

DISCUSSION PAPER NO. 11

SOCIAL SECURITY SCHEMES IN SOUTHERN AFRICA

An Overview and Proposals for Future Development

Elaine Fultz and Bodhi Pieris, December 1999

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Foreword

The International Labour Organization (ILO) is a member of the United Nations family of organizations whose special mandate is the promotion of safe and decent work in all countries of the world. Unlike other specialized UN agencies, the ILO is a tripartite organization, and each country is represented not only by its government but also representatives of its workers and employers. Similarly, ILO services are provided to trade unions and employer associations as well as to governments. Over the eight decades since its establishment in 1919, the ILO has promulgated a large body of Conventions which deal with labour and social issues. The general thinking behind these Conventions is that “the failure of any nation to adopt humane conditions of labour is an obstacle in the way of other nations which desire to improve the conditions of their own countries.”¹ The Conventions establish benchmarks for all governments in their efforts to establish decent and safe working conditions, and can also discourage backsliding by member States.

In the global economy, the fulfillment of the ILO’s mandate requires new and innovative approaches. To better equip the organization to pursue its mandate in the next century, the ILO Director General has formulated four strategic objectives. These are:

- (i) promoting and realizing fundamental principles and rights at work;
- (ii) creating greater opportunities for women and men to secure employment income;
- (iii) enhancing the coverage of social protection for all; and
- (iv) strengthening tripartism and social dialogue.

These objectives will focus the ILO’s activities in coming years, providing complementary and mutually reinforcing approaches to ensuring decent work for all people.

In the mid 1990s, the ILO sought to move even closer to its constituents through a major decentralization of staff, resources, and authority. Under its Active Partnership Policy (APP), it established multi-disciplinary advisory teams in Africa, Asia, Latin America, and Central and Eastern Europe. These teams include specialists in areas such as employment promotion, workers’ and employers’ activities, statistics, training, small business development, labour standards, industrial relations, occupational safety and health, and social security. Demand driven, the teams respond to requests from ILO member states, trade unions, and employers associations for advice on policy issues; and they assist governments in the design and implementation of development programmes and projects. The Southern Africa Multidisciplinary Advisory Team (SAMAT), based in Harare, Zimbabwe, provides these services to nine countries of this sub-region.

As one of its services, SAMAT publishes a series of discussion papers on labour and social issues, of which this paper is a part. Through this series, SAMAT seeks to create an ongoing dialogue with workers, governments, and employers by suggesting applications of the ILO Conventions in a regional context, presenting ideas for new labour and social policy directions, and providing regional statistical data and comparisons which enable member states to learn from others’ experience. Since 1996, SAMAT has published ten such papers providing a regional perspective

¹ Preamble to the ILO Constitution.

on issues involving industrial relations, occupational safety and health, training, labour standards, labour market statistics, child labour, and social security. The third in the series dealing with social security, this paper complements previous analyses of regional employment injury schemes (paper # 7) and the social protection of migrant workers (paper # 3).

Prepared by Elaine Fultz and Bodhi Pieris, this paper provides an overview of the social security schemes in Southern Africa, describing their coverage of target populations, benefit levels, and financing. Three general scheme types are compared -- individual savings schemes, universal schemes, and social insurance -- and the latter is found to have several unique advantages in the regional context. However, the analysis also shows that, with few exceptions, all three scheme types are experiencing similar problems: a shortage of resources, low rates of coverage of target populations, weak subsystems for administration, and high operating costs. In considering solutions, the authors analyze several popular reform measures and, in the final section, offer their own recommendations. These include investing in public education and labour market information at an early stage in scheme development, coordinating social security administration with other public and private activities to achieve economies of scale, and placing more emphasis on the provision of short-term benefits (e.g., medical care, sickness, maternity benefits) which meet workers' most immediate needs for protection while avoiding the build-up of a large reserve fund which is vulnerable to misuse, inflation, and poor investment returns.

The authors express their warm thanks to officials in social security institutions across the region who provided information and/or verified the accuracy of statistics drawn from other sources. These include Patrick Bhembe, Manager of the Swaziland National Provident Fund; Uven Bunsee, Project Coordinator, Legislative Redrafting Project of the South African Unemployment Insurance Fund; Buckley Mwaba, Director Social Security in the Zambian Ministry of Labour and Social Security; Musonda Cheta, Project Manager, and Ian Lialabi, Financial Controller, at the Zambian National Pension Scheme Authority; Petronella Coetzee-Masabane, Deputy Director of Professional Social Services at the Namibian Ministry of Health and Social Services; Nunkoomar Deerpalsing, Social Security Commissioner in the Mauritian Ministry of Social Security and National Solidarity; Luis Herculano, Director General of the Mozambican Institute of National Social Security; E.D.B. Humba, Deputy Director General Operations at the Tanzanian National Social Security Fund; L.T.S. Matlhaphaphiri, Coordinator, Old Age Pension Scheme in the Botswana Ministry of Local Government, Lands and Housing; David Keendjele, Operations Manager at the Namibian Social Security Commission; and Rose Mbanje, Director of the Pensions and Other Benefits Scheme of the Zimbabwean National Social Security Authority. In addition, the authors benefitted from comments and suggestions on early drafts by several readers. These included Clive Bailey of the ILO Social Security Department in Geneva; Rene Loewenson of the Training and Research Support Centre, Harare; Frances Lund, Professor at the Department of Development Studies at the University of Natal, RSA; and Peter Peek, former Director of ILO/SAMAT.

For the record, the views expressed in the paper are the authors' and do not necessarily reflect those of the ILO. It is hoped that they will encourage new thinking about the development of social security schemes in Southern Africa, particularly their relation to national systems of governance and to economic development.



Ullrich H. Flechsenhar
Director
ILO/SAMAT

Overview

Southern Africa shows important signs of having entered a political and economic transition. After an era of one-party governments, authoritarian rule, and apartheid, most countries have made the transition to multi-party democracies; and the holding of elections is becoming a common practice.² In the economic sphere, governments are seeking to address low growth rates by opening markets, soliciting foreign investment, and undertaking structural adjustment programs to reduce the burden of public debts and deregulate business transitions. There are also indications of an emerging civil society, i.e., increased activity by trade unions and employers associations and the establishment of new organizations (e.g., women, church-related groups, disabled individuals, and operators in the informal sector) which participate more freely in political issues. While many major milestones lie ahead, the region seems to have turned a corner toward greater openness and competitiveness.

The strengthening of social security can contribute in important ways to this transition. In economic terms, social security schemes are needed to support workers who are displaced or lose employer-provided benefits as markets are opened to increased competition. Social security is also a key political issue for many new governments, which regard it as a tool for national unification, poverty alleviation, and securing popular support in more democratic political systems. These potential benefits have motivated considerable regional activity. Several governments are planning to launch new schemes, and others are restructuring existing ones.

While fueled by broad interest and offering many potential benefits, these efforts also face major obstacles. First, Southern Africa has an enormous unmet human need for social security but, at the same time, restricted resources. Large proportions of national populations live and work in conditions of poverty, and governments under the pressure of structural adjustment programs have few revenues for this purpose. Weaknesses in government capacity to collect tax revenues and ensure their use for intended purposes further exacerbates the problem. In addition, large numbers of jobs have been lost in national formal sectors; and in many countries the largest share of economic activity is now informal, with low wages and little or no social security. These conditions create a need for careful consideration of which needs are most pressing, what benefit levels are affordable, and how schemes can be expanded incrementally as economic development makes more resources available.

In addition, the design features of a social security scheme impinge on the economy in major ways, affecting productivity, labour mobility, work incentives, and labour costs. It is essential to consider these impacts in scheme design. Regional experience shows that the failure to do so can have serious consequences, i.e., costly and ineffective schemes which are a burden for workers and employers.

This paper provides information and ideas to support current policy discussions of social security in Southern Africa. Its intended audience is government officials, scheme administrators, and

² Since 1994, 12 out of 14 countries in the Southern African Development Community (SADC) have adopted or re-adopted multi-party systems based on popularly elected governments. SADC, *Human Development Report* (Harare: SAPES Trust, 1998), p. xvii.

leaders in the labour movement and business community whose close involvement in social security initiatives is essential to their success. Its objectives are three-fold: first, to provide countries with information on the approaches to social security taken by their neighbours and, in this way, to promote learning from regional experience; second, to determine which form(s) of protection are best suited to conditions in the region and to workers' needs; and third, to suggest an agenda for the reform and future development of social security schemes in Southern Africa.

The paper is organized in five chapters. Chapter 1 serves as background: it offers a working definition of social security, a typology of schemes, and a description of the ILO Conventions on Social Security. Chapter 2 then turns to Southern Africa, describing the national contexts in which social security schemes today operate and their main demographic, economic, and political features. Chapter 3 uses the typology presented earlier to analyze the three types of schemes which exist across the region -- mandatory savings schemes, non-contributory schemes, and social insurance -- comparing their coverage of target populations, the contingencies addressed, benefits, and financing mechanisms. Chapter 4 profiles a recent innovation in social security for the informal sector. Chapter 5, the conclusion, assesses the likely impact of several current reform measures from a regional perspective and presents the authors' recommendations.

The analysis supports two broad findings. First, it shows that most social security schemes across Southern Africa are experiencing a common set of problems: limited resources, narrow coverage of populations, the erosion of benefits by inflation, and high administrative costs, with the latter due to a combination of weak subsystems for public administration, the dispersion of target populations over large geographic areas, and a tendency still present in many Southern African countries to regard public posts as providing an entitlement to public resources. These problems impede the functioning of all three types of schemes to various degrees. Their pervasiveness suggests that, in this region, the political and economic environments in which social security schemes operate are more important in determining their success than any particular design feature. While debates in other parts of the world focus heavily on issues of scheme design -- e.g. full funding versus pay-as-you-go, pooled risk versus individual savings, and public versus private administration -- the main challenge for this region is to address cross-cutting problems which impede the delivery of all types of protection.

Second, along side their common difficulties, the schemes also exhibit some significant differences. Of the three types examined, only social insurance provides benefits which replace a worker's lost earnings to a specified extent and which are paid periodically throughout his or her period of need. In high-risk work environments in which most employees have low wages and limited savings, such protection provides a very great enhancement to economic security. In addition, social insurance avoids some problems observed with the other scheme types -- i.e., income and asset verification and the associated administrative costs (means tested schemes); the imposition of a major financial burden on the country's general tax revenues (universal schemes); and, if a scheme is partially funded or operated on a pay-as-you-go basis, the risks of erosion of reserves by inflation, misuse, and poor investment returns (national provident funds).

Yet only a few Southern African social insurance schemes have achieved these potential advantages, due to the cross-cutting problems described above. Because these problems are rooted in larger economic and political conditions, proposals to address them are necessarily long-term. The paper recommends:

- (i) in countries with little or no social security, making short-term benefits the starting point for building social insurance, since they address the most pressing needs of workers in high-risk environments, are more appealing to excluded populations, are more affordable and simpler to administer than pension schemes, and do not involve a large build-up of reserves which can expose the scheme to inflation, misuse, and poor investment returns. In countries which do not have national pension schemes, a short-term benefit scheme would also provide vital

- support for AIDS victims and their families;³
- (ii) devising arrangements for administration which integrate social security institutions more closely with other public and private agencies with similar mandates, thereby increasing economies of scale and operational efficiency; and
 - (iii) investing in the administrative subsystems needed to operate social insurance (e.g., birth and death records and basic employment data) as an early step in scheme development.

As for long-term benefits, current economic and political conditions make the structuring of pension schemes a more difficult task. After examining the trade-offs, the paper proposes a tiered benefit structure. This would include:

- (i) a social insurance benefit which provides modest levels of wage replacement, has a redistributive element which provides low income workers with a higher return on their contributions, applies to the broadest possible segment of the national work force (i.e., does not exclude those with private coverage), and is partially funded; to be complemented by
- (ii) tax and regulatory policies which encourage supplementation of this basic benefit by private occupational schemes and savings plans of various types, in which membership would be optional.

This approach would ensure that all covered workers have a minimum level of guaranteed protection, while providing higher income workers with a range of private options for supplemental retirement savings. At the same time, it would avoid the risks posed by a large build-up of public pension reserves.

³ While short-term sickness benefits are provided by employers in most countries, a social insurance scheme could lengthen the duration of coverage. In Namibia, for example, a worker becomes eligible for short-term sickness benefits after exhausting their rights to employer-provided benefits under the Labour Act. Benefits can then continue for up to two years.

Chapter 1

Social security: an introduction

1.1 A working definition

Defined more broadly in some contexts than in others, social security schemes are in essence mechanisms through which societies pool resources to protect themselves against certain risks, based on the principle of social solidarity. Defined narrowly, social security usually includes measures to address threats to members' earnings capacity, such as sickness, retrenchment, disability, and old age. Defined broadly, it can include the full range of preventive and ameliorative benefits that a society provides its members, including education, housing, and police protection. This analysis takes as its focus the narrower definition. Based on the ILO Conventions on Social Security, it will examine ...

... the protection which [Southern African] societies provide their members, through a series of public measures, against the economic and social distress that otherwise would be caused by stoppage or substantial reduction of earnings resulting from sickness, maternity, employment injury, unemployment, disability, old age, and death; the provisions of medical care; and the provision of subsidies for families with children.⁴

In this definition, the essence of social security is that it involves a *public measure* -- usually a statute, backed up by an institutional arrangement for implementation, either public or private -- that provides for the payment of certain *benefits* -- usually cash, though not always so -- in response to the occurrence of a *specified contingency* -- e.g., old age, sickness, disability, or unemployment -- which results in *increased financial need and/or lost earnings*.

It is also useful to note what this definition excludes. First, it does not capture traditional arrangements in which social security is provided through the extended family or the community. In many parts of Southern Africa, such arrangements are vital and effective; and their existence reduces the need for public measures. While referred to briefly in Chapter 4, they are not analyzed here. Second, because the definition deals exclusively with contingencies which result in lost earnings, it excludes measures to assist individuals whose earning capacity never developed, either because of physical or mental impairments or a blighted environment. While some analyses treat such measures as social security, these are classified here as training or economic development and are thus beyond the scope of analysis. Third, because the definition deals exclusively with public measures, it also excludes occupational benefits provided by employers on an optional basis. A key difference is that social security follows workers from job to job, eliminating the risk of loss of benefits as a consequence of changing jobs and, in this way, encouraging labour mobility.

1.2 The ILO Conventions on Social Security

Over the decades since its establishment, the ILO has promulgated a large body of Conventions which deal with labour and social issues. The general thinking behind these

⁴ ILO, *Introduction to Social Security* (Geneva, 1984), p. 2.

Conventions is that “the failure of any nation to adopt humane conditions of labour is an obstacle in the way of other nations which desire to improve the conditions of their own countries.”⁵ The Conventions establish benchmarks for all governments in their efforts to establish decent and safe working conditions and can also discourage backsliding. The Conventions on Social Security establish standards for the financing, benefit structure, and administration of social security schemes. In all, 30 Conventions and 15 Recommendations deal with these issues.⁶ Many of them were adopted early in the ILO’s existence since 1919 and have undergone a gradual process of revision, with narrow requirements being replaced by broader ones. As a result, the later Conventions embody a set of general principles. The most important of these are consolidated in the Social Security Minimum Standards Convention, No. 102 (1952), which brings together all nine branches of social security and sets a basic standard that should be attainable by all countries.

Convention 102 embodies six general requirements.

- First, it stipulates that protection should extend to at least half the national work force or 20 percent of residents.
- Second, it requires that benefits be provided for at least three of the nine contingencies in the ILO definition, at least one of which must be of a long-term nature (i.e., old age, disability, employment injury, or survivors benefits) or unemployment.
- Third, it calls for the cost of benefits and administration to be borne collectively by way of insurance contributions or taxation. This requirement excludes benefits which are financed exclusively by a single employer. The portion of contributions paid by workers should not exceed 50 percent.
- Fourth, it requires that cash benefits be periodic, paid throughout a contingency, and set to replace a specified portion of a worker’s lost wages. Exceptions are provided for minor employment-related injuries and for specific cases where the administering agency is satisfied that a lump-sum will be used appropriately.
- Fifth, it establishes minimum rates of income replacement, set at 50 percent of lost wages for a worker with a family who is injured on the job, 45 percent for unemployment and maternity, and 40 percent for a married worker who retires due to old age, a worker with family who retires due to disability, or the survivors of a deceased worker.
- Finally, it requires that the government assume general responsibility for the operation of a social security scheme. In cases where it delegates this authority, worker representatives should participate in scheme management or be associated with it in a consultative capacity.

The combination of comprehensiveness and flexibility in Convention 102 has given it vitality over time. While it has been supplemented by a number of Conventions providing higher standards, it continues to be the most frequently ratified Convention on Social Security.⁷

All countries in Southern Africa have ratified one or more Conventions on Social Security, but none has as yet ratified Convention 102. This is due in large part to the limited development of social security in the region.

⁵ Preamble to the ILO Constitution.

⁶ These are out of a total number of 182 Conventions and 190 Recommendations.

⁷ The Conventions providing higher standards include number 103, Maternity Convention (1952); number 121, Invalidity, Old Age, and Survivors’ Benefit Convention (1967); number 130, Medical Care and Sickness Benefits Convention (1969); and number 168, Employment Promotion and Protection Against Unemployment Convention (1988).

1.3 Scheme types

It is convenient to classify social security schemes in three broad categories: mandatory savings schemes, non-contributory schemes, and social insurance.⁸ While some schemes exhibit mixed characteristics, these categories capture the most important distinctions among schemes as they exist around the world. The general features of each category are as follows:

With *mandatory savings schemes*, a government enacts a requirement that workers set aside a portion of their monthly earnings in an individual account. These accounts may be administered publicly as national provident funds or by private firms under government supervision (e.g., the Chilean model). Under the first option, the employer matches the worker contribution, while under the second only the worker contributes. The savings are generally targeted toward long-term contingencies. When the worker reaches a specified age, retires, dies, or becomes disabled, this amount is refunded with interest. It may be paid as a single lump sum, used to purchase an annuity, or taken gradually in a series of phased withdrawals. A distinguishing feature of this approach is that it involves no pooling of risks or resources across the work force. Thus, what a worker receives is equal to what he or she contributed, plus interest, minus administrative expenses.⁹ In this sense, these schemes are “fully funded,” meaning that all benefit obligations to a worker are financed by contributions which he or she has paid in advance.

In *non-contributory schemes*, the government establishes a system of uniform benefits for all residents of the country. These are normally financed by an annual appropriation of tax revenues from the treasury. The schemes are also of two general types, universal and means-tested. The former provides benefits to all citizens or residents who meet program eligibility criteria -- e.g., old age, disability or orphanhood -- without regard to the individual’s income, assets, or earnings history. This means that benefits are paid not only to those who were previously working in the formal sector but also to informal sector workers who experience an insured contingency and to the unemployed. The second type, means-tested schemes, has a narrower focus, protecting only the subset of these individuals who are financially needy. Reflecting the financial burden which these schemes pose for governments, non-contributory benefits are frequently set at low levels. Moreover, many countries which originally established universal schemes have restructured them to require means-testing, a measure which has proven only partially successful in reducing burdensome costs.

Social insurance schemes pool risks and resources across the covered population based on the principle of social solidarity. As a result, some workers receive more in benefits than they pay in contributions (e.g., a worker with children who is disabled at a young age), while others receive less (e.g., a worker who dies just after retiring with no dependent family members). What all workers receive is a guaranteed entitlement to replacement of a set portion of their wages if they experience an insured contingency. Eligibility and benefit levels are determined by the individual’s work history and earnings (exceptions apply to medical care and subsidies for children), and benefits are paid without reference to financial need or unearned income (e.g., interest or dividends on investments). These schemes are typically financed by contributions from employers and workers and may also include a subsidy from the state. They can be either fully funded like mandatory savings schemes, financed on a pay-as-you-go basis -- i.e., current contributions are used to pay current benefits --

⁸ ILO, “Public and Private Pension Schemes,” Training Module 1, p. 3.

⁹ In national provident funds, the deduction of interest is not actually made but is taken into account in determining the rate of interest applied to member accounts.

or partially funded -- i.e., a middle position in which a reserve is built up but equals less than the full future liability of the scheme. Partially funded arrangements offer governments considerable flexibility: they can be structured so that reserves accumulate at a rate which does not exceed a country's capacity to absorb investments, and they enable the government to schedule contribution increases on a predictable basis.

Table 1 Typology of social security schemes

SCHEME TYPE	COVERAGE	CONTINGENCIES ADDRESSED	BENEFITS	FINANCING
Mandatory savings scheme (National provident fund or privatized scheme)	Formal sector workers	Long term (principally retirement)	Refund of contributions, plus interest earned, minus administrative expenses	Contributory, fully funded
Non-contributory (Universal or means-tested)	All citizens or residents	Long term (e.g., young age, old age, widowhood, disability)	Uniform amounts for all citizens or residents	General revenues, pay-as-you-go
Social insurance	Formal sector workers	Both short term (maternity, sickness, unemployment) and long term (old age, disability, survivors)	Earnings related, based on pooled risk, and paid throughout an insured contingency	Contributory (with possible state supplement), fully funded, pay-as-you-go, or partially funded

With long-term social insurance benefits, the choice among financing options is complicated by a general tendency for scheme costs to rise over time. This rising cost curve applies to virtually all pension schemes and is driven by several factors.¹⁰ Given this curve, the choice among financing options involves trade-offs which are unavoidable and difficult to resolve. On the one hand, full funding of a pension scheme results in rates of contribution which are stable over time. Stability is achieved, however, at the cost of (i) the build-up of a large national reserve in the scheme's early years which can make it vulnerable to inflation, misuse, and poor investment returns, and (ii) a long lag time, in the order of three to four decades, between the establishment of the scheme and the point at which it can begin to pay full benefits. This lag prevents the first generation of workers from benefitting significantly from a new scheme.

Pay-as-you-go and partial funding pose a different set of trade-offs: on the positive side, they can avoid a large accumulation of reserves and the vulnerability to inflation, misuse, and poor financial performance which it creates. In addition, they can begin to make payments in a few years, so that the current generation of workers derives benefit from a new scheme. These advantages are achieved, however, at the cost of contribution rates which must rise over time. See Table 2.

¹⁰ These factors are three-fold: (i) the lengthy periods of contribution that are required to qualify for pensions mean that few workers will receive benefits in a scheme's early years; (ii) the credits provided in pension benefit formulas for additional years of work means that those who retire later in the scheme's life will generally receive higher benefits; and (iii) the gradual aging of national populations in developed countries, caused by reduced birth rates and improvements in medical care, means that the number of scheme beneficiaries will expand over time.

Table 2 Pension financing trade-offs

FINANCING METHOD	ADVANTAGES	DISADVANTAGES
Full funding	Stable contribution rate	Large fund build-up creates vulnerability to inflation, misuse, and poor financial performance
	If invested wisely, scheme reserves can help to foster economic development	First generation of workers will derive limited benefits from the scheme
Pay-as-you-go or partial funding	Smaller reserve fund lessens scheme vulnerability to inflation, misuse, and poor financial performance	Rising contribution rate
	First generation of workers can derive full or nearly full benefits	Because reserve fund is smaller, reduced potential to use reserves for economic development

The resolution of these trade-offs has sparked considerable public controversy in recent years. In developed countries, the need to increase contribution rates as pay-as-you-go pension schemes mature has caused some to question the viability of this mode of financing. Other analyses, however, indicate that these systems can weather the demographic shift now underway through a combination of reforms. Still other studies show that workers become more vulnerable to economic shocks under fully funded private savings schemes, the main alternative being advocated by critics of pay-as-you-go systems, than they are to demographic shifts under traditional social insurance schemes.

The resolution of these trade-offs depends heavily on the economic and demographic context in which a pension scheme operates, and its resolution in Southern Africa will constitute one major focus of this analysis. Chapter 5 returns to this issue and, drawing on information presented in the main text, makes a proposal for resolving these trade-offs from a regional perspective.

Chapter 2

The context: Southern Africa

The relationship between a social security scheme and its environment is a dynamic one in which influences flow in many directions. On the one hand, the economy determines the level of resources available for social security and their distribution among the population. Cultural factors determine the extent of national solidarity and citizens' consequent willingness to pool risks and resources in a social security scheme. Government plays a major role in delivering social security and/or overseeing its delivery, thus influencing the costs and operational efficiency of a scheme. At the same time, social security exerts a reverse influence in shaping these contextual variables, affecting economic productivity, rates of poverty, the health and longevity of the work force, and the popular support enjoyed by governments. These multi-directional influences make it important to begin a regional analysis of social security schemes by considering the demographic, economic, and political features of the countries in which they operate.¹¹

2.1 Economic features

The eleven countries of Southern Africa analyzed here comprise about 130 million people, approximately half of which are of working age (between 15 and 60).¹² Like sub-Saharan Africa generally, most economies have a small formal sector, a much larger agricultural sector engaged in subsistence farming, and an urban informal sector which varies significantly in size from country to country and consists mainly of self-employed individuals. Overall, formal employment comprises just over a fifth of the working age population, totaling about ten million workers. Of the remaining population, about 75 percent are engaged in small holder farming, while 25 percent live and work in urban settings.

2.1.1 Limited productivity

Southern Africa is well endowed with national resources, including minerals (gold, diamonds, uranium, copper, and chrome), water, wildlife, agricultural land, and human resources. However, economic activity is mostly agricultural (maize, tea, flowers, tobacco, coffee, and cattle) with little processing of raw materials and or value added. This is largely due to limited skill development and a low technological base. During 1980–95, annual economic growth averaged about three percent.¹³ See Table 3.

¹¹ Unless otherwise indicated, statistics in this section are drawn from the *SADC Human Development Report*, Harare: SAPES Trust, 1998.

¹² The countries under analysis are Botswana, Lesotho, Malawi, Mauritius, Mozambique, Namibia, South Africa, Swaziland, Tanzania, Zambia, and Zimbabwe. This group comprises a large subset of the Southern African Development Community (SADC), which also includes Angola, the Democratic Republic of Congo, and Seychelles, bringing its total membership to 14.

ILO Convention 168 stipulates that the minimum age for leaving school is 15 or, in the alternative, the age at which attendance ceases to be compulsory. ILO Recommendation 162 suggests 60 as the age for leaving employment.

¹³ Annual GNP growth rates during 1980–95 were Botswana, 8.8 percent; Lesotho, 3.4 percent; Malawi, 2.4 percent; Mauritius, 5.7 percent; Mozambique, 1.1 percent; Namibia, NA; South Africa, 1.3 percent; Swaziland, 4.2 percent; Tanzania, NA; Zambia, 0.6 percent; and Zimbabwe, 2.8 percent. UNDP, *Human Development Report*, 1998, p. 184.

Table 3 National gross production, per capita production, and growth

COUNTRY	GNP (US\$–1997)	REAL GNP PER CAPITA (PPPS–1997)	ANNUAL GNP GROWTH RATES (1991–97)
Botswana	–	–	5.1%
Lesotho	1.4 b.	2 480	6.6%
Malawi	2.3 b.	700	4.3%
Mauritius	4.3 b.	9 360	5.3%
Mozambique	1.7 b.	520	6.2%
Namibia	3.6 b.	5 440	4.3%
South Africa	130.2 b.	7 490	1.3%
Swaziland	–	–	2.4%
Tanzania	6.6 b.	NA	2.8%
Zambia	3.6 b.	890	0.5%
Zimbabwe	8.6 b.	2 280	2.6%

Sources: GNP and per capita GNP figures are from the World Bank, *World Development Report*, 1998, p. 190–191. Average annual GNP growth rates are from the SADC *Human Development Report*, 1998, p. 29.

However, this average masks wide variation from year to year and country to country. The former is due in large part to varying rainfall. In Malawi, for example, where the agricultural sector strongly dominates the economy, the growth rate was 7.8 percent in 1991, –7.9 percent in 1992, 10.8 percent in 1993, and –11.6 percent in 1994. As for country to country differences, the region can be divided into three groups, with Botswana, Lesotho, Mauritius, Mozambique, and Namibia at the upper end of the growth continuum; Malawi, Tanzania, Swaziland and Zimbabwe in the middle; and the lowest growth is occurring in South Africa and Zambia. It is significant that South Africa, historically the growth engine of the region, has slipped to the near bottom of the growth scale.

2.1.2 Inflation

Inflation is a persistent feature of most Southern African economies, though it has declined somewhat in recent years. During 1985–95, it averaged 25 percent per year for SADC as a whole. As shown in Table 4, national inflation levels vary widely, with Zambia at the high end of the spectrum and Mauritius at the low end.

Table 4 Average inflation and range (%), 1991–97

COUNTRY	AVERAGE	RANGE
Botswana	10.5	8.9 – 16.1
Lesotho	10.1	7.9 – 18.4
Malawi	22.8	8.2 – 83.3
Mauritius	5.7	4.6 – 10.5
Mozambique	43.5	24.3 – 70
Namibia	9.6	8.2 – 17.7
South Africa	9.0	7.4 – 15.3
Swaziland	8.4	6.5 – 13.7
Tanzania	22.6	16.1 – 34.1
Zambia	58.1	18.6 – 185.2
Zimbabwe	23.9	18.9 – 42.1

Source: SADC *Human Development Report*, 1998, p.33.

2.1.3 High and increasing informal sector employment

Over the past two decades, population increases have regularly exceeded the growth of the labour force in most countries. Among the countries for which statistics are available, only Mauritius and Lesotho have expanding labour forces. In several countries (e.g., Malawi, Zambia, Lesotho), the informal sector now provides the largest number of jobs. See Tables 5 and 6. While the conditions of informal sector work vary widely, it is generally characterized by low productivity, underemployment of workers, and an absence or near absence of formal social security.

Table 5 Average annual growth in population and employment, 1990–97

COUNTRY	POPULATION GROWTH %	LABOUR FORCE GROWTH %
Botswana	–	–
Lesotho	2.1	2.4
Malawi	2.7	2.4
Mauritius	1.1	1.7
Mozambique	3.8	3.3
Namibia	2.6	2.5
South Africa	–	–
Swaziland	–	–
Tanzania	3	2.8
Zambia	3	2.8
Zimbabwe	3.3	2.3

Source: World Bank, *World Development Report*, 1998, p.194–195.

Table 6 Composition of labour markets

COUNTRY	LABOUR FORCE AS % OF POPULATION 1995	EMPLOYMENT AS % LABOUR FORCE 1995	INFORMAL SECTOR AS % EMPLOYED
Botswana	44	37	–
Lesotho	41	–	62
Malawi	48	12	83
Mauritius	42	90*	–
Mozambique	52	16	85
Namibia	41	30	–
South Africa	39	52	17
Swaziland	36	27	–
Tanzania	51	–	–
Zambia	41	13	72
Zimbabwe	46	25	8

Sources: The first column is from the United Nations Development Programme, *Human Development Report*, 1998, p. 164–165; and the final two columns are from composite sources and represent different recent years. They are cited in ILO/SAMAT Policy Paper No. 5, *Industrial Relations in Southern Africa: the Challenge of Change*, 1998, p. 11–12. Starred figure is from the *Yearbook of Labour Statistics*, ILO, 1998, p. 118.

2.1.4 Skewed income distributions

Per capita income also varies widely, from highs of US\$9,360 in Mauritius and US\$7,490 in South Africa to lows of US\$890 in Zambia and US\$700 in Malawi.¹⁴ Within countries, the distribution of income is highly skewed, with the richest 20 percent of populations controlling a large slice of national income: about 50 percent in Zambia and Tanzania; 60 percent in Lesotho, Botswana, and Zimbabwe; and nearly 70 percent in South Africa. At the other end of the income continuum, 30 to 40 percent of the labour force is either underemployed in the urban informal sector or engaged in subsistence agriculture. Reflecting the poor conditions in these sectors, national poverty rates are also in the range of 30 to 40 percent. A large portion of subsistence farmers live in drought-prone areas without basic public services such as electricity, running water, or sewage. As there has been little land redistribution since independence, the former settler population continues to control the most productive farm lands. Land per capita among whites compared to blacks is 146 times in Zimbabwe, 300 times in Namibia, and 480 times in South Africa. See Table 7.

Table 7 Distribution of income and rates of poverty

COUNTRY	POPULATION IN POVERTY	SHARE OF INCOME OR CONSUMPTION, LOWEST 10% POPULATION	SHARE OF INCOME OR CONSUMPTION, HIGHEST 10% POPULATION
Botswana	0.27	–	–
Lesotho	0.26	0.9	43.4
Malawi	0.48	–	–
Mauritius	0.12	–	–
Mozambique	0.49	–	–
Namibia	0.3	–	–
South Africa	–	–	–
Swaziland	–	–	–
Tanzania	0.4	2.9	30.2
Zambia	0.37	1.5	31.3
Zimbabwe	0.25	1.8	46.9

Sources: Income distribution figures are from the World Bank, *World Development Report*, 1998, p. 198–199. Poverty statistics are from the United Nations Development Programme, *Human Development Report*, 1998, p. 26.

2.2 Demographic features

2.2.1 Uneven population densities

The region's largest country, South Africa, has about 39 million people, while five other countries -- Botswana, Mauritius, Namibia, Lesotho, and Swaziland -- have less than two million each. Population density ranges from a high of 1,400 people per square mile in Mauritius to 212 in Malawi, the second densest country, to lows of six and four people per square mile, respectively, in Botswana and Namibia. High population densities place a strain on land and resources in some countries, while in others thin and dispersed populations pose challenges for the provision of public services. The latter features also pose a major barrier for the collection of social security contributions and the delivery of benefits.

2.2.2 Low life expectancies

Regional life expectancies are today among the lowest in the world. During the 1960s and 70s, most countries achieved large increases in life expectancy through investments in

¹⁴ The World Bank, *World Development Report*, 1998, p. 190–1.

health care and sanitation. Between 1960 and 1995, the average life expectancy for SADC increased by 11 years, to age 52.¹⁵ However, this trend masks recent declines due to the AIDS epidemic. Between 1990 and 1995, Zambia lost 12 years; Botswana, eight; and Malawi, seven. As shown in Table 8, these losses equal or surpass the previous gains. High HIV infection rates are likely to worsen this trend in coming years. Among SADC's economically active population, infection rates are estimated at 12 percent. In countries with the most severe infection, i.e., Zimbabwe and Botswana, these rates are estimated at around 25 percent. Overall, 29 percent of the region's population is projected to die of various causes before the age of 40, compared to 20 percent for all developing countries. The figures are highest for Mozambique (38 percent), Zambia (42 percent), and Malawi (46 percent).

Table 8 Slow progress and setbacks in life expectancy

COUNTRY	1970 LIFE EXPECTANCY AT BIRTH (YEARS)	1995 LIFE EXPECTANCY AT BIRTH (YEARS)	PERCENTAGE CHANGE
Botswana	52	52	0%
Malawi	40	41	+ 2%
Zambia	46	43	- 8%
Zimbabwe	50	49	- 3%

Source: United Nations Development Programme, *Human Development Report*, 1998, p. 22.

2.2.3 High birth rates

Most Southern African countries are young by international standards, with nearly half the population below age 15.¹⁶ This is much higher than the portion for all developing countries, 31 percent. At the other end of the age spectrum, the elderly constitute less than five percent of most regional populations, much lower than the average for developed countries, around 15 percent.

2.2.4 Differing patterns of retirement

Early retirement is traditional in Southern Africa's civil service as well as in certain parts of the private formal sector. Here many workers retire from employment between age 50 and 55, frequently returning to their home village to farm. Government retirement funds and national provident funds generally pay benefits to workers who leave employment between age 45 and 55. The earliest retirement ages are in Botswana, where civil servants can retire as early as age 40, and in Swaziland, where the national provident fund pays lump-sum benefits to retiring workers at age 45.

For those who have no pensions or meager ones, by contrast, retirement from work is often not a realistic option. This population continues to work so long as they are physically able, typically until age 60 or 65.

¹⁵ This ranges from a high of 71 in Mauritius to a low of 41 in Malawi.

¹⁶ The portions are 43 percent for Botswana, 41 percent for Lesotho, 48 percent for Malawi, 30 percent for Mauritius, 46 percent for Mozambique, 37 percent for South Africa, 46 percent for Swaziland, 47 percent for Tanzania, 50 percent for Zambia, and 44 percent for Zimbabwe. *World Almanac*, 1996.

2.3 Governance

2.3.1 Signs of emerging democracy

Following their independence in the 1960s and 70s, a number of Southern African countries adopted systems of one-party rule. Their new leaders took control with high idealism and a strategy of central economic planning, and they invested heavily in social infrastructure such as education, health care, water resources, and sanitation. However, they were also inefficient and allocated jobs and public resources on the basis of family and tribal affiliation. As time passed, many adopted authoritarian styles of governance and amassed considerable personal wealth.

During the 1970s and 80s, regional economic performance declined, leading most governments to borrow heavily from international lending institutions. The lenders used their leverage to require reductions in public spending and structural adjustment programs.¹⁷ Along with the region's economic problems, these resulted in curtailments of public service. Under the combination of growing internal dissatisfaction and external pressure, most of the governments held national elections in the early 1990s, in many cases for the first time since independence. Single party regimes were replaced by multi-party democracies in all but two countries.¹⁸

These new governments appear more tolerant of political diversity than their predecessors, and there are signs that civil society is beginning to emerge as varied interest groups -- e.g., women, trade unions, employers, churches, informal sector organizations, and the disabled -- begin to become active politically. However, this transition is at an early stage. Most opposition parties are still weak, disorganized, and poorly funded; and the new organizations of civil society lack resources and training, limiting their impact and effectiveness. In many countries, biased election rules give the majority party a high portion of representation.¹⁹

2.3.2 Weak subsystems for public administration

With some important exceptions, the basic subsystems of public administration in Southern African countries do not operate effectively -- e.g., systems for issuing licenses, recording births and deaths, revenue collection, appeals of government decisions, and the issuance of unique national identification numbers. Moreover, structural adjustment programs have resulted in a decline in public services, especially medical care, and in rising user charges such as school fees. In many countries, basic health and sanitation services have not been extended outside urban areas. In 1998, an estimated 40 percent of SADC's population has no access to health care; and 50 percent had no access to sanitation facilities.

Despite the region's recent political transition, many government bureaucracies continue to operate in an unresponsive manner. This reflects a view still prevalent in many Southern African countries that public positions convey to their holders an entitlement to public resources. Given this perception, organized pressure to increase government efficiency

¹⁷ These policies are being reconsidered by international financial institutions during the 1990s, and they are now placing greater emphasis on establishing and maintaining developing countries' social and administrative infrastructure in the context of structural adjustment.

¹⁸ In 1990, only one country, Botswana, had a multi-party system of government. In 1994, all countries except Zimbabwe and Swaziland had such systems. SADC (1998), p. 2.

¹⁹ For example, winner-take-all election rules were a key cause of the civil uprising in Lesotho in 1998. Lesotho's national elections in 1998 resulted in the Lesotho Congress for Democracy receiving 61 percent of the popular vote but 78 percent of Parliamentary seats; the Basotho National Party received 25 percent of the national votes but only one seat; the Basotho Congress Party received 11 percent of the votes but no seats; and other parties received three percent of the votes but no seats.

and improve public services is rare. Absent such pressure, public officials are often slow and unresponsive and, in many cases, demand personal compensation from those who seek their help.

Together these conditions create a great need for social security in Southern Africa. Large segments of the population live and work on the edge of poverty; formal sector employment is limited and declining; inflation erodes incomes and savings; and the AIDS epidemic is reducing national productivity and leaving a generation of children without parental care. At the same time, low productivity means that social security is difficult to finance; and weak and undeveloped systems of governance pose major structural barriers to efficient administration. These constraints pose enormous challenges to those charged with delivering social security to the region's people, particularly to the groups which are most in need. The following chapter describes the social security schemes which exist today and assesses the results they have achieved operating within these constraints.

Chapter 3

Social security schemes in Southern Africa: a comparative assessment

Though social security is not extensively developed in Southern Africa, a variety of scheme types exist across the region. This chapter analyzes them according to four key features -- who is protected, which contingencies are addressed, the benefits provided, and methods of financing. The analysis is organized to correspond to the typology of schemes presented earlier -- first mandatory savings schemes, then non-contributory schemes, and finally social insurance. Within each category, schemes are described in terms of the four features of interest.

3.1 Mandatory savings schemes

In Southern Africa, mandatory savings schemes are structured as national provident funds. They exist in three countries, Swaziland, Tanzania, and Zambia, though all are at various stages of conversion to pension schemes.²⁰ All three funds are administered by parastatal organizations with tripartite boards of directors.²¹ Scheme administration is largely autonomous, with little collaboration with government in eligibility determination, benefit payments, or enforcement activities. Both workers and employers are required to make monthly contributions to a fund account in the worker's name, equal to a fraction of his or her earnings. When the worker experiences an insured contingency, these revenues plus interest and minus administrative expenses are refunded as a lump-sum payment.²²

3.1.1 Who is protected

Fund membership generally consists of employees of large and medium-sized firms.²³ Thus, it extends to only a small portion of all the workers in a country and varies significantly depending on the size of the formal sector in relation to the informal one. In Swaziland, with a working age population of 325,000 and a formal sector of 157,000, the National Provident Fund covers 64,000 workers; in Tanzania where the working age population is 15 million and the formal sector is 1,000,000, membership prior to conversion was 400,000; and of Zambia's 3.3 million labour force, membership is 270,000 workers, or about 65 percent of the formal sector. See Table 9.

²⁰ In Tanzania, the government formally converted the TNPF to a pension scheme as of 1 July 1998 but will continue for five years thereafter to offer workers a choice between a lump-sum payment and a pension. In Zambia, after conversion to a pension anticipated in mid 1999, the ZNPF will be designated the National Pension Scheme Authority (NAPSA). In Swaziland, the government hopes to approve conversion legislation before the year 2000.

²¹ This is a recent change in Tanzania where, prior to 1998, the board consisted of government representatives.

²² The deduction of administrative expenses is usually not actually performed literally but is rather taken into account in determining the interest rate applied to member accounts. In Swaziland, the lump sum is convertible to an annuity at the employee's option; but only a handful of employees have chosen this option over the life of the fund.

²³ Zambia excludes central and local government workers; Swaziland excludes government workers, teachers, domestic servants, university professionals, and non-citizens; and Tanzania excludes pensionable workers in parastatals, universities, the teaching service, and other public agencies such as the defense force, police, and prison service. Zambia allows for optional membership by self-employed individuals, though very few have chosen to participate.

Table 9 Coverage of work forces by national provident funds
(and their successor social security institutions)

COUNTRY	WORKING AGE POPULATION	FORMAL SECTOR WORK FORCE	FUND MEMBERSHIP
Swaziland	325 000	157 000	64 000
Tanzania	15 000 000	1 000 000	400 000
Zambia	3 300 000	386 000	270 000

An additional factor which restricts coverage is the national provident funds' difficulty in enforcing the contribution requirement. While no statistics are available on the numbers of covered employers which are not registered, significant portions of those which are do not contribute regularly. At the ZNPF, 30 percent of registered employers were seven months or more behind in payments during 1996; at the SNPF, the payment delinquency rate was 20 percent in 1997; and arrears at the TNPF ran at about 15 percent in 1995/6.

3.1.2 Which contingencies are addressed

The funds offer primary protection against contingencies which create a need for long-term income replacement, i.e., of old age, disability, and death (survivors benefits). Benefits for retirement are paid at age 55 in Tanzania, age 50 in Zambia (45 for those who joined the scheme before 1973), and age 45 in Swaziland. Those who continue working can collect their lump sum at age 55 in Zambia (50 for those who joined before 1973) and 50 in Swaziland. In addition, Tanzania allows for withdrawal of a worker's entire balance upon extended sickness or unemployment and, for female employees, upon marriage or pregnancy. In Zambia, workers may withdraw balances for purchase of a home; qualified female workers may receive maternity grants; and all may receive funeral grants (both types of grants are paid from a general reserve fund and not deducted from members' accounts). Both Swaziland and Zambia allow for full withdrawals when a worker emigrates.

Though national provident funds are designed to address long-term contingencies, many members actually withdraw their savings early and use them for short-term expenditures. In Tanzania, more than 70 percent of contributions were withdrawn on account of unemployment in recent years, providing only meager refunds on average for retirement.²⁴ In Swaziland, withdrawals for retirement at age 45 have risen sharply in recent years; and scheme officials believe that many workers retire in order to collect the benefit and then return to work immediately.²⁵ In Zambia, withdrawals for retirement at age 45 (for members joining before 1973) and home ownership constitute over half of ZNPF annual benefit expenditures.²⁶

Officials of all three funds cite anecdotal evidence in asserting that, once paid, benefits tend to be exhausted rapidly. This view is consistent with the single survey that examined the use of provident fund benefits systematically, undertaken by the Ghanaian NPF. It showed that payments were used primarily to: (i) improve a family home, (ii) marry a second or third wife, (iii) pay for litigation (land cases, inheritance, chieftaincy disputes, or family conflicts), (iv) rehabilitate a farm; or (v) set up a business (with a low success rate).²⁷

²⁴ ILO, *Tanzania: Report to the Government on the Development of Social Security: Review of Policy Recommendations*, 1996, p. 9.

²⁵ Between 1993 and 1996, the benefits paid for age rose from 2.3 to 6.7 million Emalangeni, while benefit for retirement rose from 2.3 to 4.2 million Emalangeni. Kingdom of Swaziland, *Twenty-third Annual Report of the Swaziland National Provident Fund*, 1996-7, p. 21.

²⁶ ZNPF, *29th Annual Report of the Zambia National Provident Fund*, 1994-5, p 7.

3.1.3 Benefit levels

A striking feature of Southern African provident funds is their very low benefit levels. In Zambia, the average payment upon retirement was approximately K150,000 (about US\$61) in 1996, or about three months pay at the minimum wage; and the funeral and maternity grants are K10,000 (about US\$4).²⁸ In Tanzania, the average benefit at retirement was approximately 50,000 Shillings (US\$70) in 1995, equal to two months average wages.²⁹ In Swaziland, the average payment in 1997 was somewhat higher at 3,000 Emalangeni (about US\$480), or about five months pay at the minimum wage in the retail and manufacturing sector.³⁰ These low benefits are largely the result of financial difficulties, described below.

3.1.4 Financing

Benefits at all three funds are financed entirely from worker and employer contributions and the interest they earn. In Swaziland, the contribution rate is five percent for workers and employers, each, on earnings up to E500 a month (US\$80). In Tanzania, it is ten percent of monthly earnings, each, for employers and workers, with no wage ceiling. (Since the conversion, eight percent of this is being targeted for a partially funded pension scheme; and the government plans to use the remainder to fund new periodic benefits for maternity and employment injury.) In Zambia, the contribution rate is 3.5 percent, each, on monthly earnings up to K150,000 (US\$62). The government has announced that it will increase the rate to five percent as part of the conversion. Since the funds simply refund accumulated contributions and interest, there are no unfunded obligations to members and no deficits are possible in theory.³¹ In Southern Africa, this approach has produced low or negative returns in recent years due to three factors.

The first is high inflation. During 1985–95, inflation in the SADC region averaged 25 percent per year. In Swaziland, the average was about 15 percent; in Tanzania, it was 32 percent; and in Zambia, it was 92 percent.³² The wage ceiling on contributions was adjusted only once during this period in Zambia; and in Swaziland, it was held constant throughout. As a result, contributions to both funds declined in real terms. Calculations for the ZNPF show that, during 1993–97, contributions in unadjusted Kwacha increased from 3 billion to 16 billion; but in inflation-adjusted Kwacha they actually fell from 3 to 2.6 billion.³³ Given the financing system for provident funds, such losses resulted in commensurate reductions in real benefits.

A second, related problem was low investment returns, due in part to the funds' heavy concentration in real estate with high maintenance costs, rates of tenant turnover, and

²⁷ Dei, Henry, "Meeting the challenge of conversion: Ghana's provident fund becomes a pension scheme," in *International Social Security Review*, Vol 50., 2/97, p. 65.

²⁸ ILO, *Republic of Zambia: Report to the Government on the Strengthening of Social Protection, Volume II, Planning and Legislation*, 1998, p. 3.

²⁹ ILO, *Tanzania: Report to the Government on the Development of Social Security: Review of Policy Recommendations*, 1996, p. 3.

³⁰ Estimate provided by Swaziland NPF.

³¹ A minor qualification is required for the ZNPF, which during the early 1990s credited member accounts at a higher rate of interest than the Fund earned. This strategy was undertaken in an effort to compensate for past losses due to inflation. As shown in Table 13, it was short-lived.

³² SADC (1998), p. 159, and ILO, *Swaziland: Report on the Actuarial study for the Development of a National Pension Scheme*, 1992, p. 13.

³³ ILO, *Republic of Zambia: Report to the Government on the Strengthening of Social Protection, Vol. IIIA, Actuarial Valuation of the Proposed National Pension Scheme*, 1998, p. 6–8.

delinquent rents and, in part, to required investments in government securities.³⁴ In a 1994 report to the ZNPF's tripartite board, the director explained:

As an organization, the [ZNPF] has grown in establishment over the last 25 years, but the financial strength of the organization was being eroded through political command decisions rather than professional management. Since its inception, the [ZNPF] was directed to invest in unprofitable real estate in outlying districts and in government loans at fixed interest rates. Investment in these areas produced lesser income year after year. The cumulative effect of income lost in one year to the next was to reduce the value of contributors' funds in real terms. Real estate investment in major cities, however, had appreciated in value, but did not produce significant cash returns as the rentals were kept unreasonably low for a long time. Hence the contributors' accounts suffered a substantial loss of income.³⁵

In addition, the investment policies of all three funds were restricted by law. The TNPF was required to invest 75 percent of income in government instruments, while for ZNPF the required ratio was 50 percent. The Swaziland government prohibited the SNPF from making foreign investments and required it to obtain approval for investments exceeding ten percent of assets. With few private investment options in Swaziland, the former requirement served to channel reserves into government instruments.

A third contributing factor is high administrative costs. In Tanzania, administrative spending averaged 25–30 percent of members' annual contributions during 1985–95; in Swaziland, about 40 percent; and in Zambia, between 65 and 110 percent.³⁶ These costs are driven by high staffing levels and employee benefits, both of which rose under state-managed economies in the periods following national independence. Today personnel costs comprise approximately 50 percent of total administrative spending in Swaziland, 48 percent in Tanzania, and 70 percent in Zambia, compared to a 20 percent standard for the region's private insurance industry.³⁷ In Zambia, fund personnel stands at about 1,100 -- down from 1,600 in the late 1980s,³⁸ but still four times the staff of the more recently established Zimbabwean national pension scheme (233).³⁹ As for employee benefits, the ZNPF provides a generous package for senior and mid-level management.⁴⁰ The cost of these in-kind benefits more than doubles salary payments.

³⁴ In its Annual Report for 1996–7, the Swaziland National Provident Fund described its efforts to reduce real estate management costs through a change in posture toward tenants: "The main emphasis has been to change the attitude from being friendly to becoming aggressive." See p.26.

³⁵ ILO, *Republic of Zambia: Report to the Government on the Strengthening of Social Protection, Vol. 5, Accounting and Financial Management*, 1998, p.17–18.

³⁶ In Tanzania, the NPF's method of measuring administrative spending excludes depreciation and notational rent on NPF-occupied buildings. Under this procedure, costs were 21 percent of contribution income in 1991–2. Adding depreciation and notional, the expense ratio would be higher than 28 percent. ILO, *United Republic of Tanzania, The Investment Policy and Financial Management of the National Provident Fund of Tanzania*, 1994, p. 12.

³⁷ *The Zimbabwe Independent Newspaper Online*, "NSSA Unable to Pay 20 Percent Salary Adjustment", website visited on 23 April 1999.

³⁸ In recent years, ZNPF staff reductions have been due largely to attrition caused by employee deaths, many of which are AIDS-related.

³⁹ The Zimbabwean National Social Security Authority (NSSA) has 1.3 million members compared to the ZNPF's 270,000. Now in its fifth year of operation, NSSA paying only funeral, survivors, and disability benefits. As it matures, it will have to increase staffing levels somewhat. Even so, this very large difference suggests overstaffing at the ZNPF.

⁴⁰ ILO, *Republic of Zambia: Report to the Government on the Strengthening of Social Protection, Vol. 5, Accounting and Financial Management*, 1998, p. 1.

High administrative costs cause the interest credited to individual accounts to fall far short of the funds' investment earnings. This pattern is illustrated in Tables 10 and 11.

Table 10 Zambia National Provident Fund, financial performance, selected years, 1985–91

YEARS	REAL RATE OF RETURN ON ASSETS	REAL INTEREST RATE CREDITED TO MEMBERS ACCOUNTS
1985–6	-5.9%	-32%
1987–8	-39%	-32%
1990–1	-32%	-47%

Source: World Bank, *Policy Research Working Paper 1716* (1997), p. 7.

As Table 11 shows, the interest credited to TNPF members' accounts in 1987–92 was in the range of 25–50 percent of what they could have earned on a normal savings account during this period.

Table 11 Tanzania National Provident Fund, financial performance, 1987–92

PERFORMANCE RATIOS (%s)	1987/88	1988/89	1989/90	1990/91	1991/92
Average gross yield on total invested assets	12.55	15.52	18.1	22.13	20.19
Average net of expenses yield on net assets	6.99	7.87	8.53	9.46	8.19
Official rate of inflation	29.95	31.2	25.8	19.7	22.3
Interest paid on provident fund balances	5.2	7.5	8.7	11	11
Interest paid on savings accounts in Tanzania	21.5	21.5	26	26	26

Source: ILO, *Republic of Tanzania: Investment Policy and Financial Management of the National Provident Fund*, 1994, p. 29.

In recent years, legal restrictions on provident fund investments have been eliminated in all three countries; and the funds diversified their investment portfolios, modestly in Tanzania and Zambia and more significantly in Swaziland. See Table 12.

Table 12 National provident fund investment portfolios

SWAZILAND NPF, 1998	TANZANIA NPF, 1997	ZAMBIA NPF, 1998
Government securities – .001%	Government securities – 56%	Government securities – 47%
Real estate – 25%	Real estate – 25%	Real estate – 45%
Equities – 34%	Equities – 2%	Shares and stocks – 5%
Treasury bills, fixed deposits, and loans (other) – 41%	Fixed income – 14%	Mortgages and loans – 3%
	Loans – 3%	

Sources: For Swaziland, figures were provided by the SNPF; for Tanzania, they are taken from the 1997 Annual Report; and for Zambia, they are taken from ILO, *Reform of Social Protection in Zambia*, Volume IIIa, 1998, p. 9.

In addition, some administrative spending reforms were implemented. At the ZNPF, these included freezes on recruitment of new staff, restrictions on salary increases, limitations on the conversion of unused leave to cash, enforced retirement rules, and limits on overtime and long distance telephone calls. Overall, however, these changes have not altered fund performance significantly. In most years, members continue to earn negative or very low returns. More recent performance is illustrated for the ZNPF in Table 13.

Table 13 Zambia National Provident Fund, key financial ratios, 1993–6

YEAR ENDING 31 MARCH	1993	1994	1995	1996
Inflation rate	138	35	45	35
Interest earned	8.7	20.7	21.3	19.3
Interest credited – Notational ⁴¹	50.2	84.3	22.2	10.3
Effective	32.1	61.2	19.2	8.2
Administrative costs as a % of contributions	51	68	110	63
Administrative costs as a % of investment income	257	91	85	98
Interest credited to members as a % of investment income	225	151	55	32

Source: ILO, *Report to the Government on the Strengthening of Social Protection, Vol. IIIa, Actuarial Assessment of the Proposed National Pension Fund, 1997*, p. 9 and 18.

Continuing low returns have fueled interest in reform, and all the countries are now at various stages of converting their national provident funds to pension schemes. In general, these conversions are proceeding slowly and have been impeded by two factors. First, actuarial studies have shown that the low retirement ages in effect at the provident funds are unaffordable for pension schemes which provide periodic, lifetime benefits. While these studies have convinced the officials most closely associated with the projects of a need for an increase, such proposals have met with resistance from others within the government and fund management. In Zambia, a proposal to increase the retirement age to 60 was rejected by government in favour of age 55, with an actuarially-adjusted option for retiring earlier. While government did not specify how the earlier retirement age will be paid for, it is clear that this decision will require significantly lower benefits or higher contribution rates over the long run. In Tanzania, the Parliament accepted increasing the retirement age to 60; but in the wake of this decision the new NSSF developed a generous early retirement option at age 55. It will increase scheme costs significantly above those in the actuarial estimates which were used to set the initial contribution rate (eight percent). In Swaziland, the fund's most recent proposal calls for an increase from age 45 to 60. This is under discussion among government, workers, and employers in Swaziland at present.

Second, all three funds are moving forward with conversion without having dealt with a

⁴¹ The notational rates of interest are calculated by ZNPF on fund balances at the beginning of the year, reduced by benefits to be paid out during the year. Calculated by the ILO, the effective rates take into account money paid into the account during the year.

major underlying cause of their poor performance, high administrative costs.⁴² In Tanzania, administrative costs were approximately 24 percent of contributions in 1998; in Swaziland, they were 44 percent of contributions during the 1997–8 financial year; and in Zambia they were 60 percent in 1998–9.⁴³ Because few workers will qualify for pensions in the years immediately following conversion, the impact of continuing high administrative costs will not be felt by the new schemes immediately. Over time, however, as benefit costs rise, the continuing need to divert scheme revenues for administrative expenses will weaken their capacity to pay promised benefits.

3.2 Non-contributory schemes

As described earlier, non-contributory schemes are of two types, universal and means tested. Both exist in Southern Africa, but many of the latter are characterized by limited funding, very low benefits, and long waiting lists which prevent eligible applicants from qualifying for extended periods, sometimes years.⁴⁴ Non-contributory schemes which provide significant benefits and cover large numbers of the target population exist in four countries: Botswana, Mauritius, Namibia, and South Africa.⁴⁵ The first three operate universal payment schemes while South Africa provides means-tested assistance.

All four schemes are operated directly by government. In Namibia, the administering agency is the Ministry of Health and Social Services; in South Africa, it is the Welfare Ministry; in Mauritius, the Ministry of Social Security and National Solidarity; and in Botswana, the Ministry of Local Governments, Lands and Housing. Only in Mauritius is this agency the same as the one that administers the national social insurance scheme. This reflects the different status afforded non-contributory and social insurance payments.

3.2.1 Who is protected

In principle, the covered populations in all four countries are very broad. In Botswana, the universal payment scheme extends to all citizens who meet program eligibility criteria; in Namibia, to all citizens and permanent residents; in Mauritius, to citizens with 12 years residence and permanent residents with 15 years residence; and in South Africa, to citizens with low income and assets.⁴⁶

⁴² In response to an inquiry by the authors, the ZNPF provided an estimate that administrative costs would increase from 60 to 91 percent of revenue expenditures between 1998/9 and 1999/2000. This projected increase is due to two factors: a decrease in scheme revenue from K22 billion to K18 billion and an increase in administrative expenditures from K13.2 billion to K17 billion. However, in commenting on a draft of this paper, an official of the Zambian Labour Ministry stated that "... the question of high administrative costs is being addressed during conversion by ensuring that when the National Pension Scheme Administration becomes operational, administrative costs shall not exceed three percent in the formative years (i.e., first three years) and one percent thereafter." It was not possible to obtain further details on this proposal or to determine how it affects the ZNPF projection.

⁴³ The SNPF and ZNPF figures were provided by the administering institutions. The TPNF estimated its costs at 18 percent, excluding depreciation and notational rents on fund-occupied real estate. In 1991–2, these items raised the ratio by about 25 percent. Thus, the current ratio including these items is probably around 24 percent.

⁴⁴ In Zimbabwe, the non-contributory benefit for blind and disabled individuals was Z194 (about US\$5) per month in 1998. Scheme recipients have petitioned the Department of Social Welfare to further decentralize payments, since the cost of a bus ride from a communal farming area to the district welfare office for a blind person accompanied by a helper was Z154, or 80 percent of the payment amount.

⁴⁵ Mauritius and Botswana also provide means-tested assistance, but these programs are smaller than their universal payment schemes. In Botswana, most means-tested assistance is in-kind.

⁴⁶ Prior to 1996, coverage in South Africa extended to both citizens and permanent residents. The Social Security Assistance Act of 1992 eliminated permanent residents; and this restriction was implemented in regulations by the Welfare Department as of 1 March 1996. This policy change was imposed as increasing numbers of migrant mine workers from neighbouring countries sought to qualify for the old age pension.

In practice, the reach of noncontributory schemes depends on a combination of geographic factors -- i.e., distances and population densities -- and available administrative resources. In Botswana, the Ministry of Local Governments and Lands is attempting to deliver benefits to a widely dispersed population with a new team of 60 pension officers. It reports:

There are pensioners who stay in settlements as far as 500 kilometers from the main [district] center, but paying officers are compelled to follow them up and pay them irrespective of their number, the time spent, the distance traveled, and the cost of transportation and subsistence. In some cases, the paying officers travel such long distances and spend a minimum of two days, only to pay one or two pensioners.⁴⁷

In South Africa, advocacy organizations hold that the Welfare Ministry's allocation of administrative resources skews the delivery of the social pension toward major cities, making it more difficult for poor blacks living in rural areas to qualify for the social pension.⁴⁸ These problems are much less severe in Mauritius, where the combination of a small geographic area, high population density, and well-developed government infrastructure makes universal pension coverage nearly universal in reality.

3.2.2 Which contingencies are addressed

The single contingency covered by all four schemes is old age. This is defined as age 60 and above in Mauritius and Namibia; 65 and above in Botswana; and 65 for men and 60 for women in South Africa. In addition, Mauritius provides protection in the event of disability, widowhood, and orphanhood; South Africa covers disability and provides subsidies for young children (under age seven); and both South Africa and Botswana compensate small numbers of war veterans.⁴⁹ Current beneficiary caseloads are presented in Table 14.

Table 14 Non-contributory schemes, target population, contingencies covered, and beneficiary caseloads, 1999

COUNTRY AND SCHEME	COVERED POPULATION	CONTINGENCIES	BENEFICIARY CASELOAD
Botswana – universal pension scheme	citizens	old age war veterans	71 000 6 200
Mauritius – universal pension scheme	citizens with 12 years residence and permanent residents with 15 years	old age disability widows orphans	109 000 17 000 21 000 737
Namibia – universal pension (known as social pension)	citizens and permanent residents	old age blind and disabled war veterans	82 000 12 000 111
South Africa – means-tested pension (known as social pension)	citizens with low income and assets	old age war veterans disability children	1 800 000 9 565 629 000 435 000 ⁵⁰

Source: Numbers provided by the administering institutions.

⁴⁷ Government of Botswana, Ministry of Local Government, Lands, and Housing, *Old Age Pension Scheme*, 1999, p. 7.

⁴⁸ Tilley, Alison, "Social Security in South Africa," (in draft), 1999, p. 4.

⁴⁹ While the number of war veterans is declining swiftly, a new scheme in South Africa to cover those who participated in the liberation struggle may result in a re-expansion of recipients. The new benefit will be administered by the Ministry of Defense.

⁵⁰ There are some dual beneficiary families included in these figures, which include about 200,000 women receiving the parent portion of the State Maintenance Grant, about 200,000 children receiving the same, about 40,000 receiving the Foster Care grant, and about 80,000 receiving the new Child Support Grant.

While the elderly are by far the largest category of recipients, there is evidence in three of the four countries that the pensions paid to them have a broad ripple effect. In rural South Africa where there are large numbers of unemployed and more than a third of the population lives in poverty, the social pension is a significant source of income for both immediate and extended families. A 1993 survey showed that one quarter of South African households were in receipt of social pensions and that these transfers constituted 18 percent of their income. In Namibia and Botswana, the combination of urbanization and AIDS mortalities is fueling a similar phenomenon, with growing numbers of elderly using their pension for food, clothing, and school fees for grandchildren left in their care.⁵¹ In an effort to address this problem, Botswana is providing supplemental in-kind support to pensioners who provide care for AIDS orphans.⁵²

With very few AIDS cases and an economy approaching full employment, Mauritius again presents a different picture.⁵³ Here the practice of living in extended families continues to be widespread even in urban areas, and most elderly individuals share the households of their working children. In this context, universal pensions in effect prevent a subsidy by the working generation of their elderly parents and, in this way, give the parents an increased measure of financial autonomy.

3.2.3 Benefit levels

Benefits vary substantially among the four countries. Monthly old age pensions are 110 Pula in Botswana (US\$23); 1,400 Rupees in Mauritius (US\$55); N\$160 in Namibia (US\$26); and a maximum payment of 500 Rand in South Africa (US\$80), depending on the income and assets of the recipient. In Mauritius, the same amount, 1,400 Rupees, is payable to disabled individuals and widows; and a smaller benefit, 785 Rupees, is payable for orphans, along with a minimal guardian's allowance. In South Africa, the benefit for disabled and war veterans is identical to that for elderly (R500 maximum); and young children can receive a grant of up to R100, depending on household size and income. In both South Africa and Namibia, these benefits are the result of a recent equalizing process which eliminated large disparities in payment levels based on race.⁵⁴

How adequate are these benefits to meet recipients' basic needs? Again the picture is mixed. In the two countries with the lowest payments, Botswana and Namibia, pensions fall short of meeting the costs of basic subsistence. A 1996 study of the Botswana pension showed that it fell 20 percent below these costs in rural areas and 80 percent below in urban centers.⁵⁵ Moreover, the measure of subsistence was a strict one, which excluded all furniture except a bench, all electrical devices, all snacks and sweets, and all nonessential clothing such as socks, stockings, coats, and rain wear.⁵⁶ In Namibia where no official poverty level has been established, it is estimated that N\$250–300 is necessary to cover subsistence costs in urban

⁵¹ Amupadhi, Tanfeni, "Affirmative action needed on pensions," in *The Namibian*, 10 March 1999.

⁵² This support was initiated after the Minister of Local Government and Lands visited an elderly woman who was attempting to support nine orphaned grandchildren with her pension.

⁵³ In 1998, the unemployment rate in Mauritius was 5.9 percent.

⁵⁴ In Namibia, the previous benefit for whites was seven times that for blacks. In South Africa, the differential was somewhat greater: R1 for an African, R5 for coloured and Indians, and R10 for whites as of 1982. By 1992, it was R293 for Africans, R318 for coloured and Indians, and R345 for whites.

⁵⁵ In Botswana, individuals who are 65 and over and poor may also receive the so-called destitutes allowance, in the form of food rations equal to 90 Pula per month.

⁵⁶ ILO working paper, "The adequacy of the proposed pension for over 65s," 1996, p. 2.

areas.⁵⁷ Here the level of the pension is a growing source of public dissatisfaction; and with national elections scheduled for December 1999, it is becoming a major political issue. A motion to increase the pension amount from R160 to R500 has been tabled in Parliament, and a coalition of civic and religious groups led by the Council of Churches is lobbying for it, citing elderly individuals' use of the pension to support their grandchildren, particularly AIDS orphans, as a key justification.

In Mauritius and South Africa, pensioners have somewhat greater purchasing power. The Mauritian universal pension was increased by more than 100 percent between 1989 and 1995 (from 308 to 630 Rupees) and then nearly doubled again in 1996 (from 630 to 1,220 Rupees), bringing it to twice the amounts paid in Namibia and Botswana in US dollar equivalents. The financial implications of these increases are discussed in the following section. In South Africa, the social pension exceeds the national poverty level;⁵⁸ and a comparison with a group of 11 countries with similar levels of economic development shows that it also exceeds their minimum pension benefits.⁵⁹

3.2.4 Financing

All four schemes are financed by annual appropriations of general revenues from the national treasury. For 1999, costs are estimated as follows:

Table 15 Costs of non-contributory schemes

COUNTRY AND SCHEME	COST (1999)	US\$ EQUIVALENT
Botswana, universal pension	105 million Pula	US\$22.9 million
Mauritius, universal pension	1.9 billion Rupees	US\$76 million
Namibia, social pension (universal)	175 million N. Dollars	US\$28 million
South Africa, social pension (means tested)	17 billion Rand	US\$2.7 billion

Source: Information provided by scheme administrators.

How burdensome are these costs on government budgets? In the three countries with the highest expenditures, the cost of the social pension is regarded as a national problem. In Namibia, payments to 3,000 new applicants were delayed for five months (December 1998–April 1999) due to lack of funding; and the Ministry of Health and Social Services projects that budgeted funds will fall short during 1998–9 by N\$60 million.⁶⁰ To control costs, the Ministry is seeking to means-test the pension; and the government has so far

⁵⁷ The World Bank, "Namibia's Emerging Pension System: Evaluation, Challenges, and Options," 1999 (in draft), p. 6.

⁵⁸ The South African *Report on Poverty and Inequality* defines the poverty cut-off as the poorest two quintiles of households, who earn R353 per adult.

⁵⁹ This relation with other countries was illustrated by the so-called Smith Committee, a study commission established by the Minister of Finance to assess the adequacy of the nation's pension schemes. This group compared South Africa with eleven countries of comparable levels of GDP – Costa Rica, Panama, Czechoslovakia, Venezuela, Brazil, Turkey, South Africa, Chile, Hungary, Mexico, and Uruguay. Its findings were two-fold: first, that South Africa was the sole country in the group without a national social insurance scheme to provide retirement and disability benefits to the work force; and second, that South Africa's social pension is relatively high in relation to the minimum benefit available under the contributory schemes in the other countries. *Report of the Committee on Strategy and Policy Review of Retirement Provision in South Africa*, December 1995, p. 40.

⁶⁰ *The Namibian*, "Pensioners Plight Put on the Table", 18 February 1999.

rejected the Parliamentary motion to increase its amount (described earlier) because of cost. In South Africa, the social pension constitutes 8.2 percent of the government budget and 91 percent of Welfare Department spending. As the elderly caseload is projected to increase steadily over the next decade by 2.5 percent per year, national discussions of social security reform focus on how to limit the social pension's cost.⁶¹ In Mauritius, recent increases in the universal pension, described earlier, have boosted its cost to more than double the national social insurance scheme's annual contribution income. The government estimates that, if the scheme were financed by contributions, the rate would have to be 17 percent. With the elderly in Mauritius also projected to increase by 2.5 percent per year into the foreseeable future, scheme costs are expected to reach six times annual contributions to the social insurance scheme in 35 years.⁶² Anticipating this rising burden, the Ministry of Social Security and National Solidarity stated:

The greater problem under the National Pension Scheme is not so much the future viability of the contributory part of the scheme (which can always increase its rate of contribution) but the continued ability of the government to finance payment of universal pensions⁶³

A 1998 actuarial report suggests raising the retirement age and means-testing benefits as means of controlling costs. The report is currently under consideration in Mauritius. Scheme costs in Botswana are somewhat more modest, due in part to the higher age of eligibility (65 for both men and women) and to the fact that the scheme is still in an early start-up phase, having begun operations in late 1996.⁶⁴

A second cost consideration, though of lesser magnitude, relates to administration. In countries with dispersed populations and limited government infrastructure, administrative costs are driven up by the need to perform several tasks. First, to establish eligibility for the old age pension, it is necessary to determine the ages of many individuals for whom no official birth records exist. In Botswana, this is accomplished via interviews and the collection of affidavits from community leaders, peers, and relatives. These activities are carried out by Age Assessment Committees established in each district of the country. Each consists of the district commissioner, a pension officer, a medical officer, a social welfare officer, a national registration officer, and a senior tribesman/woman.

Second, the scheme must deliver benefits to sparsely populated areas. In Namibia and South Africa, those who live far from post offices and banks receive the payment via private armoured vehicles which transport cash to predetermined pay points at a set day and hour each month -- e.g., a crossroad in a rural area or a designated tree. The costs are high (in Namibia, N\$18 per payment, or more than ten percent of the benefit); and security is a major issue.⁶⁵

Third, it is necessary to obtain regular and up-to-date information on pensioner deaths. In Botswana, pensioners are required to complete and return Life Certificates on a quarterly basis. In Namibia, this is done only once a year. The issuance and processing of these

⁶¹ A proposal put forth by the Welfare Department in a White Paper would do so by making retirement savings mandatory for all formal sector workers. *Government Gazette*, 2 February, 1996, p. 28.

⁶² GAD, *Actuarial Review of the Mauritius NPF as at 30 June 1995*, p. 2-4.

⁶³ Government of Mauritius, Ministry of Social Security and National Solidarity, "Social Security Scheme – Mauritius", 1997, p. 4.

⁶⁴ Government of Botswana, Ministry of Local Government and Lands, "Old Age Pension Scheme," 1999, p. 2.

⁶⁵ One creative firm devised a security system which involves dropping a large volume of ink from the vehicle ceiling if the door is opened without entering a secret password.

certificates is heavily manual, making this a time-consuming task for both pensioners and government and resulting in many errors on both sides, including incorrect benefit terminations. A recent report on the Botswana scheme stated:

In spite of numerous notices and announcements to urge pensioners to go to the nearest Commissioners of Oaths to sign these Life Certificates, the scheme continues to terminate quite a significant number of pensioners from the payroll every month because pensioners forget to sign the Life Certificates. However, once the Life Certificates are signed, the pensioners get reinstated and paid arrears.⁶⁶

In South Africa, the Welfare Department has undertaken a project called Ghost Buster to detect dead beneficiaries. Here the problem involves not only families which fail to report a beneficiary's death but also fraud rings within the Welfare Ministry which use deceased beneficiaries' identification details to collect multiple benefits. Project Ghost Buster involved re-registrations of the entire beneficiary caseload in several provinces.

The full cost of performing these tasks is not consistently reflected in the schemes' administrative budgets, since other government agencies may subsidize them by providing services free of charge -- e.g., reliance on district councils to estimate age in Botswana. When functions are privatized as in Namibia, their costs become clearer. This helps to explain the wide range of administrative costs across the four schemes. In Namibia, these costs equal 15 percent of annual benefit payments; in Botswana, 4.5 percent; and in Mauritius, two to three percent. Citing the complexities of decentralized administration, the RSA Welfare Department was not able to provide an estimate.⁶⁷

However, the most revealing measure of the financial burden of non-contributory schemes is not dollars spent on either benefits or administration. It is rather the economic strength of the countries where these schemes exist. As shown in Chapter 2, South Africa, Mauritius, Botswana, and Namibia rank one, two, three and four respectively in Southern Africa in terms of per capita GNP. No country at the middle and lower end of the income scale has undertaken such a broad and inclusive social protection initiative.

3.3 Social insurance

Social insurance schemes contrast with the universal and means-tested schemes in that benefits are financed by contributions and set to replace a portion of a worker's earnings. They contrast with national provident funds in providing periodic payments rather than lump-sums. Both features constitute strong advantages in meeting workers' need for social protection, and they are responsible for growing regional interest in developing social insurance. As things stand today, three countries -- Mauritius, Zimbabwe, and Mozambique -- operate pension schemes and two -- Namibia and South Africa -- operate schemes to provide short-term benefits.⁶⁸ As described in section 3.1, Tanzania has entered a five-year transition to a pension scheme; Swaziland and Zambia are planning similar conversions; and Namibia is preparing to launch a national pension scheme to complement its short-term benefits.

⁶⁶ Government of Botswana, Ministry of Local Government and Lands, "Old Age Pension Scheme," 1999, p. 6.

⁶⁷ For Namibia, see World Bank, "Namibia's Emerging Pension System: Evaluation, Challenges, and Options" (in draft), 1999, p. 11; for Botswana, the information was provided by the Ministry of Local Government and Lands; and for Mauritius, by the Ministry of Social Security and National Solidarity.

⁶⁸ In addition, five countries -- Zambia, Zimbabwe, Mauritius, South Africa, and Namibia -- operate employment injury schemes based on social insurance principles. The latter category is described in ILO/SAMAT Policy Paper No. 7, *Employment Injury Schemes in Southern Africa: An Overview and Proposals for Future Directions*, and is not included in this section.

The administrative arrangements for delivering these benefits involve both government and parastatal organizations. In three countries -- Mozambique, Namibia, and Zimbabwe -- schemes are operated by parastatals with tripartite governing boards, similar to those which administer the national provident funds. In Mozambique, the administering institution is the National Institute of Social Security (NISS); in Namibia, the Social Security Commission (SSC); and in Zimbabwe, the National Social Security Authority (NSSA). In all cases, the Labour Ministry is responsible for promulgating social security regulations and providing oversight. In two countries -- Mauritius and South Africa -- social insurance schemes are operated directly by government. The administering agency in Mauritius is the Ministry of Social Security and National Solidarity, while the South African UIF is operated by the Labour Ministry.

3.3.1 Who is protected

Like national provident funds, social insurance schemes generally protect members of the formal sector work force. Most schemes exclude part-time and temporary workers, domestic workers, and civil servants.⁶⁹ Three countries, Mauritius, Namibia, and Zimbabwe, provide voluntary coverage for self-employed individuals.⁷⁰ This is intended primarily as a means of reaching the informal sector, where employers typically do not keep records that make mandatory coverage possible. However, response rates are low. In Mauritius, about 500 self-employed individuals have registered voluntarily, or one half of one percent of the target population.⁷¹ In Namibia, 142 self-employed individuals have joined; and in Zimbabwe, NSSA's records indicate that just six have done so.⁷²

Except for Mauritius, coverage is further limited by significant non-compliance among employers, particularly small businesses and those located outside major urban areas. In Zimbabwe, NSSA estimates the legally covered population at 2.4 million, while the registered population is 1.3 million, or 52 percent.⁷³ In Namibia, a 1997 survey showed that 55.3 percent of the employed labour force was registered with the SSC.⁷⁴ While no estimates are available for South Africa, non-compliance is regarded as a major problem; and the Labour Department has established compliance "hit squads" to target chronically non-complying firms and reorganized its provincial Labour Centres to give compliance officers more resources and clout. In Mozambique, the government eliminated a legal exclusion for firms employing ten or fewer employees in 1997, thereby creating a significant compliance challenge.

National coverage statistics are provided in Table 16.

⁶⁹ Namibia excludes workers who are employed for two days a week or less; South Africa excludes government, casual, domestic, and temporary workers; Mauritius excludes workers in government and parastatals; and Zimbabwe excludes government workers, domestic workers, and the military. Those countries which exclude government workers cover them under a separate scheme.

⁷⁰ In Zimbabwe, employees who were scheme members for at least one year and become self-employed or unemployed may continue their membership.

⁷¹ In Mauritius, there is also a large benefit subsidy for voluntary members: contributions by self-employed are increased by 50 percent for the purpose of calculating benefits.

⁷² At NSSA, record keeping difficulties may have caused some omissions, but scheme officials believe that their number, if any, is not large.

⁷³ NSSA, "Questionnaire for the [ILO] Study of Quantitative Performance Indicators," 1998.

⁷⁴ This figure understates compliance somewhat due to statutory exclusions for those who work less than two days a week and for workers under age 16 and those over 65. ILO, *Namibia Labour Force Survey, 1997: An Interim Report of Analysis, August 1998*.

Table 16 Social insurance coverage of national populations

COUNTRY AND SCHEME TYPE	LABOUR FORCE	SCHEME MEMBERSHIP
Mauritius – pension scheme	485 000	280 000
Mozambique – pension scheme	9 451 000	240 800
Namibia – short-term benefits	672 000	264 100
South Africa – short-term benefits	15 117 000	4 900 000
Zimbabwe – pension scheme	5 304 000	1 267 964

Sources: Labour force figures are from *World Bank Africa Database, 1998/99*. Coverage statistics were provided by the administering institutions. Statutory exclusions are described in footnote 69.

3.3.2 Which contingencies are addressed

The national pension schemes in Mozambique, Mauritius, and Zimbabwe cover old age, disability, and survivorship; and the Mozambican scheme also provides sickness benefits. The South African Unemployment Insurance Fund (UIF) covers unemployment, sickness, maternity, adoption of a child, and death (survivors) benefits. The Namibian Maternity, Sickness, and Death (MSD) Fund covers the named contingencies.

3.3.3 Benefit levels

Cash payments are set in relation to a worker's insured wages by all the schemes but with varying replacement rates. For pensions, a worker who retires after 30 years in Zimbabwe would receive monthly payments equal to 40 percent of his or her insured wages; in Mauritius, this ratio is 33 percent; in Mozambique, it is 40 percent of the highest two years of earnings; and in Tanzania, it will be 45 percent when the new scheme is fully operational. The retirement age is 60 for all four schemes, but Zimbabwe provides an early retirement option at age 55 for workers in arduous employment and Tanzania is planning an early retirement option at age 55, described in section 3.1. Disability and survivors benefits are calculated in relation to retirement pensions, as shown in Table 17. Only one country, Mauritius, has legislated annual cost-of-living adjustments in benefits. Given the high levels of inflation in Southern Africa, the absence of such adjustments is eroding beneficiaries' purchasing power. In Zimbabwe, NSSA estimates that the real value of benefits declined by 23 percent in fiscal year 1994–5 and 22 percent in 1995–6.⁷⁵

For short-term benefits, the South African UIF replaces 45 percent of a worker's covered wages for up to six months in a year. This is a modest replacement rate by international standards. The Namibian MSD Fund provides higher rates -- 80 percent of insured wages for maternity and 60 percent for sickness, reduced to 50 percent after six months. The maximum duration of 12 weeks for maternity benefits and, for sickness benefits, it is two years. The MSD Fund also provides a uniform N\$2,000 death benefit.

⁷⁵ NSSA, "Questionnaire for the [ILO] Study of Quantitative Performance Indicators," 1998.

Table 17 Social insurance benefits

COUNTRY	CONTINGENCIES COVERED	BENEFITS
Long-term contingencies: old age, disability, and survivorship		
Mauritius	Old age, disability, and survivors	<i>Retirement:</i> 33% of average earnings after 40 years of contributions (higher benefits for sugar industry). <i>Disability:</i> based on pension points with minimum income replacement of 30%. <i>Widows:</i> same as disabled. <i>Orphans:</i> 15%.
Mozambique	Old age, disability, survivors, and sickness	<i>Retirement:</i> 40% of average salary during last two years. <i>Disability:</i> 60% of average daily salary. <i>Survivors:</i> 50% of insured's pension for surviving spouse, up to 50% for children.
Tanzania	Old age, disability, and survivors	<i>Retirement:</i> 1.5% of worker's average earnings per year, up to maximum of 67.5%. Minimum benefit is 30% of average wages or 80% of minimum wage, whichever is higher. <i>Disability:</i> same as retirement but with an additional 1% of average earnings per year (temporary disability, 60% of average earnings) <i>Survivors:</i> 40% of insured's entitlement (100% if no children), with remaining 60% divided among the children. Entitlement goes to parents if no spouse or children.
Short-term contingencies: sickness, maternity, unemployment, and death		
Zimbabwe	Old age, disability, and survivors	<i>Retirement:</i> 1.33% of average monthly insurable earnings at the date of retirement. <i>Disability:</i> sliding scale depending on the employee's average monthly insurable earnings in the period of contribution. <i>Survivors:</i> widow/widower receives 40% of insured's benefit; children, 40%; parents' 12%; and others, 8%.
Namibia	Maternity, sickness, and death	<i>Maternity:</i> 80% of wages for 12 weeks. <i>Sickness:</i> 60% of wages for six months, 50% thereafter for up to 18 months. <i>Death:</i> N\$2,000.
South Africa	Unemployment, sickness, maternity (and adoption) and death	45% of weekly earnings for up to six months.

3.3.4 Financing

Both short-term schemes are financed on a pay-as-you-go basis. Here, as explained in Chapter 1, current contributions are used to pay current benefits and to fund a small financial reserve to meet unexpected cost and income fluctuations. All three pension schemes are partially funded and, with the exception of Swaziland, partial funding will also be used by the provident funds which are converting to pension schemes.⁷⁶ For short-term benefits, the combined rate for workers and employers is in the range of two percent and, for pensions, it is six to nine percent. See Table 18.

⁷⁶ SNPF management anticipates partial funding of a basic social insurance benefit, complemented by a fully-funded individual savings scheme.

In two countries, Mozambique and Tanzania, contributions are levied on a worker's entire earnings. Mauritius has established a ceiling on covered earnings, currently Rs 55,500, which it adjusts annually for inflation. Zimbabwe also imposes a ceiling but has no indexing. This means that the real value of scheme revenues is being eroded each year, causing a commensurate reduction in the portion of a worker's wages which will be replaced by benefit payments.

The length of the minimum contribution period required for eligibility also varies by scheme type. Pension schemes generally require at least 15 years of contributions, whereas the MSD Fund requires six months and the UIF, at least 13 weeks during the previous year.⁷⁷

Table 18 Social insurance contribution rates, 1999

SHORT-TERM BENEFITS	CONTRIBUTION RATE	COVERED WAGES
Namibia – MSD Fund	0.9% workers, 0.9% employers	N\$3 000 per month (US\$480)
South Africa – UIF	1.0% workers, 1.0% employers	R88 920 per year (US\$14 300)
LONG-TERM BENEFITS	CONTRIBUTION RATE	COVERED EARNINGS
Mauritius – MSSNS National pension scheme	3% workers, 6% employers 10.5% employers (sugar industry)	Rs55 500 per year (US\$2 220)
Mozambique – INSS National pension scheme	3% workers, 4% employers	No ceiling
Tanzania – NSSF National pension scheme (when conversion complete)	4% workers, 4% employers	No ceiling
Zimbabwe – NSSA National pension schemes	3% workers, 3% employers	Z\$4 000 per month (US\$105)

How adequate are these rates to finance the schemes' benefit commitments? The answer is simpler to arrive at for short-term benefits where expenditure patterns are more stable over time. Here the MSD Fund and UIF differ markedly, with the former accumulating a large surplus and the latter facing chronic deficits. A 1998 actuarial assessment of the MSD Fund showed that benefit payouts equaled just 64 percent of contribution income, of which 17 percent was administrative costs, up from 12 percent in 1997.⁷⁸ This large gap between income and expenditures means that the Fund is accumulating excess reserves. This study concluded that a rate of 0.6 percent, as opposed to the current 0.9, is adequate to finance the MSD Fund.

⁷⁷ Mauritius is a noteworthy exception in having no minimum contribution period for its national pension scheme.

⁷⁸ ILO, *Report to the Government on the Development of Social Security: Actuarial valuation of the Maternity, Sickness, and Death (MSD) Fund*, 1999.

At the UIF, by contrast, benefit payouts exceeded contribution income in most recent years, causing Fund's reserve ratio to fall from 150 percent of benefits in 1990 to just 25 percent in 1995.⁷⁹ Since then, the scheme has gone technically bankrupt and has placed restrictions on eligibility and benefits as a means of containing costs.⁸⁰ This financial crisis results from a combination of higher unemployment levels in the South African formal sector, which have increased both the number of claims and their duration, and weak financial controls at the UIF. It is noteworthy that, as five to seven percent of contribution income, administrative spending is not a source of the UIF's financial difficulties.

The main weaknesses in UIF financial controls are three-fold. First, the absence of a national register of employers leaves it unable even to estimate the numbers of non-complying firms. With no master list, it cannot target enforcement activities optimally or judge their success. Second, those employers who do register are required to report only their aggregate wage bill and total work force to the UIF, not the names of individual workers or the wages they receive. This provides leeway for employers to reduce their contributions by underestimating wages. Third, the UIF uses an outdated system of eligibility determination which relies on a so-called Blue Card. Workers must carry it from employer to employer to obtain their signature and stamp as verification of employment. Because the UIF lacks information against which to check Blue Card entries (i.e., the names of scheme contributors and their wages), fraudulent claims can go undetected.

In 1999, the Labour Department is undertaking a major rewrite of the UIF authorizing statute to address these problems. At the same time, it is under heavy pressure to extend coverage to excluded groups such as temporary, part-time, and domestic workers for whom administration is costly.

For long-term social insurance benefits, the question of regional schemes' financial adequacy is more difficult to assess due to the recency of their establishment. The oldest scheme, Mauritius, has been in existence two decades; but even there most pensioners receive a small benefit based on a few years contributions.⁸¹ With Mozambique's NISS in its ninth year of operation, Zimbabwe's NSSA in its fifth year, and the Tanzania NSSF still in a transition period, most scheme members across the region will contribute for several more decades before receiving benefits. To date, only Mauritius has undertaken a long-term actuarial analysis of its capacity to meet these future obligations. Without such studies, it is possible to make only very general observations. Three patterns are noteworthy.

First, all the schemes are currently building up large financial reserves. In Mauritius, 1999 contributions are estimated at R837 million, while benefit payments will total R479 million and administration, R21 million. Thus, even after two decades of operation, the scheme is still investing more than 40 percent of its annual contribution income.⁸² In Zimbabwe, 1997 contributions to NSSA totaled Z\$740 million, benefit payments were Z\$36 million, and administration was Z\$87 million, leaving more than 80 percent of contributions for investment. In Mozambique, the NISS received contributions of M115 billion in 1998, paid out M12 billion in benefits, and incurred administrative costs of M28 billion. Here ten percent of contribution income was used to pay benefits, 26 percent was used for

⁷⁹ Meth C, R Naidoo, and B Shipman, *Report of the Task Team on Unemployment Insurance and Related Coverage Issues*, 17 December 1996, Appendix 5.2, p. 3.

⁸⁰ Certain types of dependents have been excluded on the basis of marital status of people in the family; the number of payment days has been capped at 20; and restrictions have been placed on the types of documentation which are acceptable as proof of eligibility.

⁸¹ GAD, *Actuarial Valuation of the Mauritius NPF*, 30 June 1995, p. 6.

⁸² When the reinvestment of annual interest and dividends is counted, 85 percent of total scheme income is being invested.

administration, and a full 64 percent was invested. As shown in Table 19, there is wide variation in the investment of these surpluses.

Table 19 Investment of social security assets, Mauritius, Mozambique, and Zimbabwe

INVESTMENT TYPE	MAURITIUS NPS – 1998	MOZAMBIQUE NPS – 1998	ZIMBABWE NPS – 1997
Government issues	58%	–	16%
Equities/shares	6% (4 % shares/ bonds; 2% stock exchange)	32%	29%
Housing and real estate	13%	22%	10%
Banks/money markets	2% commercial banks, 13% DBM deposits	44% DBM deposits	46% money market
Other			–
Foreign investment	6%		
Loans	2%	2%	

Sources: Figures for Mauritius were provided by the Ministry of Labour and Social Solidarity; for Zimbabwe, from the *NSSA Annual Report, 1997*; and for Mozambique, by the NISS.

While a rapid accumulation of reserves is normal in the early years of a pension scheme, so are the challenges that it poses for financial management. In Mauritius, for example, pension scheme investments contributed to a glut in local financial markets in 1998 and, as a consequence, to falling interest rates. The scheme had to move some investments overseas to offset losses. In Zimbabwe, NSSA has come under pressure from trade unions to invest in the construction of affordable housing and, from government, to purchase and hold parastatals being sold off as part of structural adjustment.⁸³ In Namibia, the Social Security Act provides authority for transfers from the reserve fund to a national development fund, to be used for education and training for disadvantaged citizens. No such transfers have occurred to date. While all these objectives are positive in a broad social sense, it is unclear that they will produce the profits needed to fulfill future commitments to scheme members.

Second, while currently flush with reserves, all the schemes face a rising cost curve that will require increased contributions over time. The low rates of contribution currently in effect are made possible by two factors -- the recency of the schemes' establishment and the low average ages of populations in Southern Africa, as shown in Chapter 2. However, as the schemes mature, more members make the contributions necessary to qualify for benefits, and economic development causes the average ages of covered populations to rise, these rates will have to increase. Both the timing of the increases and their magnitude will depend heavily on national economic performance. International experience suggests that the ultimate contribution rate may be in the order of five to 15 percent of insured wages for employers and employees, each, or even higher under unfavourable demographic and economic conditions.

⁸³ Government's objective is that NSSA hold these parastatals for subsequent sale to indigenous businesses.

In addition, all schemes except Mauritius face increased short-term costs due to the AIDS epidemic. Only one country, Namibia, has systematically investigated the impact of AIDS on pension expenditures; and this analysis suggests that costs may rise by roughly one third over the next 25 years, followed by a downward trend and perhaps small long-term savings to the scheme.⁸⁴ While an increase of this general magnitude may be judged affordable in light of the low contribution rates currently in effect, this issue requires high priority attention in national social and economic planning. Contributory pension schemes have a vital role to play in coping with the AIDS epidemic, but advance planning is necessary to ensure that financing is adequate to meet the increased demands.

Yet a third pattern is that, with an exception for Mauritius, all the schemes face the challenge of tightening financial controls. Because they make limited use of automation, most are unable to generate timely information on contributions received, benefits paid, and administrative expenses incurred. In both Zimbabwe and Mozambique, legally mandated actuarial analyses of scheme financing are overdue by several years.⁸⁵ In addition, some schemes routinely make use of worker contributions for non-social security purposes -- e.g., donations to community events, cash contest prizes, and cars and upgraded air transport for government officials. Some of these expenditures are small, and others benefit the community, the government, or scheme employees. However, they create a precedent of uses which are at odds with scheme administrators' fiduciary duties to protect member contributions.

Stronger financial controls are also needed over administrative spending. The 1997 administrative spending ratios were approximately 24 percent of contributions for Tanzania; 12 percent in Zimbabwe; 24 percent for Mozambique; and about three percent for Mauritius. Because new schemes normally incur high start-up costs, it is difficult to formulate a precise benchmark against which to evaluate these spending levels. Even so, it is clear that these rates must fall significantly if the schemes are to operate in workers' interests. Moreover, the difficulties experienced by the national provident funds in reducing administrative costs point to a need to act quickly, before spending patterns become entrenched.

3.4 A comparative assessment

The preceding sections show that social security schemes across Southern Africa are experiencing several common problems. Coverage of target populations tends to be narrow, leaving most South Africans without any formal social protection. The benefits paid by many schemes are inadequate to meet basic needs. With non-contributory schemes, a heavy reliance on general tax revenues strains government financing, keeping benefits at low levels in most countries. Third, with some noteworthy exceptions, scheme operational efficiency is low, resulting in high administrative costs. This is due in part to the region's weak infrastructure for public administration, in part to dispersed and hard-to-reach populations, and in part to a tendency in Southern Africa to regard public posts as providing their holders with broad latitude in the use of public assets.

Along side these cross-cutting similarities, there are also some striking differences. *National provident funds* clearly rank lowest on the criteria of interest. Though intended for long-term contingencies, benefit payments tend to be exhausted rapidly on short-term expenditures. The financing method, full funding, is mismatched to the economies where they exist, with inflation offsetting much of the interest credited to member accounts. Until recently, returns

⁸⁴ ILO, "Discussions between ILO Actuarial Consultant and Private Pension Actuaries: Meeting Notes and Subsequent Analysis," 1999.

⁸⁵ Linsell, David, "Actuaries Start at NSSA Five Years Late," *The Daily News*, 28 April 1999, p. 26.

were also diminished by statutory requirements that the funds invest in low-yield government instruments. High levels of administrative spending further erode member savings. Together these factors have led to a widespread erosion of confidence in the schemes and, as a consequence, to efforts to convert them to pension schemes in all three countries.

Non-contributory schemes rank higher on the coverage criterion but low on the other three. These schemes' strongest advantage is their capacity to reach beyond the formal sector to the large majority of Southern African workers -- subsistence farmers, the urban informal sector, and the chronically underemployed who are able to find only temporary or part-time work. Even here, however, coverage is less than universal in practice due to geographic factors (i.e., long distances and low population densities) and restricted administrative funding. As for targeted contingencies, in countries with large populations of poor people, regional experience suggests that it is simply not possible to direct protection narrowly at particular needs. Instead the extended family channels protection provided for one contingency (e.g. old age) to members who face other problems (e.g., underemployment or orphanhood), creating a broad ripple effect. Moreover, limited economic development creates a trade-off between payment adequacy and the financial burden posed by non-contributory schemes. This is because, in developing countries, governments must draw from relatively small revenue bases to finance benefits for a relatively large population which does not pay taxes. The resulting financial strain keeps benefits low (Botswana), places pressure on the national treasury (South Africa, Mauritius), or both (Namibia). Means-testing may be applied in an effort to alleviate this burden, but this is costly administratively and may induce some members of the beneficiary population to decline to work and save.

Social insurance is more difficult to evaluate due to these schemes' more recent establishment. On the positive side, the pooling of risks and resources across the covered population enables them to pay benefits throughout most contingencies.⁸⁶ In a region where large numbers of workers live in poverty or on its edge, this is a great enhancement to economic security. Moreover, all the schemes set payment levels in relation to members' insured earnings. With regular indexing, this provides an important measure of adequacy in relation to their previous standard of living. With the exception of the UIF, earmarked financing in the form of worker and employer contributions enables the schemes to operate without government subsidies.⁸⁷ In addition, the financial systems used by these schemes -- pay-as-you-go for short-term benefits and partial funding for pensions -- makes them less vulnerable to inflation, misappropriation of reserves, and poor investment returns than fully funded schemes.

Yet these schemes also exhibit some of the weaknesses described earlier: Coverage is narrowly restricted to the formal sector. With two noteworthy exceptions (the UIF and Mauritian pension scheme), operating expenses are high, in the neighbourhood of 12 to 24 percent of annual contribution income. Only two schemes, the UIF and the Mauritian pension scheme, provide regular inflation indexing for benefits and insured wages. In addition, all the pension schemes are financed by scaled premiums which must increase over time. See Table 20.

⁸⁶ Like most other unemployment schemes, the UIF is an exception, covering only short-term unemployment (up to six months of benefits in a year).

⁸⁷ As described in Chapter 2, UIF contribution rates are inadequate; and the scheme is in technical bankruptcy.

Table 20 Comparison of schemes types

	INDIVIDUAL SAVINGS SCHEMES (PROVIDENT FUNDS)	NON-CONTRIBUTORY SCHEMES	SOCIAL INSURANCE
BREADTH OF COVERAGE	Narrow – restricted to formal sector workers	Broader – includes the unemployed and those who never worked but still restricted by high dispersion of populations	Narrow – restricted to formal sector workers
ADEQUACY OF BENEFITS	Inadequate – lump sum payments are low in relation to long-term needs and tend to be exhausted rapidly	Mixed picture	More adequate – only SI benefits are set in relation to a worker’s lost wages and paid throughout his or her period of need (exception: UIF)
BURDEN ON GOVERNMENT REVENUES	No burden, due to reliance on contributory financing	Generally heavy burden	Generally no burden due to contributory financing (exception: UIF)
OPERATIONAL EFFICIENCY	Very low due to high personnel costs	Mixed picture	Mixed picture

In sum, social insurance schemes offer unique advantages in enhancing workers’ social security, but they are plagued by some of the same problems which exist with respect to other scheme types in Southern Africa -- narrow coverage and high administrative costs. It is therefore important to consider whether these problems can be addressed and, if so, how. The following chapters will turn to this question.

Chapter 4

Social insurance for the informal sector: a recent innovation

The preceding chapter shows that efforts to extend social security to the informal sector have been largely unsuccessful. The high cost of non-contributory schemes keeps their benefit levels low and limits their existence to a few higher-income countries. Voluntary membership in social insurance schemes has failed to attract significant numbers of informal sector operators. Given the predominance of the informal sector in most Southern African countries, these limitations constitute a major barrier to extending protection broadly to national populations.

In an effort to identify new approaches, the ILO undertook a major demonstration project in the early 1990s involving associations in the urban informal sector of Dar es Salaam.⁸⁸ Recognizing that the vast size of the informal sector limits the potential for extending protection through government subsidies, the project provided only technical assistance, no direct funding. As a first step, it involved surveying the target groups to determine what protection they wanted and were willing to pay for themselves. Assistance was then provided with the structuring of small social insurance schemes to deliver these benefits. To date, five schemes have been established covering some 6,000 informal sector workers and their families. These schemes differ from formal ones not only in the population covered but also in insured contingencies, benefits, and administrative systems.

The initial project surveys showed that the protection of greatest interest to informal sector operators is of a short-term nature. Old age protection was not a top priority, nor were disability or survivors benefits. See Table 21.

Table 21 Benefits desired by informal sector operators

TYPE OF BENEFIT DESIRED	PRIORITY 1		PRIORITY 2		PRIORITY 3	
	%	RANK	%	RANK	%	RANK
Medical/sick/injury	62.4	1	8.4	5	0.3	8
Medical/maternity	6.3	3	0.1	10	0.1	10
Sick/injury benefits	5.6	5	15.0	3	2.0	7
Disability benefits	5.7	4	12.3	4	4.5	6
Old age pension	9.3	2	26.7	1	12.0	4
Funeral costs	3.7	7	24.0	2	23.8	2
Survivors benefits	0.7	9	7.6	6	12.8	3
Maternity benefits	0.1	10	2.3	8	6.2	5
Education for family	1.6	8	3.3	7	38.0	1
Do not know	4.6	6	0.3	9	0.3	9

Source: A.D. Kiwara, Institute for Development Studies, University of Dar es Salaam, "Social Security for the Informal Sector," January 1999, p. 5.

⁸⁸ Aryee, George, *Promoting Productivity and Social Protection in the Urban Informal Sector: An Integrated Approach, Report on ILO Pilot Projects in Bogota, Dar es Salaam, and Manila*, Geneva: ILO, 1996.

To deliver this protection, the ILO assisted in structuring health insurance schemes to provide primary care and selected preventive services. Administration of these schemes is carried out largely by the associations themselves, with assistance from a local umbrella organization known as UMASIDA (United Medical Aid Schemes in Dar es Salaam) which provides training, financial auditing, and general support. Association leaders collect contributions from members on a daily basis, thereby helping to keep them affordable; authorize them to visit a clinic when they are ill; negotiate group discounts with local physicians; and devise agreements whereby the physicians provide services close to the members' work sites, thereby saving them time and money associated with travel to a hospital. Cooperatives that wish to join a scheme or establish a new one are screened for stability of membership, as well as for the group's capacity to make the required contribution (20 Tan. shillings per day, or about US\$0.03).

As the schemes have gained experience, they have put measures in place to prevent fraud and increase transparency. These include photo identification cards, official seals for embossing documents, and circulating invoices. Leaders are also trained to facilitate group decision making, thereby encouraging open debate and policy making by consensus.

Financial calculations show that, when the group discounts and reductions in lost work time are taken into account, the schemes actually produce financial savings for their members. One scheme member commented:

Before the scheme, I could not go to work when one of my children fell ill. I had to go around to look for money to take the child to the dispensary. Things have now changed. I come to work because the scheme takes care of that.⁸⁹

Reflecting widespread member enthusiasm, membership has expanded from an initial 1,500 workers and family members to the current total of 6,000. Word of the schemes' benefits has spread to neighbouring countries. A pilot project modeled on it is now being undertaken with ILO technical assistance in Uganda and, in Zimbabwe, the domestic workers union is exploring the possibility of establishing a similar scheme.⁹⁰

Those most closely involved in the project have identified its major lessons.⁹¹ There are five of these. First and foremost, it shows that improving productivity and social security are not incompatible goals in the informal sector. Under selected conditions, they can be achieved simultaneously. Second, the varied nature of the informal sector requires a highly individualized approach. Groups with high productivity can finance their own benefits, while the very poor can only be reached through other means. Third, in an environment where many aspects of life are uncertain, workers are most interested in short-term protection. The larger element of voluntarism in these arrangements makes it necessary to take this preference into account in scheme design. Fourth, stable group organization is essential, since it is only through reliance on the group that operational costs can be kept at reasonable levels. Finally, member involvement in administration can provide important secondary benefits -- i.e., the fostering of group cooperation, self-discipline, and negotiating skills. These benefits are described vividly in a recent evaluation by a local project consultant:

As an organized group, they have learned that they can sit and negotiate with a health care provider. Before the scheme was established, most of the members thought that the relationship between a sick person and a health care provider was dictated by the provider. In other words, the provider had power over the sick person.

⁸⁹ ILO-STEP, "Mburahati Case Study" (draft no. 3), 4 May 1999, p. 3.

⁹⁰ Masiko, A., "Social Security Health Insurance and Ensuring Work Place Safety in the Informal Sector in Uganda," 1998.

⁹¹ Aryee (1996), p. 14-31.

The experience ... shows that the power equilibrium is now changing toward a kind of partnership between the health care provide and the scheme. This has necessitated a change in attitude and behavior from both parties.⁹²

For a population which is often poorly organized, weak politically, and unable to interact as an equal player with the individuals and institutions in the immediate environment, such grass roots empowerment constitutes a very major benefit.

However, the schemes are still at an early stage of development; and their ultimate potential is dependent on three important unknowns. First, there are unanswered questions about informal associations. How robust and sustainable are they over time? Can they be established for the sole purpose of expanding social protection? Is the solidarity among members which accounts for their success dependent on small group size? Can they be used to provide other forms of social security to members? These questions are the focus of current research within the ILO and elsewhere.

Second, to ensure transparency and greater access to capital, it will be necessary to link these schemes to institutions in the formal sector. While such linkages are being discussed in Tanzania, none has as yet been devised; and it is not clear how they will be structured.

Third, like all forms of social protection, these schemes are dependent on economic productivity of their members, who must generate a surplus sufficient to make the required contributions. In this sense, the fate of these schemes is linked to broader unknowns about the prospect for improved growth in Southern Africa's vast informal sectors.

⁹² ILO-STEP, "Mburahati Case Study" (draft no. 3), 4 May 1999, p. 2.

Chapter 5

Proposals for reform of social security in Southern Africa

Chapter 3 showed that most social security schemes in Southern Africa are experiencing a common set of problems: limited resources, narrow coverage of populations, the erosion of benefits by inflation, and high administrative costs, with the latter due to a combination of weak subsystems for public administration and a lingering tendency in South Africa to assume that public posts provide their holders with an entitlement to public resources. These problems impede the functioning of all three types of schemes to various degrees. Their pervasiveness suggests that, in Southern Africa, the political and economic environments in which social security operates are more important in determining its success than any particular design feature. While debates in other parts of the world focus heavily on issues of scheme design -- e.g. full funding versus pay-as-you-go, pooled risk versus individual savings, and public versus private administration -- the main challenge for this region is to address cross-cutting problems which impede the delivery of all types of protection.

This chapter takes this approach in analyzing several possible reform proposals. The first is conversion of national provident funds to social insurance pension schemes, a change undertaken by number of African countries with ILO assistance (Chapter 3); the second involves extending social security to the informal sector through small social insurance schemes for group associations and collectives, an ILO innovation (Chapter 4); the third involves establishing fully funded, privately managed national savings schemes to replace social insurance, as advocated by the World Bank and some segments of the Southern African pension industry and implemented by several South American countries. The final proposal is formulated by the authors, and it takes as its starting point the unique advantages which social insurance can offer in the Southern African context. It is described in section 5.4 and then evaluated according to the same regional criteria as the other proposals.

5.1 Conversion of national provident funds to social insurance pension schemes

Now implemented in Tanzania and underway in Swaziland and Zambia, this reform is being undertaken in response to the chronically weak financial performance of provident funds. It involves moving from lump-sum payments to periodic ones and, in Tanzania and Zambia, from full funding to partial funding.⁹³ While pensions are generally a far more effective form of social security than lump sum payments, these conversion efforts receive a mixed rating on the evaluation criteria. See Table 22.

⁹³ In Swaziland, the SNPF is proposing a two tier system consisting of a partially funded pension benefit and a supplemental individual savings scheme which will be fully funded.

Table 22 Conversion to social insurance: impact on reform criteria

LIMITED RESOURCES	NARROW COVERAGE	COSTLY ADMINISTRATION	VULNERABILITY TO INFLATION
Yes, short-term advantage.	No, few planned coverage extensions.	No, may worsen the problem if contribution rates are increased without administrative spending reforms.	Yes, COLAs are planned by all three funds; but positive impact is threatened by the need to divert contributions to cover high administrative costs.

5.1.1 Limited resources

Reliance on partial funding means that initial contribution rates can be lower than those required to ensure the schemes' long-term financial solvency. This is an advantage in making pensions more affordable in low income countries in the short-run. However, partial funding also commits future generations to higher contribution rates, since these rates must rise over time as scheme expenditures increase. The burden which these higher rates impose will depend heavily on economic development in coming years and decades.

5.1.2 Narrow coverage

None of the conversion projects call for significant coverage extensions. Zambia will cover new hires in the civil service but, given the large scale government retrenchments in progress there, this approach will probably take many years to expand coverage significantly.

5.1.3 Costly administration

As noted previously, all three conversions are moving ahead without measures in place to deal with a major cause of the provident funds' poor performance, high administrative costs.⁹⁴ If worker and employer contributions are increased as part of the conversion in the absence of administrative spending controls, conversion could actually worsen this problem.

5.1.4 Vulnerability to inflation

Indexing of benefit payments for inflation or wage increases can be accomplished with relative ease under pay-as-you-go and partially funded social insurance schemes.⁹⁵ The solution lies in a legal requirement for annual adjustments in benefits, covered wages, and all flat dollar amounts used in scheme administration. Implemented properly, such adjustments will not result in financial difficulties since revenues and pay-outs will rise simultaneously. All three schemes are planning to index benefits in this manner.

However, high administrative spending threatens the new schemes' capacity to provide indexed benefits over the long term, since it will divert revenues which could otherwise be used for this purpose to administration.

⁹⁴ Moreover, in Zambia, the contribution rate will be increased from 3.5 to five percent as part of the conversion; and the scheme has budgeted to increase administrative costs from 60 to 91 percent in 1999–2000. Thus, conversion may actually serve to worsen the drain caused by high administrative spending.

⁹⁵ With fully funded schemes, a hedge against inflation is available in some countries through purchase of bonds whose yields are indexed to future inflation rates. However, because the sole issuers of such instruments are governments, their purchase has the effect of channeling the revenues back into current public expenditures.

5.2 Social insurance schemes for informal sector associations

The new micro health insurance schemes being developed with ILO support in Tanzania and emulated elsewhere look quite different from traditional social insurance: membership is voluntary rather than mandatory (i.e., associations decide whether or not to establish a scheme and members decide whether or not to join); they rely heavily on their own members for administration; they focus exclusively on short-term health insurance benefits; and they are operated without the need for a large build-up of funds. As shown below, these features seem well suited to address the region's main problems:

Table 23 Development of social insurance schemes for the informal sector: impact on reform criteria

LIMITED RESOURCES	NARROW COVERAGE	COSTLY ADMINISTRATION	VULNERABILITY TO INFLATION
Yes, short-term benefits are generally less costly.	Yes, for the subset of informal sector operators with stable organization and ability to pay.	Yes, through reliance on voluntary labour by associations.	Yes, due to small reserves and short-term benefits financed on pay-as-you-go basis.

5.2.1 Limited resources

Chapter 3 showed that short-term benefit schemes are considerably less costly than pensions -- for the formal sector, in the range of one to two percent of covered wages. Under the UMASIDA approach, group discounts further reduce member costs. Given the short time horizon of many informal sector operators, contributions are collected on a daily basis, a practice which also helps make the schemes affordable.

5.2.2 Narrow coverage

The rapid growth of the Tanzanian schemes suggests that they may have considerable potential to deliver new social security to excluded populations. However, the schemes are still at an early stage of development and their ultimate usefulness is dependent on several important unknowns. Described in Chapter 4, these relate to the stability of informal sector associations over time, to the potential for linking these schemes with formal social security institutions and, most fundamentally, to the prospects for increasing productivity and incomes in the Southern Africa's informal sectors.

5.2.3 Costly administration

These schemes' heavy reliance on members themselves for administration keeps their cost low. In Tanzania, oversight and auditing are provided by a part-time financial auditor and full-time clerical assistant. The cost of linking informal sector schemes to formal social security institutions is a significant unknown.

5.2.4 Vulnerability to inflation

Pay-as-you-go schemes for short-term benefits are less vulnerable to inflation than pensions, and the negotiation of group discounts helps to offset inflation in health care costs. Moreover, scheme reserves are small.

As noted previously, these schemes also provide broader social benefits. Their pluralistic form of administration encourages cooperation and self-regulation within informal sector groups; and the management experience which their leaders gain helps to empower them to deal with external organizations such as medical providers and local governments. This

form of ‘people power’ is helpful in encouraging new competitiveness and openness at the grass roots level of Southern African societies, thus complementing the liberalization taking place in many countries at the central government level.

5.3 Establishing privately-managed individual savings schemes

The major alternative to social insurance being debated in Southern Africa and elsewhere is the privatized individual savings approach. Advocated by the World Bank, this reform has been undertaken in recent years by a number of countries in South America and Central Europe.⁹⁶ Chile is the international trend leader with a system now in operation for nearly two decades.

In Chile, workers’ retirement savings are held and invested by private pension management firms. These firms offer varied investment options, compete for members, charge fees for their services, and report regularly to workers on investment yields. Membership in one AFP or another is mandatory for all public and private sector employees entering the work force except for the military, which established the scheme. AFPs are regulated by a specialized government agency to ensure their financial solvency. The contribution rate is ten percent of monthly earnings (there is no employer match), and workers must also purchase private disability and life insurance. At retirement age (65 for men and 60 for women), they may choose either to purchase an annuity or to begin a series of phased withdrawals. For those whose savings turn out to be inadequate, the government provides a minimum benefit funded from general revenues.⁹⁷

What is the potential of this reform to address the problems which characterize social security in Southern Africa? The evidence suggests that, on the whole, it is not well-suited to these environments. See Table 24.

Table 24 Privatized individual savings schemes: impact on reform criteria

LIMITED RESOURCES	NARROW COVERAGE	COSTLY ADMINISTRATION	VULNERABILITY TO INFLATION
No, long-term benefit schemes are costly; and there are no cross-subsidizes for low income workers.	No, could worsen the current scope of coverage through reduced compliance.	No, administrative costs are high.	No, schemes are highly sensitive to the relation between inflation and investment returns.

5.3.1 Limited resources

Contribution rates must be set at relatively high levels to finance long-term benefits, and the individual savings approach provides no cross-subsidies for low-income workers. In addition, workers must purchase supplemental disability and life insurance, further increasing costs.

⁹⁶ The South America countries are Argentina, Bolivia, Chile, Columbia, Mexico, Peru, and Uruguay. Also see James, Estelle, “New Models for Old-Age Security: Experiments, Evidence, and Unanswered Questions,” *The World Bank Research Observer*, Vol. 13, No. 2, August 1998, p. 279.

⁹⁷ This benefit is 85 percent of the legal minimum wage, rising to 90 percent for those age 70 and above.

5.3.2 Narrow coverage

The Chilean experience shows that narrow coverage is a major problem of privatized savings schemes. With multiple competing firms, workers who wish to avoid making contributions find it easier to avoid detection. At the same time, private firms concerned primarily with the financial bottom line of their operations have little motivation to seek out individual evaders, particularly low-income workers whose savings (and commission fees) will be small. In Chile, about 86 percent of the workforce is covered by the AFP scheme; but only 55 percent comply. Moreover, compliance is skewed toward the upper end of the income scale, with funds catering to higher paid workers achieving 80–90 percent compliance while funds for lower paid workers achieve rates of only 45–55 percent.⁹⁸

5.3.3 Costly administration

Reliance on multiple private firms to administer savings schemes also means a loss of operational efficiency since, with fewer workers per firm, it is impossible to achieve the same economies of scale as with a single administering agency. In addition, the Chilean experience indicates that private firms advertise extensively in an effort to attract customers from their competitors, further driving up administrative costs. The costs of managing worker accounts run at about 15 percent of annual contributions; and the costs of converting these savings to annuities at retirement may raise this by half again. Given the lesser developed systems of administration in Southern Africa, they would probably be higher yet in this region.

5.3.4 Vulnerability to inflation

Fully funded schemes are very sensitive to the relation between inflation and investment returns. While investment returns in Chile during most of the past two decades have been high (in the neighbourhood of 12 percent per annum), recent financial difficulties in Asia and South America have caused a reversal. The size of the losses has led the country's Undersecretary for Social Security to advise workers approaching retirement to continue working until conditions change.⁹⁹

In Southern Africa, there are fewer productive options for investment, capital markets are less well developed and regulated, and returns are often offset by currency deterioration. These problems are reflected in much lower earnings than those achieved in South America. See Table 25.

⁹⁸ Roger Beattie, "Evaluating the World Bank Model", 13 February 1996, p. 3.

⁹⁹ Horlick, Max, "Reversal of Fortune in Latin America," *IBIS Review*, Volume 13, No. 8, March 1999. Sources: Spencer Charles D and Associates, Inc, Chicago, p. 14.

Table 25 Southern African stock exchanges, financial performance, 1998

STOCK EXCHANGE	YEAR ESTABLISHED	NO. LISTED COMPANIES	US\$ CAPITAL RETURN, 1998	EXCHANGE RATE CHANGE
Botswana	1989	12	14.3%	-14.5%
Mauritius	1989	40	5.8%	-10.9%
Malawi	1995	3	-25%	-57.3%
Namibia	1992	33	-46.6%	-17.3%
South Africa	1887	642	-27.6% ¹⁰⁰	-17.3%
Swaziland	1990	4	NA	NA
Tanzania	1998	NA	NA	NA
Zambia	1994	7	-58%	-57.3%
Zimbabwe	1896	66	-54.8%	-49.2%

Source: Mbendi, *Newsletter of Standard Bank London Limited*, 28 February 1999.

Moreover, the strongest advantages of social insurance -- i.e., wage-related benefits which are paid periodically throughout a contingency -- are not features of the individual savings system. With no pooling of risks or resources among scheme participants, these schemes make no benefit promises and provide no guarantees of any particular yield. Instead the risk of poor investment returns is shifted entirely to workers, whose retirement savings may turn out to be inadequate. Moreover, because workers may choose to withdraw their savings gradually rather than purchasing an annuity at retirement, this approach poses the risk that they will outlive their savings. In Chile, the government has attempted to address these problems by providing a guarantee of a minimum benefit funded by general revenues. However, as shown in Chapter 3, such a guarantee is beyond the financial reach of most Southern African countries and costly for the few which have established it.

5.4 Strengthening social insurance

As has been shown, the problems which impede social security schemes in Southern Africa are rooted in larger general weaknesses in the region's political and economic systems. While progress is being made on both fronts, it is necessarily a long-term undertaking; and there are no easy shortcuts to making social security work in the absence of larger changes. This section therefore considers how best to synchronize the development of social insurance with the economic and political progress that is now underway. It offers five suggestions, followed by an evaluation similar to the ones just made.

5.4.1 Start out slowly

In countries with little or no social security, governments face the issue of when and how to begin development. In a region with enormous unmet needs, they often feel pressure to move ahead. However, there are risks associated with doing so in the absence of basic prerequisites. The first is a sense of nationalism which is broadly shared by the population,

¹⁰⁰ The all-share index on the Johannesburg Stock Exchanges produced returns of 50.3 percent in 1993, 19.9 percent in 1994, 6.2 percent in 1996, and 6.8 percent in 1997, when it experienced a sharp downturn as a result of the Asian financial crisis.

needed as a basis for the pooling of risks and resources across the covered work force. Given that most national boundaries in Southern Africa were established by colonial governments, tribal affiliation often determines social relations and government allocation of jobs and benefits. For a social insurance scheme to succeed, workers must also be willing to pool risks and resources based on national solidarity.

Second, a scheme must be designed to complement other national goals. No type of social security scheme can exist if it is in conflict with a people's other basic aspirations. Ensuring such consistency requires a tradition of active consultation among government and its social partners.

Third, government must be able to ensure the long-term stability of an administering agency. Many individuals will participate in a scheme for 35 years or more, either as contributors or beneficiaries. The administering institution must be stable enough to give them confidence that it will fulfill its promises when the time comes.

Fourth, a government must be able to collect contributions and manage them for their intended purpose. No matter how needed or badly desired, the objectives of a contributory scheme cannot be achieved if workers or employers are able to avoid making required payments or if resources, once collected, are diverted to other purposes. This is a key criterion and major challenge for Southern Africa.

5.4.2 Build on demonstrated government proficiencies

A tenet of popular management literature is that every large organization that works must have evolved from a successful smaller one. Its corollary is that a large organization that does not work cannot be made to do so. Both observations point to the need to develop small and efficient social insurance bureaucracies before expanding their tasks. There are two possible approaches.

One option is to make the first step the establishment of a short-term benefit scheme. Namibia provides an example of this development path and reveals its advantages. First, short-term benefits *respond to workers' most pressing concerns*. As shown in Chapter 4, benefits to address short-term needs are given high priority by workers. Expressing this sentiment, one social security official from the region noted:

SADC countries need to achieve a better balance between short- and long-term savings. Outsiders tend to emphasize pensions as the most pressing need, but there are a host of problems that can occur before a Southern African worker reaches retirement age. In addition, these new retirement schemes place large sums at the disposal of governments that won't be held accountable for making payments for many years.

Second, because short-term benefits can be put in place rapidly, workers and employers receive *swift feedback on the administering agency's performance*. They do not have to wait a decade or more to observe whether the scheme is keeping its commitments. Third, as noted above, short-term benefits require *smaller financial reserves* and may therefore be less attractive as a source of revenue for other purposes. Fourth, short-term benefits are *easier to administer* than pension schemes. Eligibility determination and benefit computation are simpler processes, and the need for long-term record keeping is reduced. Fifth, with contribution rates in the neighbourhood of one to two percent of wages, short-term benefit schemes are *more affordable* than pension schemes; and they do not exhibit a rising cost curve which requires that pension contribution rates be increased over time. Finally, because short-term benefits are of much greater interest to the informal sector, a scheme which offers them is *in a stronger position to extend coverage* to excluded groups. From this

perspective, it is not surprising that the first social insurance schemes in Europe were not pensions but short-term benefits.¹⁰¹

A second approach is to convert an existing employment injury scheme to social insurance. Today half the countries in Southern Africa operate individual employer liability schemes which mandate that employers compensate injured workers directly. Because these schemes provide only lump-sum payments, their conversion to systems of shared risk based on social insurance principles would improve protection significantly. At the same time, conversion would involve the creation of a national administering agency whose performance could serve as a gauge of the country's readiness for new initiatives.¹⁰² Malawi is an example of a country which is pursuing conversion as a first step in expanding social protection.

5.4.3 Seek economies of scale in administration

As shown in Chapter 3, a striking feature of social insurance schemes in the region is their formal autonomy from government. With two exceptions (Mauritius and South Africa), they are structured as parastatal organizations with tripartite boards of directors. They have their own enforcement teams, do not normally share information with government agencies, and have not sought to establish "one stop shopping" which would enable workers to deal with a single agency in applying for multiple benefits.

While some observers hold that such autonomy is helpful in preventing government interference which might impede the schemes' efficiency, regional experience fails to confirm this view: the highest levels of efficiency have been achieved by the two schemes operated directly by government. Moreover, a key source of inefficiency at the parastatals is their broad responsibility to administer social insurance without coordination with other organizations with related mandates and functions. Given their isolation, their efficiency could be increased through devising cooperative arrangements for administration. Like the others, this is a long-term proposal whose success hinges on stronger governance and economic development. Some current examples are, however, suggestive of the possibilities.

In Namibia, the government will award tenders to private firms only if they present evidence of having paid their employment injury contributions. In South Africa, the UIF and Welfare Department (social pension scheme) recently shared lists of their respective beneficiaries in order to identify ineligible recipients.¹⁰³ In Zimbabwe, the workers compensation scheme is amending its application form to enable trade unions to file claims on behalf of injured workers. In Tanzania, associations of informal sector operators carry the major burden of administering health insurance schemes -- e.g., collecting contributions, negotiating with providers, and authorizing treatment. There is also potential for "piggybacking" on existing administrative arrangements in other areas. In Malawi, the government has established a number of ties with small holders which might be used for collecting contributions -- e.g., free deep-dunks for removing parasites from livestock, a program for loaning poultry which has a national register of participating farmers, and requirements that tea and tobacco grown by small holders be sold only through national associations, which register and keep track of them.

¹⁰¹ The first social insurance schemes were created by the government of Germany between 1883 and 1889. Sickness insurance was initiated in 1883 and was managed by existing mutual aid funds. Employment injury followed in 1884, administered by employers' trade associations. Invalidity and old age followed in 1889. ILO, *Introduction to Social Security* (Geneva, 1984), p. 3.

¹⁰² Social insurance schemes for employment injury do not, however, require that administrators engage in long-term record keeping for individual workers, since benefits are financed entirely by employers.

¹⁰³ The comparison revealed 1,015 duplicate cases, amounting to a savings of 477 million Rand per month, as of 14 September 1998. R.H. Alley, RSA Department of Welfare, "Presentation on Social Assistance," 19 November 1998.

5.4.4 Invest in national statistics and information systems

The preceding chapters show that scheme operational efficiency is severely impeded by the absence of up-to-date national statistical data and information systems. In their absence, the UIF is beset by fraudulent claims which it cannot detect and high levels of employer non-compliance; the universal pension scheme in Botswana must rely on six-member Age Assessment Committees in each district of the country to make what could be routine eligibility determinations; Namibia is planning to launch its national pension scheme without providing cost-of-living adjustments; and the RSA Welfare Department has reregistered entire provincial populations of social pension beneficiaries to detect deaths. The information needed to streamline these operations includes annual rates of inflation and wage growth, birth and death records, and information on the identity of employers and employees. In planning for the launch of social insurance schemes, governments should invest in developing the systems which generate this information as a very high priority. This is a key area where strengthening social protection can promote and reinforce national economic development.

5.4.5 Tiered pension benefits

Chapter 1 described a set of trade-offs inherent in the choice among systems for pension financing and discussed the difficulties which these trade-offs present for pension design. On the one hand, full funding results in rates of contribution which are stable over time; but this stability is achieved at the cost of: (i) the build-up of a large national reserve which can make a scheme vulnerable to inflation, mismanagement, and poor investment returns, and (ii) a long time lag -- perhaps three decades -- between the inception of the scheme and the point at which it can begin to pay full benefits. This lag prevents the first generation of workers under a new scheme from benefitting from it.

On the other hand, pay-as-you-go and partial funding can avoid a large accumulation of reserves and thereby minimize the vulnerability to inflation, misuse, and poor economic performance which it entails. They can also begin to make payments within a few years, so that the current generation of workers benefit from a new scheme. These advantages are achieved, however, at the cost of rising contribution rates. See Table 26.

Table 26 Pension financing trade-offs

FINANCING METHOD	ADVANTAGES	DISADVANTAGES
Full funding	Stable contribution rate	Large fund build-up creates vulnerability to inflation, misuse, and poor financial performance
	If invested wisely, scheme reserves can help to foster economic development	First generation of workers will derive limited benefits from the scheme
Pay-as-you-go or partial funding	Smaller reserve fund lessens scheme vulnerability to inflation, misuse, and poor financial performance	Rising contribution rate
	First generation of workers can derive full or nearly full benefits	Because reserve fund is smaller, reduced potential to use reserves for economic development

(i) Resolving the trade-offs

Under today's political and economic conditions, the optimal choice in a regional context seems clear: full funding poses greater risks, as evidenced in the poor performance of national financial markets and provident funds. Thus, the pragmatic question for countries which wish to proceed with launching pension schemes now is not how to avoid rising contribution rates but how to mitigate this effect. Here the best approach is a mixed system which sets wage replacement rates at modest levels and relies on private supplementation. This can be achieved through a system of tiered benefits structured as follows:

Table 27 A tiered pension benefit structure

TIER ONE	TIER TWO	TIER THREE
A minimum income related to subsistence levels, provided as a means-tested or universal payment.	A compulsory social insurance scheme which is operated on a pay-as-you-go or partially funded basis, provides modest benefits, and has a redistributive component for low-income workers.	A voluntary, complementary tier which meets individuals' need for supplementation of the basic benefit through a variety of fully-funded arrangements including private pension schemes, personal savings, and personal pension plans.

As shown in the analysis of non-contributory schemes (Chapter 3), tier one can be only a long-term goal for most Southern African countries; but it would be useful for long-term planning purposes to accept it in principle as the primary form of social protection for those with no earnings. Moreover, if tier one is means-tested, the establishment of tier two will serve to reduce its costs and increase its affordability over time. Tier three can consist of a variety of arrangements which cater to the tastes and preferences of middle and upper income workers who have additional resources to spend on retirement protection. Whatever the types of benefits and administrative arrangements for tier three, the success of the tiered approach is dependent upon tier two having several features.

(ii) Important tier two features

First, it is important that tier two provide a pillar of basic protection to all formal sector workers, regardless of their level of earnings, savings, or access to other benefits. Without compulsory coverage under tier two, those workers who lose their tier three personal retirement savings unexpectedly -- i.e., through job loss, bad investments choices, or poor performance by financial markets -- will have no earnings-related cushion to fall back on. They will face destitution and/or place a drain on public resources via means-tested assistance.

Second, tier two benefits should be set at modest levels.¹⁰⁴ By keeping wage replacement rates modest, contributions can also be set lower; and they will have to increase less steeply as the scheme matures. The rising cost curve will not disappear, but its angle can be flattened.

Third, in Southern African countries, it is important for tier two to include a distributive element which provides a higher rate of wage replacement for workers at the lower end

¹⁰⁴ This raises the question of what level of benefits should be considered modest. As the ILO Conventions on Social Security do not envision a tiered benefit scheme, this is an area for new thinking and analysis. The most widely examined model is the U.S. Federal Employees Retirement System (FERS), where tier one is set to equal 30 percent of a worker's high three years of wages. However, FERS membership is disproportionately high income workers for whom 30 percent of high wages goes further in meeting basic needs than the equivalent wages of a low-income worker. Thus, for schemes with a more heterogeneous membership, it is appropriate to boost the replacement rate for those at the lower end of the income scale to at least the ILO benchmark of 40 percent of earnings after a working career of 30 years.

of the income scale. This is needed because most low-income workers will be unable or unwilling to supplement their basic benefit through tier three, as shown by low compliance among low-income workers in Chile. Tier two will thus be their only source of retirement protection. In addition, a redistributive benefit formula can help to address the skewed distributions of income which characterize most Southern African countries today. Because this can be done without means testing, there is no social stigma for low-income workers and no financial disincentives for them to work or save.¹⁰⁵

Together these features serve to strengthen private supplemental arrangements under tier three in several ways. A requirement for participation by all formal sector workers in tier two means that government regulation of tier three can be less stringent than if it were the sole or major vehicle for social protection. Less constrained by regulation, tier three schemes can offer workers more varied investment options, including instruments which pose higher risk and offer higher potential profit. This helps to diversify the market for supplemental retirement savings, enabling it to satisfy a wider range of worker preferences. At the same time, modest tier two benefits encourage workers to invest in tier three supplemental coverage.

(iii) Other mixed systems

While there is wide agreement these days on the wisdom of mixed retirement systems, arrangements other than tiering are also possible. An option widely advocated by some pension funds in the region involves excluding those with tier three coverage from tier two, effectively making these tiers alternatives. For a worker who has such existing occupational coverage or an employer who provides it, this arrangement may seem quite logical. From a broad public policy perspective, however, it is inferior to the tiered benefit structure for several reasons.

First, exclusions from participation in the public social insurance scheme would presumably be provided only to those with equivalent private coverage; but *deciding what is equivalent would be a complex and difficult task*. Cost-of-living increases vary widely from scheme to scheme, as do benefits for dependents, survivors, and disability. As a result, decisions would be messy, difficult to reach, and likely to produce dissatisfaction among those who are excluded from the public scheme as well as those who are required to participate.

Second, the option to rely on private occupational coverage as a substitute for social insurance creates a *major need for regulation* of the former, as shown by the Chilean experience. For example, it would be necessary to prohibit the withdrawal of pension savings upon termination of employment, a popular option among workers in Southern Africa. In addition, the portability of pension rights from job to job would have to be ensured, a very complex task.

Third, if portability is less than complete, some workers will make contributions to two separate schemes over a period of years but in amounts which are insufficient to qualify for benefits under either. In effect, they will *slip through the holes in the social safety net*. This is a particularly serious risk in the event of disability.

Finally, the ability to opt out of tier one could *threaten the financial solvency of the public scheme*, since a decreasing proportion of potential contributors would participate. Exemptions would probably be sought by large establishments employing higher paid workers and providing greater employment security. Smaller, non-exempted establishments would be

¹⁰⁵ The Namibian Social Security Commission opted for a progressive formula of this type in developing proposals for a national pension scheme. It calls for workers with very low earnings receive around 70 percent replacement rates after 30 years of contributions while those at the high end of the income scale would receive 30–40 percent.

more costly to administer but would pay smaller amounts of administrative charges, as their employees tend to have lower earnings. Action by the government to remedy this problem by raising the contribution rate would encourage still more small firms to seek exemptions. This would create a downward spiral in the public scheme's membership and financing and erode the social solidarity on which social insurance must rest.

These disadvantages suggest that the optimal approach is one in which tier two: (i) applies to all workers, (ii) provides modest levels of wage replacement, (iii) includes a redistributive element for low-income workers, (iv) is financed on a pay-as-you-go or partially funded basis, and (v) is supplemented by a range of fully-funded private savings options.¹⁰⁶

5.4.6 Impact on reform criteria

How does this full set of proposals measure up in addressing the region's problems? Because a number of the proposals have multiple impacts, they are listed separately below.

Table 28 Long-term proposals for strengthening social insurance: impact on reform criteria

LIMITED RESOURCES	NARROW COVERAGE	COSTLY ADMINISTRATION	VULNERABILITY TO INFLATION
Modest positive impact from:	Modest positive impact from:	Yes, from:	Yes, from:
(i) establishing short-term protection first,	(i) investment in national statistics and information system to improvement enforcement,	(i) satisfying prerequisites for social insurance,	(i) reliance on pay-as-you-go or partially funded systems with small reserves, and
(ii) setting wage replacement rates at modest levels, and	(ii) cooperation in enforcement with other government and private agencies, and	(ii) building on demonstrated govt. proficiencies,	(ii) development of necessary statistical information for legislating annual inflation adjustments in long-term benefits.
(iii) providing cross subsidies for low-income workers.	(iii) establishing short-term benefit schemes, which are of great interest and more affordable to informal sector workers.	(iii) investing in statistics and information systems needed for scheme administration; and	
		(iv) seeking economies of scale through cooperative arrangements for administration and enforcement	

As can be seen, the overall result is positive but mixed, with the latter two problems yielding to the recommended actions more or less fully in the long-term while the first two are only modestly remediable. This is a reflection of the close link between social security and

¹⁰⁶ It is useful to anticipate that, if tier two is mandatory for all workers, the pension industry may exert pressure to require tier three participation as well. Such a requirement would provide them with significantly larger volumes of business. Such mandatory supplementation exists in several countries in Europe and, as noted earlier, is being planned in Swaziland as a replacement for the national provident fund. However, the viability of this approach hinges on government capacity to regulate private savings plans to ensure their solvency. As shown in section 5.3, such capacity is yet to be developed in most countries in the region. Until it exists, tier three participation should be encouraged in the ways described earlier but should remain optional to workers.

economic development. While limited resources and narrow coverage can be addressed in part by government action apart from economic development, the other problems can be fully solved only when such development improves employment and incomes.

5.5 Conclusion

The lessons derived from regional experience in this analysis point to the benefits of regular exchanges of information and experience among Southern African countries. There are no more compelling lessons than those derived by neighbours attempting to deal with similar problems and challenges. Exchanges can take a variety of forms, including tripartite meetings, newsletters, visits and training attachments to neighbouring social security institutions, and increased reliance on regional consultants in technical cooperation projects. The potential benefits to be gained are three-fold.

First, in the policy debate that typically precedes the launching of a new social security scheme, officials from neighbouring countries who have already taken this action can speak with a high level of authority. Those who have been successful in a similar setting are living proof that it can be done. Second, administrators from countries with similar economies and cultures may have faced and coped with similar administrative problems that do not arise in more distant settings. Examples include how to structure survivors benefits when families are extended, how to cope with an unreliable banking system, and how to deal with claimants for retirement benefits who have no documentation of their date of birth. A third and related advantage is that administrators from neighbouring countries can be highly motivating to people who are struggling to set up a new scheme.

ILO/SAMAT has been working to encourage and support such exchanges in recent years, and their results have been extremely positive. For example, as part of its technical support for the conversion of the Zambia National Provident Fund to a pension scheme (1997), it arranged a seminar in Lusaka by the director of the Zimbabwe national pension scheme on the lessons of its experience for the Zambian initiative. Participant evaluations showed that this was the high point of their training. As part of its social security development project in Namibia (1998), SAMAT arranged training attachments and visits to social security institutions in Uganda, Mauritius, South Africa, Ghana, and Zimbabwe. In the latter case, four senior managers from the Namibian Social Security Commission (computerization, benefits, administration, contributions collections, and finance) were attached to their counterparts at the Zimbabwean National Social Security Authority for a period of two weeks. Their wrap-up session was an exciting event in which many useful suggestions for improvement were offered by both sides. To encourage the development of informal sector social security schemes, SAMAT together with the Friedrich Ebert Foundation and the University of Zimbabwe School of Social Work sponsored a seminar in which informal sector workers from Tanzania who had started such a scheme shared their experiences and the lessons learned with Zimbabwean informal sector workers and government officials (1998). As a follow up, a group of informal sector workers from Zimbabwe visited Dar es Salaam to observe a health insurance scheme in operation. These experiences are now providing the basis for plans to establish a similar scheme in Zimbabwe. At SAMAT's request, the Mauritian Ministry of Labour and Social Solidarity has provided training in various aspects of social security administration to officials from Zambia, Zimbabwe, and Namibia (1996-99). As the oldest pension scheme in the region, Mauritius has provided both technical expertise and inspiration to its neighbours.

SAMAT stands ready to continue to assist with such exchanges. The ILO's tripartite structure enables it to provide services to trade unions and employers associations as well as government, and its decentralized structure helps to make it accessible to all three. In addition, the office can provide a wide range of technical services -- actuarial analysis, training, computerization, legislative drafting, and accounting and financial management -- to social security institutions.

SAMAT also has a range of educational materials on social security developed by the ILO which it will share with governments and their social partners.

The newly-established SADC Subcommittee on Social Security and Occupational Safety and Health also has a major role to play. Here, member states can identify and publicize best regional practices in social security; develop quantitative performance indicators to gauge administration; share information on innovations; arrange training exchanges; develop reciprocal agreements for protection of migrant workers; and issue and publicize annual reports which enhance transparency in administration.

In these ways, the region's experience, both past and present, can provide the best available guidance for those on the cutting edge of efforts to develop and strengthen social security for the people of Southern Africa.

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