency.	World Bank (2005)
Unemployment	Unemployment refers to the share of the labor force that is without work but available for and seeking employment.	World Bank (2005)
Capital Flows	Gross private capital flows are the sum of the absolute values of direct, portfolio, and other investment inflows and outflows recorded in the balance of payments financial account, excluding changes in the assets and liabilities of monetary authorities and general government. The indicator is calculated as a ratio to GDP in U.S. dollars.	World Bank (2005)
Opposition Divide	Herfindahl Index of Opposition Parties: this is the sum of the squared seat shared of all opposition parties.	Keefer et al., 2004.
World Bank Loans	This is the net disbursements of loans and credits less repayments of principal from the International Bank for Reconstruction and Development (the World Bank). Loan data are in current U.S. dollars, divided by GDP in current U.S. dollars.	World Bank (2005)
Left Party	Dichotomous variable coded 1 if the largest governing party is of the Left, 0 otherwise.	Keefer et al., 2004.
Compliance	Ratio of contributors to working age population, where contributors are defined as workers making regular contributions to national social security pension system.	Palacios and Pallarès-Miralles, 2000.
Parliamentary	Indicator of whether the Chief Executive is a prime minister in a parliamentary system (2), indirectly-elected president (1) or directly-elected president in a presidential system (0)	Keefer et al., 2004.
Majority	The margin of the majority is the fraction of seats held by the government, calculated by dividing government seats in the legislature by total seats.	Keefer et al., 2004.
Democracy	Democracy Score is Freedom House Political Rights Score.	Freedom House "Freedom in the World" Country Ratings 1972-2004
Latin America	Binary variable indicating whether a country is located in Latin America and the Caribbean region.	Author calculation.
Implicit Pension Debt	IPD is an instrument calculated following the method used by James and Brooks (2001) using social spending as a percentage of GDP as the main predictor.	International Monetary Fund <i>Government Financial Statistics</i> .

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- ¹ Hecló 1974; Wier and Skocpol 1985; Pierson 1994, 2000a, 2000b.
- ² Pierson 2004; Thelen 2004.
- ³ See Pierson 1994, 1996, 2000a, 2001.
- ⁴ Müller 2001, p. 71; Nelson 2000.
- ⁵ Pierson 2001; Myles and Pierson 2001.
- ⁶ Myles and Pierson 2001; Pierson 2000a.
- ⁷ See, for example, Hecló 1974; Skocpol 1995.
- ⁸ Pierson 1994, 1996, 200, 2001.
- ⁹ Myles and Pierson 2001, p. 306; Pierson 2001, p.415. See also, Arthur, 1994 p. 6-7, 1996, p. 100; Mahoney 2000, p. 526-527; Myles and Pierson 2001, p. 306.
- ¹⁰ For the concept of ‘path-departure’ in pension reform, see Ebbinghaus 2005, p. 17; Hering 2003, 2004.
- ¹¹ Baldwin 1990; Esping-Andersen 1999, p. 32; Mares 2003; Taylor-Gooby 2004.
- ¹² Esping-Andersen 1999, p. 33.
- ¹³ See Green-Pedersen (2002) for these criteria for structural change in the welfare state. Also see, Pierson 2001, p. 419-420.
- ¹⁴ Pierson 1994, 2001.
- ¹⁵ Myles and Pierson 2001, p. 306; Pierson 1996, p. 154, 2001a, p. 418; Pierson and Weaver 1993; Weaver 1986.
- ¹⁶ Pierson 1994, p.18, 2001, p. 411-413; Myles and Pierson 2001, 306-313.
- ¹⁷ Kitschelt 2001; Ross 2000a, 2000b.
- ¹⁸ Pierson 2000, 2001, p. 414-415. Although institutional change can occur despite rising costs of exit, such revisions are likely to be heavily bounded, as North (1990) has shown.
- ¹⁹ James 1998. The task of financing this transitional cost is complicated by the political difficulty of obliging the working generation to pay twice into the old age pension system – once to finance the pensions of the prior generation and again to save for their own retirement. Myles and Pierson 2001, p. 312-3; Pierson 1996, p. 286.
- ²⁰ Pierson 2001, p. 416.
- ²¹ Mahoney 2000; Pierson 2000b.
- ²² Thelen 1999, 2004.
- ²³ Baldwin 1990, pp. 5-10; Levi 1990, 1997; Rothstein 1998 pp. 134, 222; Svallfors 2002, p. 184.
- ²⁴ See, for example, Bergmark et al. 2000.
- ²⁵ Pierson 2000, p. 77.
- ²⁶ Greif and Laitin 2004, p. 639. Denzau and North (2000) also focus on belief change as a central mechanism of institutional change, but in that case it is the acquisition of new information that challenges prior beliefs or ‘mental models’ that leads to change.
- ²⁷ Levi 1990, 1997.
- ²⁸ Privatization implies that principles of mutualism, solidarity or burden-sharing are supplanted by those of individual freedom and responsibility. In place of expectations associated with redistributive risk-pooling systems, such as benefit guarantees, private pension systems offer individuals the possibility for high rates of return, ownership and choice among competing pension fund managers.
- ²⁹ For ideas and ideology change in institutional reform, see Blyth 2002; Denzau and North 2000.
- ³⁰ Pierson 1994, 1996, 2001; Pierson and Weaver 1993; Weaver 1986.
- ³¹ Kitschelt 2001; Müller 2001, p. 75; Ross 2000a.
- ³² Cukierman and Tommasi 1998; Kitschelt 2001, p. 275; Ross 2000a
- ³³ Hering 2003; Levitsky and Way 1998; Murillo 2001.
- ³⁴ Kitschelt 2001, p. 275. In this view, the advantages of the left to enact welfare state reform are conditioned powerfully by the broader partisan configuration of the electoral arena, rather than simply by the partisan stripe of the governing party. parties of the right. This study lacks sufficient data on the broader configuration of partisan competition in the global sample of countries, and thus does not test the hypothesis that the advantages of the left are mediated by the partisan identification of the major partisan rival.
- ³⁵ Myles and Pierson, 2001, 313; Pierson 1997, p. 286.

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- ³⁶ In other cases, such as in Argentina and Poland, governments have used privatization revenue or other discretionary income to finance the transitional cost of pension privatization.
- ³⁷ Mosley 2003.
- ³⁸ Levi 1997.
- ³⁹ There are several reasons why it is important to consider this question as an antecedent to analysis of differences among structural reformers. First, there is a risk that political and economic factors shaping whether a country privatizes also influence decisions about *how much* structural change these countries adopt. To the extent that we were to overlook the selection process, the prior decision to privatize, analysis of variation among set of privatizing nations may be biased in quantitative and qualitative ways. For discussion, see Achen 1986; Brehm 1993, p. 96; Heckman 1979.
- ⁴⁰ For these simulations I use the following standard assumptions of the number of years in work and retirement, and rates of return to private benefits net of administrative fees: 1.) 35 years of payroll contributions; 2.) 4.5% annual rate of return on investments; 3.) 2% yearly growth in wages; 4.) 20 years of retirement.
- ⁴¹ This instrument is generated using the methodology based on spending data; see James and Brooks 2001.
- ⁴² Kitschelt 2001; Ross 2000. Kitschelt, however, emphasizes that the partisan ‘center of gravity’ alone should not be deterministic, but that such credibility is mediated systematically by the broader strategic configuration of legislative competition, and thus by the partisan identity of the main political rivals as well.
- ⁴³ For legislative fragmentation, collective action and market reform see Johnson and Crisp 2003.
- ⁴⁴ Murillo 2002.
- ⁴⁵ Levi 1991, 1997.
- ⁴⁶ For one thing, explicit debt must be borrowed at the market interest rate, while ‘interest’ on implicit pension liabilities is the rate of growth of the economy. Middle income and developing country governments, moreover, typically pay a high price to borrow internationally; an increase in explicit debt typically leads to a higher interest rate charged on sovereign debt in such nations. In addition to higher borrowing costs, declines in perceived creditworthiness also diminish access to future credit, making pension privatization potentially quite costly for the most cash-strapped governments.
- ⁴⁷ Quantitative and comparative case research on pension reform in Latin America and Eastern Europe casts doubt on the hypothesis of World Bank coercion in these regions. See, Hunter and Brown 2000; Nelson 2000, 2004; Brooks 2005.
- ⁴⁸ Recall that in the Freedom House indicator of political rights lower scores indicate higher degrees of democratic freedom.
- ⁴⁹ For discussion of the process of democratization as non-teleological, see Rose and Shin 2001, p. 333.
- ⁵⁰ This term is inspired by Esping-Andersen 1999.
- ⁵¹ See Offe (1991, p. 878) for discussion of the threat to self-sustaining economic change from the absence of democratic legitimation.
- ⁵² Müller 2001 p. 58; Orenstein 2000; Stark 1992.
- ⁵³ Cerami 2005, p. 10; Müller 2003, p.65; Deacon et al. 1997, p.43.
- ⁵⁴ Fultz and Ruck 2001, p.3.
- ⁵⁵ Fultz and Ruck 2001, p.3.
- ⁵⁶ Chłoń et al. 1999.
- ⁵⁷ Among post-communist nations, NDC pension reforms have been adopted so far in Latvia, Poland and in a modified version, in Russia. Brooks and Weaver 2006; Williamson 2004.
- ⁵⁸ Kitschelt et al. 1999; Roberts n.d., p. 12.
- ⁵⁹ Orenstein 2000.
- ⁶⁰ Augusztinovics 1999; Müller 2003; Orenstein 2000, p.8. Braithwaite, Grootaert and Milanovic (2000) report that in some FSU nations, pension values fell below subsistence levels in the late 1990s. In Hungary, the real value of state pensions fell by 25 percent in the 1990s, while in Kazakhstan, the government merely accumulated arrears in pension promises.
- ⁶¹ Augusztinovics 1999, p. 95; Müller 2003, p. 67. Pension spending in Hungary reached 9.7 percent of GDP at this time.
- ⁶² Augusztinovics 1999, p. 95
- ⁶³ Levitsky and Way 1998, p.175; Hausner 1999, p. 106.
- ⁶⁴ Müller 2001.

⁶⁵ Workers contribute 12.22 percent of wages to the NDC account, and 7.3 percent to the funded account. Under the old system, contributions by employers of 45 percent of the earnings (plus budget subsidies) were used to finance the retirement system along with the disability, occupational injury, sickness and family allowance benefits. The reform reduced the overall (employer and employee) contribution rate to 36.59 percent, reapportioned most of this to workers and grossed-up wages so that the effect would be neutral with regard to take-home pay. The NDC accounts will initially be credited with 15 percentage points of contributions overall (including that from employers), while the remaining 21.59 will be used to finance other social insurance benefits. See, Chłoń et al. 1999, p. 17-18.

⁶⁶ Certain mechanisms of redistribution remain within the system, but these are separated from the main instruments of self insurance. For instance, the system provide for a minimum pension guarantee valued at approximately 27 percent of the average wage. Much like the Chilean system, this benefit will top-up the accounts of workers who have contributed to the system for 25 years (20 for women) but have failed to accumulate sufficient funds in both their notional and funded pension accounts to finance a benefit that reaches this minimum level.

⁶⁷ Chłoń and Mora 2003; personal communication with Estelle James, June 14, 1998.

⁶⁸ Appel 2000, p. 531; Chłoń and Mora 2003, p. 135-6; Müller 1999, p. 138.

⁶⁹ The communist successor SLD also enjoyed the advantage of strategic mobility and little in the way of a stigma for its association with the former ruling communist party. Kitschelt et al. 1999, p. 231.

⁷⁰ Guardiancich 2004, p.55; Kitschelt et al. 1999, p. 252.

⁷¹ Shabad and Slomczynski 1999.

⁷² Poland was also under an IMF agreement in the mid-1990s, for which it made explicit commitments to deficit reduction. The pension reform was expected to generate an average annual deficit of 1.6 percent of GDP, which was lower than the pre-reform ZUS deficit. The real cost was considerably higher, however, on account of the high rates of enrollment in the private system. Chłoń et al. 1999.

⁷³ Chłoń and Mora 2003 p. 148-9.

⁷⁴ Chłoń and Mora 2003; Chłoń et al. 1999; Roberts n.d.; Seleny 1999, p. 490.

⁷⁵ Both OPZZ and Solidarity had strong reservations about the deeper NDC reform of the pay-as-you-go component of the pension system, however. Chłoń et al. 1999, p. 16; Nelson 2001.

⁷⁶ In the case of the media, the Polish government used World Bank support to sponsor ‘study trips’ for members of the Polish government and press to Chile and Argentina to examine the pension reforms in those countries. Chłoń et al. 1999; Chłoń and Mora 2003 p. 148-9; Müller 1999.

⁷⁷ A survey of 1,200 adults in April 1997 revealed that more than half of respondents ‘agreed strongly’ that pensions should be accumulated in individual accounts, while another third ‘agreed’ with this statement; only four percent disagreed. When asked whether pensions should depend on contributions or should be the same for all workers, nearly three-quarters supported the contribution link, while twenty percent supported the idea of equal pensions. Not surprisingly, responses on the last question varied strongly with income. Chłoń 2000, p.11-12. Also see, Chłoń and Mora 2003; Hausner 1999, p.107; Góra and Rutkowski 2000.

⁷⁸ Williamson 2004, p. 6.

⁷⁹ Chłoń 2000 p. 20.

⁸⁰ Offe 1991, p. 882; Seleny 1999, p. 488. Indeed, the SLD-PSL government had come to office in 1993 on the platform of restoring ‘fair’ pensions, and carried this theme throughout its launch of the pension reform. Chłoń et al. 1999, p. 12.

⁸¹ Hausner 2001, p. 217.

⁸² Müller 2001, p. 65. Fultz (2002, p.6) cites widespread uncertainty about the new pension system among Polish workers at the time of reform. Workers were given a one-time option to join the private pension system, but many reported that the rules of the system remained unclear, and many workers lacked access to the information that would help to assess whether participation in the funded system would be beneficial to them.

⁸³ Müller 1999b; Nelson 2000.

⁸⁴ Rodrik 1996, p. 10.

⁸⁵ Fultz 2002.

⁸⁶ At the time of Poland’s privatization, the financial sector was under-developed, and in particular the sectors that were essential for a private pension system were described by reformers as “practically non-existent.” Chłoń 2000, p.5; Chłoń-Domińczak and Góra, 2003; Fultz 2002, p. 5.

⁸⁷ Barr 1999; Fultz 2002; Gomulka 2000; Stanko 2003.

⁸⁸ Comparing balances in workers' accounts with their gross contributions revealed the bleak scenario of negative real returns in Poland that spanned from a high of -3 percent to a low of -14 percent from January 2000 to 2001. In Hungary, this ratio averaged -4.1 percent between 1998 and 2000. Fultz 2002, p. 7.

⁸⁹ For analysis of the public information campaigns in Poland and other reforming countries, see Chłoń and Mora 2004; Chłoń 2000.

⁹⁰ Chłoń 2000.

⁹¹ "Security through Competition: Performance Analysis of the Second Pillar" 2000, p. 105-108.

⁹² Chłoń and Mora 2004, p. 149.

⁹³ "Chile's Candidates Agree to Agree on Pension Woes" *New York Times*, January 10, 2006.

⁹⁴ Fultz and Ruck 2001; Orenstein 2000, p. 42.

⁹⁵ Fultz and Ruck 2001, p. 17; Orenstein 2000, p. 46; Rocha and Vittas 2001, p.9.

⁹⁶ Fidesz, for instance, abolished the compulsory movement into the private pension system for new entrants in the labor force, although this rule that was later reversed once again after the 2002 election when the Socialists and Free Democrats returned to power. The Socialists-Free Democrat coalition also raised the employee contributions to the private pension system were raised from 6 to 7 percent of wages – a planned increase (which was eventually to reach 8 percent) that had been eliminated by Fidesz. Fultz and Ruck 2001, p.17; Iwasaki and Sato n.d., p. 5-6.

⁹⁷ Párniczky 2003, c.f., Iwasaki and Sato n.d., p. 10.

⁹⁸ In Latvia, the NDC reform, which came into effect in 1997 (the private pillar was implemented in 2001) has been revised nine times, and was subject to a referendum in late 1999. Fultz and Ruck 2001, p. 17.