CHAPTER 5

HOW EFFECTIVE ARE SOCIAL PROTECTION POLICIES IN LAC?

- A characterizing feature of labour markets in Latin America and the Caribbean is their high informality levels.
- The formal-informal segmentation of the labour force results from a mix of legal exclusions and non-compliance by firms and workers.
- Segmented labour markets are a source of inequality and one of the contributing factors in low productivity growth. The mix of contributory and non-contributory social insurance programmes across the region, coupled with transitions between formality and informality, and, at times, inconsistent rules and conditions for access, results in reduced efficacy of insurance and contradictory impacts on inequality.
- Informal workers are less well protected from risks and, in general, receive lower-quality services than formal workers.
- Informality is strongly associated with self-employment or employment in small low-productivity businesses, which is a critical factor in determining worker earnings (and a crucial factor in long-term growth).
- Social insurance and social assistance are complements and not substitutes in a working social protection system. Eligibility for social assistance programmes should not depend on the formal or informal status of workers, and the region should not expect targeted transfers on their own to reduce poverty.
- A guiding principle for social protection in the region must be universality in social insurance systems, understood in three dimensions: (i) the entire population exposed to a given risk covered through the same programme; (ii) the source of financing the same for each programme; and (iii) in-kind benefits of the same quality for all.

5.1. Social protection systems affect both inequality and economic growth

Governments throughout Latin America and the Caribbean (LAC) respond to the region's high inequality by deploying a large set of policies and programmes. Some are focused on enhancing household assets and human capital to improve household outcomes in the labour market, notably through investments in education; and on increasing household standards of living through, for instance, subsidies for housing.

In parallel, governments also deploy policies to change household incomes and consumption, including through progressive income taxes; exemptions to value added taxes or other consumption taxes on certain goods; subsidies for electricity, gasoline and the like; school meals or other programmes that distribute food; income support for the poor through conditional cash transfers (CCTs) and similar programmes; insurance against risks, such as illness, disability and death; pensions for the elderly; minimum wages; training programmes to improve workers' opportunities in the labour market; special tax regimes for small firms; microcredits for low income entrepreneurs, and so on. The list varies from country to country, but, in most countries, it is long. Numerous or not, these policies show the deep concern among governments in LAC about inequality, a welcome response given the situation documented in chapter 1.

Good intentions are not enough. Judging by the region's high and persistent income inequality, policies focused on changing household incomes and consumption are not as effective as they could be and certainly not as circumstances demand. This is apparent if one compares the most widely used measure of inequality, the Gini, before and after taxes and transfers in LAC countries and other regions (see chapter 3).

This chapter analyses some of the main programmes and policies implemented in the region to combat inequality: social insurance and labour regulations to protect workers from risks, such as illness, disability, death and the vagaries of the labour market; minimum wages to help individuals with low incomes; programmes to transfer benefits to poor households, and special tax regimes to support low-income entrepreneurs and promote small firms. These policies are jointly considered under the umbrella of social protection, and the chapter focuses on them for two reasons: (1) in most countries in LAC, they attract an important share of the national budget allocated to increase social welfare; (2) they impact the behaviour of workers and firms in the labour market and thus, indirectly, the performance of the economy and the opportunities that workers have to increase their incomes over their lifetimes. The chapter evaluates these policies from two separate but complimentary dimensions: (1) their effectiveness in reducing inequality and (2) their impact on firm and worker behaviour in the labour market and thus on productivity. The chapter provides another perspective on the links between high inequality and low growth, complementing those presented in chapters 3 and 4, and building on 12 background papers produced specifically with this purpose.[1]

A couple of caveats are in order. First, the chapter focuses only on a subset of policies and programmes. There is no discussion of income taxation and little analysis of taxes on consumption or subsidies for electricity or gasoline. Because these tax and subsidy policies are also important determinants of inequality, it is essential to complement the discussion here with an analysis of their impact. There is always a trade-off between breadth and depth, and, hopefully, the analysis in this chapter, while incomplete, is sufficiently informative and suggestive of areas in need of attention by policymakers interested in simultaneously reducing inequality and accelerating growth.

Second, there is large heterogeneity in the social protection policies deployed in the region. The chapter focuses on common trends and features, but their individual relevance varies from country to country. Each country is different, and their specificities and peculiarities have to be considered. Comparisons across countries must be carried out with care not only because laws and institutions vary, but also because, even in countries with similar laws and institutions, the quantitative importance of the various factors that determine outcomes also vary.

The chapter proceeds as follows. Section 5.2 introduces a simple framework to help in understanding the complex structure of social protection in LAC. Section 5.3 describes three stylized facts on labour markets in LAC that play a central role in social protection outcomes. Sections 5.4 and 5.5 combine the framework and stylized facts to explore the impact of social protection on inequality and productivity. Section 5.6 concludes with a proposal for a substantive change in social protection.

5.2. The structure of social protection

Social insurance

The cornerstone of social protection in LAC is the combination of social insurance programmes for workers in firms and regulations on job stability and minimum wages. This combination has been in place in most countries since the 1930s or 1940s, and, although it has evolved since then, its main features persist and continue to play a dominant role in social protection and growth outcomes.

---

[1] The country studies are as follows: Argentina: Alzúa and Pacheco (2021); Brazil: Firpo and Portella (2021); Chile: Morales and Olate (2021); Colombia: Alvarado, Meléndez, and Pantoja (2021); Dominican Republic: Barinas and Ñopo (2021); Ecuador: Ñopo and Peña (2021); Honduras: Ham and Membreño Cedillo (2021); Jamaica: Mera (2021); Mexico: Correa et al. (2021); and Perú: Ñopo (2021). The conceptual framework is covered by Levy and Cruces (2021), and the minimum wage by Flabbi (2021).

Various features of this combination are relevant. First, social insurance programmes are by and large limited to workers who have a relation of dependency and subordination with firms and receive monetary remuneration in the form of wages or salaries. Second, they are financed mostly from contributions by firms and workers that are proportional to worker salaries or wages, which leads to the contributory social insurance (CSI) label. Third, programmes to insure against the risks of illness, disability, accidents at work, death, and longevity and, in a few countries, loss of employment are bundled. Fourth, workers who are covered are also subject to regulations on job stability and minimum wages, so that the bundle of CSI programmes is in turn bundled with these regulations. Fifth, benefits bear the role of legal entitlements that can be enforced through the courts. But the most important feature of this combination is, sixth, that it does not cover all workers. Many are left out, principally the self-employed, but also, in some cases and with some variation across countries, entrepreneurs, agricultural and domestic workers, workers who do not receive a monetary remuneration, workers in firms who are relatives of the firm owners and share the surplus of the family enterprise, and workers in firms who are not under a relation of dependency because they are paid on a piece-rate or other like basis. Independent workers providing services to firms under a commercial rather than a labour contract as employees may also be left out (box 5.1).

Box 5.1: Exemptions to CSI, job stability and minimum wage regulations

Argentina: Non-remunerated workers; special regimes for self-employed; entrepreneurs.

Brazil: Non-remunerated workers; special regimes for self-employed; entrepreneurs.

Chile: Self-employed and non-remunerated workers; entrepreneurs.

Colombia: Self-employed workers earning below one minimum wage; non-remunerated workers.

Dominican Republic: Self-employed, independent, domestic, and non-remunerated workers; workers in family firms, entrepreneurs.

Ecuador: Self-employed, independent, domestic, and non-remunerated workers; micro-entrepreneurs; workers in agriculture.

Honduras: Self-employed, independent, domestic, and non-remunerated workers; micro-entrepreneurs; workers in agriculture.

Jamaica: Non-remunerated workers.

Mexico: Self-employed, independent, domestic, and non-remunerated workers, workers in family firms, agricultural producers, entrepreneurs.

Peru: Self-employed, independent, domestic, and non-remunerated workers; special regimes for workers in micro-firms.

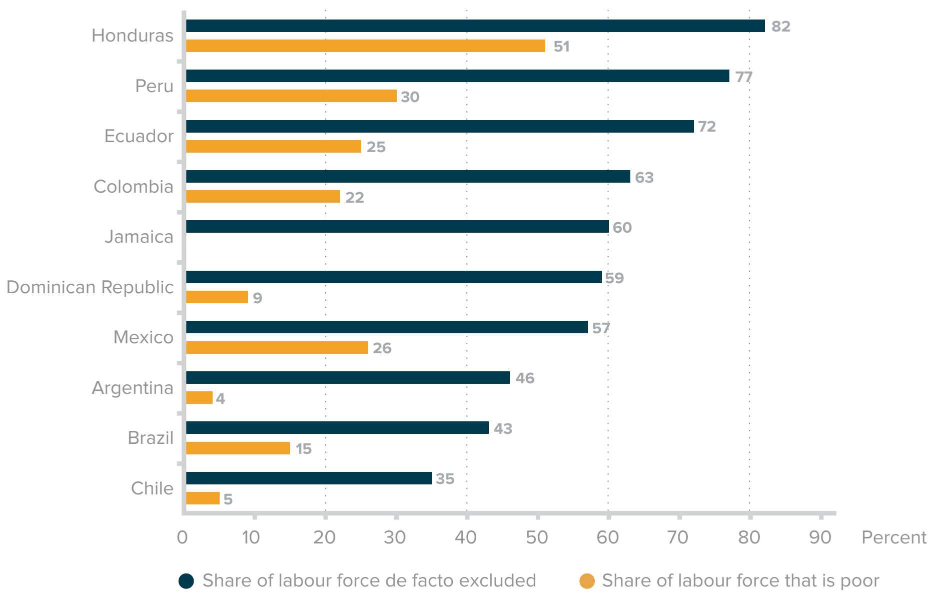
Sources: UNDP LAC Working Papers 14–23: Alvarado, Meléndez, and Pantoja 2021; Alzúa and Pacheco 2021; Barinas and Ñopo 2021; Correa et al. 2021; Firpo and Portella 2021; Ham and Membreño Cedillo 2021; Mera 2021; Morales and Olate 2021; Ñopo 2021; Ñopo and Peña 2021.

There is heterogeneity across the region. In some countries, such as Argentina and Brazil, the self-employed are required to participate in CSI programmes, although, in this case, the regulations on job stability and minimum wages do not apply. These workers are sometimes offered subsidized contribution rates, depending on their income level. In other countries, such as Colombia, the self-employed are also required to participate, but only if their income exceeds the minimum wage. But these are exceptions; by and large, the requirement to participate in CSI programmes is restricted to workers in firms under a relation of dependency who are also covered by regulations on job stability and minimum wages.

In addition to legal exclusions, another factor limits the coverage of CSI programmes: in a context in which laws and regulations are imperfectly enforced, non-compliance by firms and by the self-employed if they are required to contribute. Non-compliance may result from explicit evasion or from elusion in situations in which the borderline between a dependent and non-dependent worker is fuzzy and the requirement to comply ambiguous. Non-compliance is facilitated if the production unit is small measured by the number of participants. Authorities in charge of enforcing laws have great difficulty separating evasion from elusion and, in the case of the former, in establishing and collecting fines. Indeed, because CSI regulations may not apply to these firms, and, even if they do, they can be enforced only with difficulty, they are replaced by tacitly accepted social norms that de facto sanction non-compliance, even if de jure it may be argued that illegal behaviour is taking place. Figure 5.1 shows that, in all countries, an important share of the labour force is excluded from the most important social protection programmes—in many, more than half. For reference, the figure also shows the share of workers who are poor.

Figure 5.1: Large shares of the labour force are excluded from the most important social protection programmes

Share of the labour force excluded from contributory social insurance, selected LAC countries



Source: Levy and Cruces 2021, Background Paper of the UNDP LAC RHDR 2021; UNDP calculations using national household surveys.
Note: Workers in households under the poverty line of $5.50 a day, 2011 purchasing power parity.

This exclusion is a grave issue. In response, governments in the region have created programmes to provide some insurance to those left out. A few features of these programmes are worth highlighting. First, they are mostly restricted to health and retirement pensions, although some countries include other benefits, such as a child allowances (Argentina) or childcare services (Mexico). Second, benefits measured either by quality or monetary value are generally subpar compared with those offered by CSI programmes, and they exclude any income floors or protections against the loss of employment. Third, they are financed from general government revenues, a key difference from their CSI counterparts, which are paid from contributions by firms and workers; for this reason, these programmes for the otherwise excluded are labelled non-contributory social insurance (NCSI). And fourth, they are usually offered to all workers excluded from CSI programmes, regardless of whether this results from a legal mandate or non-compliance.

As with CSI, there is heterogeneity across the region. In Colombia, for instance, contributory and non-contributory health programmes in principle provide the same benefits. Mexico's non-contributory pensions cover all the elderly, even if some have a contributory pension. In Brazil, a single health programme financed from general revenues covers all workers, making irrelevant the contributory/non-contributory distinction for health coverage, but not for pensions. In Chile, the government contributes to CSI programmes, which might therefore be labelled semi-contributory. There are, indeed, many country specificities, and the contributory–non-contributory classification should be considered a conceptual distinction rather than a sharp divide that applies equally to all countries in LAC.

The key point is that the interphase between the design and operation of CSI and NCSI programmes, on the one hand, and enforcement, on the other, segments the labour force into two categories: formal workers, who are covered by CSI programmes and job stability and minimum wage regulations, and informal workers, who receive whatever benefits are offered by NCSI programmes.

The formal-informal segmentation of the labour force, the central feature of labour markets in LAC, results from a mix of legal exclusions and non-compliance. In countries where all are required to participate in CSI programmes, such as Jamaica, segmentation results only from non-compliance. But, in other countries, segmentation would persist even under full compliance because some workers are simply not required to participate. Informality is a complex phenomenon that results from institutions, laws, and law enforcement. Across LAC countries, it is partly legal and partly illegal, and the segmented labour markets are not only a source of inequality, but also one of the contributing factors to low productivity growth.

Social assistance

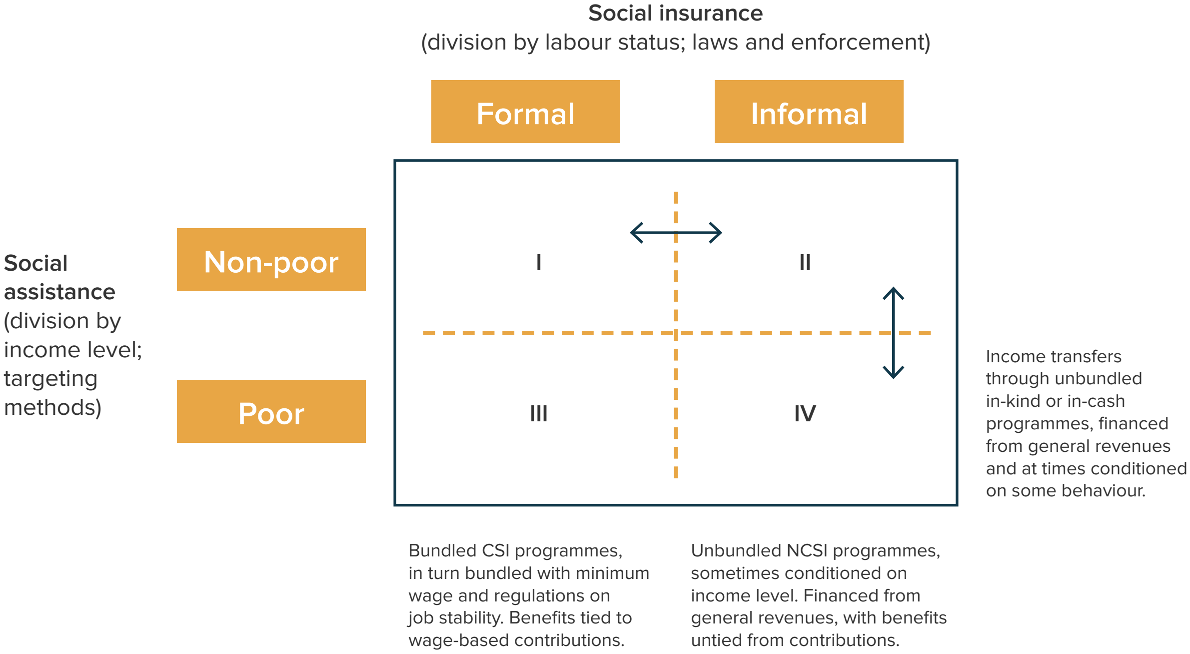
Because all workers are exposed to risks, such as illness, disability, unemployment, or death, regardless of their incomes, CSI and NCSI programmes should cover all. In parallel, however, some worker incomes may be so low as to place the workers in poverty, requiring additional programmes to increase their consumption. These social assistance programmes are by definition focused on a subset of the population, and their main objective is to redistribute income in favour of this subset.

The distinction between social insurance and social assistance programmes should not imply that the former do not redistribute income. In most cases, they do (although not always in the desired direction!). Rather, the point is that, even if there were a society without poverty and thus with no need for social assistance, social insurance programmes would still be needed to pool risks among the population and protect society from negative shocks. Yet, the fact that poor workers benefit from social assistance programmes does not eliminate the need of these workers for social insurance. They face the same risks faced by non-poor workers. Clearly, it would be a mistake to think that social insurance programmes are only for the non-poor.

Figure 5.2 synthetizes this discussion by separating workers according to their labour status and income, the vertical dotted line by labour status, formal and informal, and the horizontal line by income, poor and non-poor. Leaving out unemployment, the sum of workers in the four quadrants equals the labour force. Although sometimes lumped together, poverty and inequality are not the same. In most countries, there are more informal workers than poor workers (that is, more workers in quadrant II than in quadrants III and IV). Nonetheless, most poor workers are informal (that is, more of them are in quadrant IV than III).

Figure 5.2: Poverty and informality are not the same

Structure of social protection



Source: Levy and Cruces 2021, Background Paper of the UNDP LAC RHDR 2021.

Figure 5.2 is a stylized description capturing commonalities among programmes across countries in the region. There are also important differences. CSI programmes differ not only with respect to their mandated coverage, but also in terms of their costs, scope, quality of benefits and nature of enforcement. The same is true of minimum wages and regulations on job stability. NCSI programmes also differ in terms of their generosity and rules of access, sometimes covering all informal workers and sometimes only those workers who are poor. Social assistance programmes differ in the methods used to identify those who are poor (targeting techniques), rules of access and benefits. The resulting interaction among all these elements is complex and requires a case-by-case analysis, as exemplified in the 10 country studies that are background papers of this report.[2]

[2] UNDP LAC Working Papers 14–23: Alvarado, Meléndez, and Pantoja (2021); Alzúa and Pacheco (2021); Barinas and Ñopo (2021); Correa et al. (2021); Firpo and Portella (2021); Ham and Membreño Cedillo (2021); Mera (2021); Morales and Olate (2021); Ñopo (2021); Ñopo and Peña (2021).

Figure 5.2 serves to make an important observation: in LAC, access to social protection results from the interphase of the formal or informal status of workers in the labour market and their income. Because worker incomes also depend on labour market performance, outcomes in this market become the central determinant of the efficacy of social protection: which workers of which income level have access to this or that health, pension, childcare, or other programme; which are protected in the case of disability, death, or the loss of employment; who is paid at least the minimum wage; which programmes are paid from contributions by firms and workers and which from general tax revenues; and, as a result, how much income is redistributed across households and in which direction.

In all countries, the distribution of workers among the four quadrants of figure 5.2 results from the decisions of millions of firms and workers, which depend on a large set of policies, many far removed from social protection: regulations on international trade, credit, property rights, and so on. But the distribution also depends on (1) the set of policies and programmes directly associated with social protection—CSI programmes and job stability and minimum wage regulations, NCSI programmes and social assistance programmes; (2) the functioning of these, as given by their costs and by the rules of access and the quality of benefits; and (3) the enforcement of the associated laws and regulations.

Firms play an important role in social protection because they are the demand side of the labour market. Social protection outcomes therefore depend on what firms do. However, what firms do depends on social protection policies. Figure 5.3 depicts the two-way interdependence between firms and social protection, an interdependence that is not always fully appreciated.

The interdependence between firms and social protection is an inevitable outcome of the way social protection is structured in the region, particularly social insurance, dependent as it is on the formal-informal status of workers. This interdependence implies that, in any country in LAC, if social protection policies were different, the same workforce with the same human capital would be distributed differently among the four quadrants of figure 5.2. In other words, if these policies were different, the number of individuals in each quadrant would change, and so would social protection outcomes. The two-way arrows in figure 5.2 highlight that this distribution depends on social protection policies. This leads to an observation that has not been appreciated adequately: the design of social protection policies, while focused on household welfare, needs to pay careful attention to the impact of the policies on firms because social protection outcomes depend heavily on what firms do.

Figure 5.3: Social protection outcomes depend on what firms do; which depends on social protection policies

- Are there many firms without dependent workers?
- Do firms comply with laws on CSI, job security and minimum wage regulations?
- Are there many micro or small firms where the relation of dependency is ambiguous?
- What is the skill composition of the labour demand of firms?
- Do firms offer workers short- or long-term contracts? How many firms invest in labour training?
- Do firm entry, exit and growth patterns increase worker productivity?

- How costly are CSI contributions? What is the quality of benefits and the rules to access them?
- Do job stability regulations allow firms to adjust to negative shocks? Are minimum wages high or low?
- Is enforcement of CSI and minimum wage laws dependent on firm size? Can firms replace them with tacitly accepted social norms if the firms are small?
- Are there special tax regimes for low-income entrepreneurs? Do they vary with firm size?
- Do firms evade more if NCSI programmes are present or expanded?
- Do the self-employed have to participate in CSI programmes?

Source: Levy and Cruces 2021, Background Paper of the UNDP LAC RHDR 2021.

The distinction between CSI and NCSI programmes in figure 5.2 is almost meaningless from the perspective of the countries of the Organisation for Economic Co-operation and Development (OECD), in which the coverage of social insurance programmes is close to universal. Indeed, in these countries, all NCSI programmes targeting subsets of the population would likely be considered social assistance programmes. But, in LAC, the distinction between CSI and NCSI is central because it reflects the fact that entitlements and obligations with respect to social insurance differ depending on how workers participate in the labour market. And the distinction between NCSI and social assistance programmes is also central because it responds to two different circumstances: the lack of coverage by CSI programmes of workers who are not necessarily poor and the low incomes of some households even if household members have jobs with CSI coverage. There is an important overlap between households that lack CSI coverage and households that are poor, contributing to the conflation of NCSI and social assistance programmes. But this overlap is not perfect because there are some poor households with workers who are covered by CSI programmes and some non-poor households that benefit from NCSI programmes (in fact, in some cases, they benefit more than poor households do).

The result is that the structure of social protection in LAC is substantially different from that in OECD countries. Furthermore, the diversity of funding sources, the multiplicity of programmes, the differences in rules on who is entitled to what and when, and the weakness of the institutions enforcing contributions and delivering benefits make for a complex environment. As one would expect, firms and workers react to this environment. Firms react because it determines when they must pay for the social insurance of their workers and when not; when they can evade contributions and when not; when they can adjust to negative shocks and when not. They will adjust their business decisions accordingly. Similarly, workers react because, depending on whether they work on their own or are employed by firms as dependent workers, they may or may not have to contribute for some benefits; they may or may not have access to benefits that neither they nor the firm employing them have to pay for; and, depending on their income, they may or may not qualify for other benefits, or may lose them, if their income or labour status changes.

The weakness of the region's institutions, which is sometimes conceived of as limited state capacity, creates important gaps between the de jure letter of the law and the de facto meaning of the law for the everyday life of workers and firms. These gaps may vary by firm size, as is the case in the enforcement of the minimum wage or job stability regulations, for instance, but they may also vary by region, such as when the quality of benefits like health services vary between, say, large urban areas and more remote rural ones. In some cases, as a result of these gaps, tacitly accepted social norms rather than laws govern the relations between firms and workers.

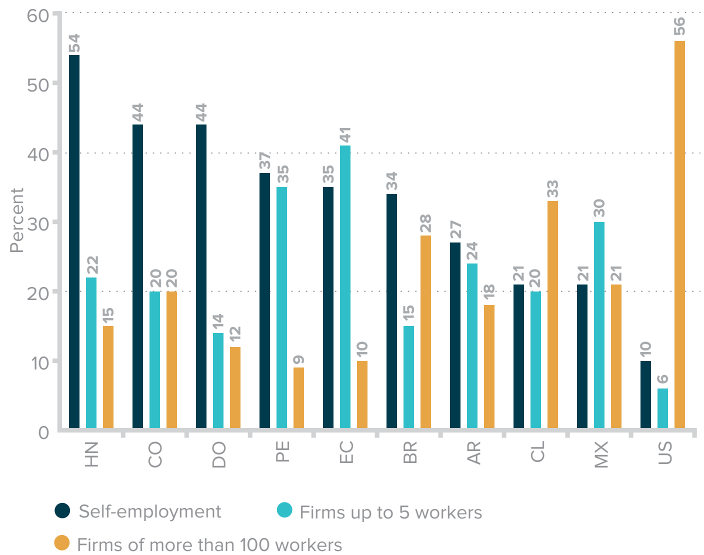
5.3. Three stylized facts about the labour markets in the region

The distribution of employment

In most countries, because self-employed workers are not required to participate in CSI programmes and because, even if they are, enforcement is weak, the share of these workers in total employment matters substantially for social protection. In addition, because non-compliance with CSI, job stability, and minimum wage regulations is greater among smaller economic units, the number of workers employed by firms at various sizes also matters. In this vein, figure 5.4 presents data on the share of workers who are self-employed, employed in firms with up to 5 (or 10) workers, or employed in larger firms in various LAC countries and, for reference, the United States. Although the data are not fully comparable because the labour and firm classifications used by countries do not always coincide, they still offer a useful picture.

Figure 5.4: A large share of the workforce in LAC is dispersed in self-employment or in small firms

Self-employment and employment distribution by firm size



Sources: UNDP LAC Working Papers 14–23; SUSB (Statistics of U.S. Businesses) (dashboard), US Census Bureau, US Department of Commerce, Suitland, MD, https://www.census.gov/programs-surveys/susb.html.
Note: Firms up to five workers: Chile, up to 9 workers; Dominican Republic, Ecuador, Honduras and Peru: up to 10 workers. Firms of more than 100 workers: Brazil, Chile, Colombia, Dominican Republic and Mexico: 50 workers or more. Honduras: 150 workers or more.

Self-employment is widespread in LAC. Together with employment in small firms, it accounts for approximately half of all employment even in larger countries, such as Brazil and Mexico, and even more in some countries, such as Ecuador (76 percent) and Peru (72 percent). These numbers are important for social protection because the self-employed and workers in small firms tend to be informal (figure 5.2, quadrants II and IV). But they also matter for productivity because they imply that a large share of the workforce in LAC is employed in small units, that is, economic activity is very dispersed.

The large dispersion in economic activity means there is a large number of small firms. Although more difficult to document because few countries have a full census of firms, the existing data are unambiguous: the size distribution of firms is skewed in LAC. A vast majority of small firms employ between a half and two thirds of all workers; there are few medium-size firms, and a tiny share of large firms employ around one quarter or, at most, one third of the labour force.

In many cases, it is difficult to make a sharp distinction between the self-employed (or a one-person firm) and a micro-firm with two or three workers because the size of these undertakings is fluid. If demand merits it, they can rapidly expand to four or five workers, and, if it does not, they can contract equally rapidly to two or one, a situation facilitated by the combination of legal exclusions and tacitly accepted social norms that de facto place these firms beyond the reach of regulations on job stability. Many of these firms perform their economic activities on the street or within the household; few are incorporated as separate legal entities, and even fewer have access to formal credit at commercial banks. The viability of these firms is precarious; they are typically shortlived and exhibit high rates of entry and exit. They thus create precarious, often shortlived employment.

Considered together, self-employed workers and workers in micro-firms constitute the bulk of the ubiquitous informal sector that characterizes the region's economies, reflected in the large share of the labour force receiving benefits from whatever combination of NCSI and social assistance programmes are available, as documented in figure 5.1.

Workers in LAC are not always formal or informal

Contrary to what is at times assumed, evidence from two sources shows that workers transition back and forth between formality and informality: (1) panel data from employment surveys in a few countries that follow the same individuals over a given period and (2) administrative registries of social security agencies in other countries. Table 5.1 provides examples of the first type of data, in all cases for the years 2018–2019 (before the COVID-19 pandemic). The upper panels depict worker transitions among formal, informal, unemployed, and out of the labour force status in Dominican Republic (panel a) and Mexico (panel b). The lower panels do the same for Brazil, separating workers according to where they fall on the income distribution (panels c and d). The data on Brazil also allow the identification of transitions into self-employment.

The diagonal in each panel of table 5.1 shows the share of workers who remained in the same status from one year to the next. In Dominican Republic, for instance, of all workers who had been formally employed in 2018, only 78.9 percent had the same status one year later; 9.7 percent transitioned to informal employment, 3.3 percent to unemployment, and 8.1 percent left the labour force. More generally, at least 20 percent of workers in each case had changed status by one year later, as can be inferred by focusing on the numbers in the main diagonal of each panel. Similar patterns are observed in Mexico, but with less persistence in unemployment. The data on Brazil show that workers in the top 25 percent of the income distribution (the top 25), particularly formal sector workers, transition less into another status relative to workers in the bottom 25 percent of the income distribution (the bottom 25), indicating that the former spend proportionately more time in formality.

Table 5.1: Workers may transition among formality, informality, unemployment, or inactivity

Transitions in labour status in a single year

a. Dominican Republic

	Formal	Informal	Unemployed	Out of labour force
Formal	**78.9**	9.7	3.3	8.1
Informal	12.5	**74.0**	1.9	11.6
Unemployed	17.4	30.4	**29.0**	23.2
Out of labour force	5.7	14.7	1.8	**77.8**

b. Mexico

	Formal	Informal	Unemployed	Out of labour force
Formal	**73.8**	15.4	1.6	9.1
Informal	14.5	**64.0**	1.9	19.5
Unemployed	22.8	31.9	**15.5**	29.7
Out of labour force	6.6	15.8	1.6	**75.8**

c. Brazil (bottom 25)

	Employed-Formal	Employed-Informal	Self-employed	Unemployed	Out of labour force
Employed-Formal	**71.1**	8.7	6.9	9.0	4.3
Employed-Informal	4.9	**48.1**	12.0	12.2	22.8
Self-employed	2.3	10.3	**53.5**	6.5	27.3
Unemployed	12.8	17.4	13.1	**30.9**	25.8
Out of labour force	1.2	3.6	4.5	4.3	**86.4**

d. Brazil (top 25)

	Employed-Formal	Employed-Informal	Self-employed	Unemployed	Out of labour force
Employed-Formal	**86.2**	4.0	2.6	3.0	4.2
Employed-Informal	23.3	**47.7**	13.0	5.1	10.9
Self-employed	5.6	6.8	**75.4**	3.1	9.0
Unemployed	21.4	13.2	9.7	**29.6**	26.1
Out of labour force	3.4	3.8	3.7	5.4	**83.8**

Sources: Barinas and Ñopo 2021; Correa et al. 2021; Firpo and Portella 2021. Background Papers of the UNDP LAC RHDR 2021.
Note: Bottom 25 = bottom 25 percent of the income distribution. Top 25 = top 25 percent of the income distribution.

Administrative registries of social security agencies record the contributions of workers to CSI programmes, thereby providing information on formality, given that workers who contribute are considered formal. However, the registries capture workers only after they have been formally employed for the first time. In addition, they do not record what happens when workers are not contributing, although the presumption is that some workers transition to informal employment, some to unemployment, and some out of the labour force, as detected for Brazil, Dominican Republic and Mexico. Administrative data are not as precise as panel data from employment surveys, but have the advantage of following workers for longer periods. Such data therefore give another type of information on formal formal-informal transitions.

The contribution density—defined as the ratio of the length of time that workers have contributed to CSI programmes over the length of time that they could have contributed since they first enter formality, summarizes this worker behaviour. A contribution density of 100 percent implies that, after workers enter formality for the first time, they maintain formal that status. A density of 50 percent signifies that workers were formal only half the time they could have been, beginning when they first acquired that status. High densities thus imply that workers spend most of their time in formality, and low densities suggest the opposite.

Data on contribution densities are difficult to compare across countries because they are available for different periods and are not always available by income level. The cases of Chile and Colombia are illustrative. Between 2009 and 2016, the average contribution density in Chile was 40 percent, but this average masks the fact that, among the bottom 20, 51 percent of workers exhibited densities of 20 percent at most, and only 38 percent had densities higher than 80 percent. This compares, respectively, with 9 percent and 82 percent for workers in the top 20. The results on Colombia are similar, although workers are classified in the data by wage levels rather than income quintiles. In 2010–2020, the average contribution density was 42 percent, but it was 39 percent among workers earning up to 1 minimum wage, and 68 percent among workers earning between 5 and 10 minimum wages.[3]

In the other countries under study, there are no panel employment surveys or detailed administrative data, but it is still possible to infer similar patterns. Jamaica is a case in point. The data allow a classification of workers by income quintile and distinguish among workers who had contributed in the previous 12 months, workers who had contributed before, and workers who had never contributed. Among the bottom 20, only 12 percent had contributed in the previous year; 13 percent had contributed during the year before that, and 75 percent had never contributed. Among the top 20, the respective shares were 46 percent, 24 percent and 31 percent.

In sum, three facts stand out. First, many workers transition between formality and informality; they are formal part of the time and informal the other part. Second, spells of formality are inversely correlated with income, that is, low-wage workers spend less time in formality relative to higher-wage workers. And, third, because of these transitions, average contribution densities are low, less than 45 percent in most countries on which data are available (compared with 60 percent or more in OECD countries). These facts indicate that labour markets in LAC are dynamic, characterized by significant churning. They also imply that at least in some countries, the issue is less that low-wage workers cannot enter into formal employment, than it is that they cannot maintain that status for long periods of time.

---

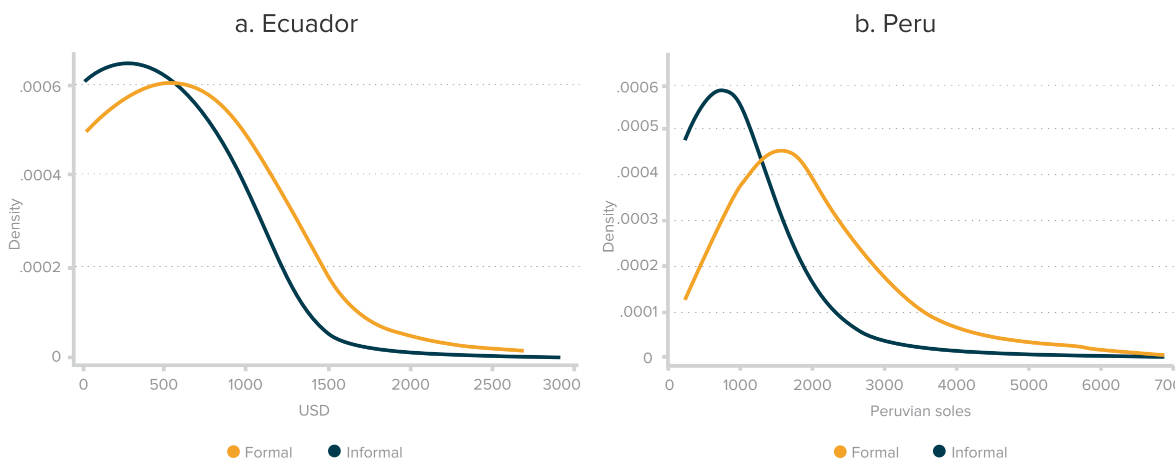
[3] CAF (2020) data on Argentina, Brazil, Ecuador, and Uruguay show a similar picture. In all four countries, the average contribution density increases with income. Moreover, the differences are significant: in Argentina, 14 percent for workers in the bottom 20 versus 60 percent in the top 20; in Brazil, 35 percent versus 71 percent; in Ecuador, 20 percent versus 69 percent; and, in Uruguay, 31 percent versus 71 percent. In Mexico, the average contribution density in 1997–2015 was 46 percent, but 13 percent among those earning 1 minimum wage, 39 percent among those earning 2 minimum wages, 52 percent among those earning 3 minimum wages, and 74 percent among those earning 10 or more minimum wages (Castañón Ibarra and Ferreira Blando 2017).

Overlap between the formal and informal wage distributions

Because some formal workers may be poor, it is not the case that every formal worker earns more than any informal worker. In fact, many informal workers earn more than some formal workers. Thus, formality is not fully equivalent to high income, nor is informality fully equivalent to low income.

Labour income distributions offer more insights into this phenomenon. Figure 5.5 depicts the distributions in Ecuador and Peru. If formality were synonymous with high income, the distributions among formal workers would be completely to the right of the distributions among informal workers, with no overlap between them. Figure 5.5 makes clear that, in Ecuador and Peru, this is not the case, and in fact, in both countries, although the formal labour income distribution is to the right of the informal distribution so that the average formal labour income exceeds the average informal one, there is considerable overlap.

Figure 5.5: The overlap in formal and informal labour income distributions



Sources: Ñopo 2021; Ñopo and Peña 2021. Background Papers of the UNDP LAC RHDR 2021.

Similar data are found on other countries in LAC. In all cases, the mean formal labour income is higher, but some informal workers earn more than some formal ones. This is consistent with the fact that informality is associated with many forms of participation in the labour market, some of which may be, in net terms, more well remunerated than the net wages that some formal firms can offer their workers.

Summing up

These three stylized facts—large shares of self-employment and employment in micro-firms, transitions in labour status, and the overlap between formal and informal earnings—result from the interactions of firms and workers in the labour market. These interactions depend on many policies, some of which are outside the domain of social protection. But they also depend on these policies because they impact two key dimensions: worker welfare and firm profitability. These three stylized facts likewise determine the impact of social protection policies on inequality and productivity.

5.4. Social protection, inequality, and protection against risks

Social insurance

If all workers in a country were formal and had the same income, CSI programmes would have no impact on inequality. Workers would contribute an amount proportional to their income—the same for all—that would be sufficient to pay for the stipulated benefits given the expected distribution of contingencies (illness, disability, death, and so on). In parallel, all workers would be permanently covered. Thus, CSI programmes would pool risks among all members of society, but would be neutral from the perspective of income distribution.

The situation in LAC is different for many reasons. First, there are large differences in incomes across workers; so, when contributions are proportional to incomes, but benefits are not, some redistribution is inevitably involved. Second, workers transition between formal and informal status and are thus covered by CSI programmes only part of the time. Third, permanence in formality is positively correlated with income. And fourth, the many rules and conditions of access governing programmes for health, pensions, and protections against loss of employment introduce discrepancies between individual contributions and benefits, thereby de facto redistributing income in ways that are not always obvious or desirable. This has three implications. First, it is not possible to separate the impact of CSI programmes in protecting workers against risks (the insurance function) from their impact on inequality (the redistribution function); these impacts exist side by side. Second, the impact of CSI programmes on these two dimensions varies across countries because of differences in the formal-informal composition of labour markets in these countries and their labour market dynamics and because the eligibility rules for individual programmes also differ. Third, as a result, while there are some common features, the specificities of countries are extremely relevant; thus, the discussion in this section needs to be accompanied by examination of the individual country studies.[4]

[4] See UNDP LAC Working Papers 14–23.

Incomplete risk pooling and ineffective coverage

An underappreciated aspect of CSI programmes is their effectiveness when workers transition from formal to informal status in a context of segmented labour markets. A first point to note is that risks are pooled only between a subset of all workers, inherently increasing the costs of insurance.

A second point is that formal-informal transitions reduce the efficacy of CSI programmes in protecting workers against risks. Consider, for example, protection against disability. If workers are formally employed when they suffer a disability, they will receive a disability pension or, at least, some compensation, but not if the disability occurs while they are informally employed. Consider next the support for working women or men after childbirth (under the form of maternity or paternity leave or, sometimes, one-time payments): they receive the benefit only if the event occurs while they are formally employed. Or consider the sudden death of the main breadwinner in a household: the family obtains a survivorship pension if the death occurs when the breadwinner was formally employed, but not if, at that moment, the breadwinner was informally employed. More generally, workers may suffer negative shocks when they are formally or informally employed, but are only protected in the first case. It is as if one purchased fire insurance for a house or accident insurance for a car that covered these contingencies only during weekdays, but not on weekends and not at night; clearly, such erratic coverage is unsatisfactory.

The inefficacy of CSI is not neutral across income levels. Because higher-income workers spend more time than lower-income workers in formality, they are protected during longer periods. Thus, the impacts of negative shocks fall disproportionately on those who have less capacity to bear them. The interaction between income-dependent spells of formality and labour status–dependent access to protections is particularly unfavourable to poor workers.

With varying degrees of coverage across countries, workers get some insurance through NCSI programmes when they are informally employed, almost always at lower quality or generosity than CSI programmes. But, with a few exceptions, these programmes insure only against health and longevity risks (through non-contributory health and pension programmes). Workers are not insured against unemployment, disability, or death if they are informally employed. The result is that households in LAC—particularly low-income households—bear many more risks on their own or through family and friend networks relative to households in OECD countries, where these risks are more broadly shared. One might say that the formal-informal segmentation of the labour force constrains solidarity across members of society, narrowing the space for nourishing social capital.

Erratic redistribution in health and pension programmes

CSI programmes may redistribute income across workers, although the extent and direction vary from programme to programme. Usually, health programmes are the most redistributive: workers contribute in proportion to their wages or salaries, but all receive the same in-kind benefits; in other words, high-income formal workers cross-subsidize low-income formal workers. This is the case in Colombia, Ecuador, and Mexico, for example. But, in some countries, the redistributive potential of CSI health programmes is diminished or even nullified by decisions to opt out of the risk pool. This is exemplified by the case of Chile (box 5.2). The case of Honduras is different, but yields a similar result. As in Chile, formal workers are required to contribute to health insurance, but, in this case, the contributions are not proportional to worker wages. They are capped at one minimum wage. Because, in principle, there are no formal workers earning below this amount, the implication is that high- and low-wage workers in Honduras pay the same amount and receive the same benefits. Thus, there is no redistribution.

The fact that contributory health programmes may not redistribute towards low-income workers does not preclude redistribution through other health programmes, in particular non-contributory ones. By construction, these are financed from general revenues and cover mostly lower-wage workers because these workers spend less time in formality than higher-wage workers. Thus, NCSI health programmes are highly redistributive. In many countries, in fact, they are the most redistributive of all social protection programmes considering the resources allocated to them, which are usually between 1.5 percent and 2.5 percent of GDP, significantly higher than the resources allocated to targeted poverty programmes.[5]

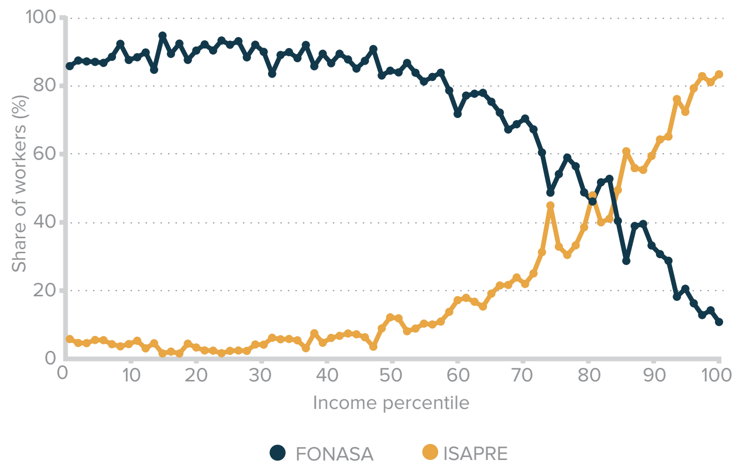
[5] This is in line with findings of the Commitment to Equity Institute. The website of the institute is at https://commitmentoequity.org/about/. See Lustig (2017).

Box 5.2: Health programmes in Chile

In Chile, workers are required to contribute 7 percent of their salaries for health insurance. They then have the option of using their contributions for private insurance (Instituciones de Salud Previsional) or to pool them in the public national health fund (Fondo Nacional de Salud). In the first case, they can complement their contributions with additional resources to benefit from higher-quality services. In the second case, they may obtain subsidies depending on their income, in the form of co-payments, and have access to publicly provided health care services. Figure B5.2.1 shows the share of workers contributing to each option by income. Higher-income workers clearly do not pool their contributions in the national health fund and thus avoid cross-subsidizing low-income workers. Thus, in Chile, CSI health programmes do little to redistribute income from high- to low-earning workers, and all workers do not receive services of the same quality.[a]

Figure B5.2.1: CSI health programmes in Chile do little to redistribute income from high- to low-earning workers

Share of workers contributing to health programmes, Chile, 2017
By income percentile



Source: Morales and Olate 2021, Background Paper of the UNDP LAC RHDR 2021.

[a] A similar situation occurs in Peru. In Argentina, formal workers contribute to health insurance managed by labour unions, but workers can channel their contributions to private providers, for which labour unions act as intermediaries. High-wage workers benefit from these arrangements by contracting for better services with greater coverage.

Differences in quality between CSI and NCSI programmes are relevant because, except for Colombia, in all countries with both types of programmes, CSI programmes cover more complex and costly interventions. Furthermore, CSI services are sometimes provided by social security institutes, while NCSI services are provided by health ministries (as in Ecuador, Honduras, Mexico, and Peru), where waiting times are longer and medicines less readily available. These differences affect out-of-pocket expenditures for minor complications, such as stomach infections. But they matter more if there is a serious problem, such as a brain tumor, that may not be covered by NCSI programmes and that may leave families in financial ruin.

As a result, the largest redistributive impact occurs in countries in which there is a single health programme that provides services of equal quality for all and that is financed by general revenues, particularly taxes on income or consumption. In absolute terms, more resources are collected from higher-income households, including those that derive income from land or financial assets, because the income and consumption of these households are greater, that is, the pool of contributors is the largest possible and includes individuals with non-wage income. At the same time, all households receive similar benefits. This is the case in Brazil and Jamaica, the only two countries in the region with unified health programmes, which are fully financed from general revenues in the case of Brazil and almost fully financed in Jamaica (box 5.3). The access and quality of care are delinked from worker status in the labour market. Brazil spends 3.9 percent of GDP on its Sistema Único de Saúde, the publicly funded health care system. Jamaica spends 3.3 percent of GDP on its National Health System. For social protection, it is almost impossible to think of money more well spent: universal coverage with equal quality regardless of income or of the vagaries of the labour market.

What about contributory retirement pension programmes? In principle, they help workers smooth consumption over time and manage longevity risks. In LAC, they operate through two modalities: pay-as-you-go (PAYG) benefit systems, as in Brazil, Ecuador, and Jamaica; or defined contribution systems, which are usually based on individual accounts administered by private firms, as in Chile and Mexico. However, in some countries, such as Colombia, Honduras, and Peru, both modalities coexist, while, in others, such as Argentina, modalities have changed from PAYG to defined contributions and back again to PAYG.

If the contribution rate in the PAYG modality is actuarially fair, there is no redistribution involved.[6] The same holds in the defined contribution modality, where worker pensions are proportional to the amounts accumulated in the individual worker accounts. But this is rarely the case in LAC. Five features imply that contributory pension programmes have

[6] A PAYG system is actuarially fair if the parameters of the system are such that contributions paid are equal to the expected value of the pension received.

strong redistributive impacts, although not always in the appropriate direction: eligibility requirements for benefits, formal-informal transitions, actuarially unfair contribution rates in PAYG systems, indexing rules, and separate and usually more generous regimes for certain groups, such as teachers in Brazil or public sector workers in Jamaica.

Box 5.3: A single health programme financed through general revenue in Brazil

After the Brazilian Constitution of 1988 transformed the country's social welfare system, the Unified Public Health System (Sistema Único de Saúde) was established in 1990 to fulfil the constitutional mandate of health care as a fundamental right and a responsibility of the government through universal, integrated, decentralized, and democratic public health care provision.[a]

Public health expenditures, which amounted to 3.9 percent of the country's GDP in 2017, have been found to be progressive, particularly considering that funding comes from the overall governmental budget and is not financed through payroll taxes on formal workers.[b] The system is financed through mandatory contributions from all levels of government: municipalities and states are required to allocate 12 percent and 15 percent of their annual tax revenues to health expenditures, respectively, while federal transfers were initially conditional on GDP growth.[c] Starting in 2017, however, federal health care spending was fixed for 20 years at 15 percent of net revenue and is to be adjusted to inflation thereafter.[d]

For the past three decades, this system has guaranteed access to health care to every citizen free of cost, irrespective of their status within the labour market.[e] In retrospect, the system has been responsible for the expansion of access to health care across the country and the improvement of health outcomes that have particularly benefited the less advantaged.

Although the system encompasses all Brazil's population through public health care, nearly one quarter of Brazilians do not use it as their main source of care, potentially as a matter of choice.[f] Indeed, approximately 23 percent of Brazilians had private medical insurance in 2018, 70 percent of which received this insurance as an employment benefit.[g]

a. de Castro et al. (2019).
b. Higgins and Pereira (2014); IBGE (2019).
c. Piola, de França, and Nunes (2016).
d. Massuda et al. (2018).
e. Firpo and Portella (2021).
f. Bhalotra, Rocha, and Soares (2019).
g. Tikkanen et al. (2020).

Many countries require workers to contribute for a minimum number of years before they are entitled to a retirement pension, regardless of whether modalities are the PAYG or a defined contribution system. In Jamaica, workers must contribute for at least 9 years; in Brazil, Ecuador, and Honduras, 15; in Peru, 20; in Mexico, 25; in Colombia, 25 in the PAYG modality and 22 in the defined contribution modality; and in Dominican Republic, 30. In Argentina, workers must also contribute for 30 years, although this requirement is lowered through a host of special regimes.

Formal-informal transitions make it impossible for many workers to reach the stipulated threshold. The workers contribute to a pension during some periods of their working life, but may be denied a pension when they reach retirement age. This is a serious issue: in Colombia, between two thirds and three fourths of contributing workers will not qualify for a pension depending on whether they are in the PAYG or defined contribution modality. A similar result is found in Jamaica, where two workers in five will not obtain a pension in the PAYG modality, and, in Mexico, where about two workers in three will not qualify for a pension in the defined contribution modality. This is even a more worrisome in the case of women, who, in several countries, have a lower retirement age relative to men, but are required to contribute for the same number of years.

But, even if workers qualify, formal-informal transitions imply that the amount of the pension is diminished because accumulation occurs only if the worker is in formal status. Thus, even if workers obtain a pension, the replacement rate will be low because they will not have saved for their pension all the time, thereby also limiting the consumption smoothing purpose of pensions. Replacement rates depend on other factors as well, but the point here is that, all else is equal, pensions are proportional to the time spent in formality.

What happens if workers do not qualify for pensions after paying into the system? Depending on the laws, workers may lose all or part of their contributions, or they may get them back in a lump sum payment, sometimes with interest, sometimes without interest. In the former case, worker savings are de facto expropriated or heavily taxed; in the latter, longevity risks are fully transferred to workers, partly nullifying one of the purposes of these pensions.

A few examples are illustrative. In Honduras, workers who do not qualify for a pension get back less than a third of what they contributed (a tax of about 71 percent on accumulated contributions), while workers who do qualify receive a pension that is nine times their contributions, partly financed with the contributions of those who did not qualify. Because low-income workers are substantially less likely to qualify, they end up subsidizing high-income workers who do qualify, making the scheme regressive.

In Brazil, workers who do not qualify lose all their contributions, a large tax considering that workers and firms contribute 28 percent of wages; it is also likely a regressive tax considering that low-wage workers are more likely not to qualify.

In Ecuador, workers who fail to qualify—typically low-income workers–lose all their contributions. Meanwhile, workers who do qualify— typically higher-income workers—are subsidized because the government covers 40 percent of the value of pensions, absorbing 1.6 percent of GDP.

The same happens in Jamaica: workers who do not qualify receive nothing back.

The situation in Peru is mixed. Workers who do not qualify in the PAYG modality lose all their contributions, a tax of 100 percent that is used partly to fund the pensions of workers who qualify. In the defined contribution modality, workers get back all their contributions in a lump sum, with interest. However, even if workers qualify in the latter case, they may still not obtain a pension because Peruvian regulations give them the option to claim all their savings in one payment, rather than requiring them to purchase an annuity. Because this option is chosen by 95 percent of retirees, the result is that, for all practical purposes, Peru does not have a defined contribution pension system. Rather, it has a system of obligatory savings for the day of retirement, and workers bear the risks of longevity by themselves from that day on.

Contributory pensions may also have important redistributive impacts if workers qualify, particularly if, in the PAYG modality, the contribution rate is below the actuarially fair value of benefits. In these cases, the government fills the gap, and workers obtaining pensions receive subsidies. In principle, the subsidies may be progressive or regressive depending on the incomes of those receiving the benefits. In practice, they are often regressive because higher-wage workers are more likely to qualify for the pensions.

These impacts can be large, as exemplified by the case of Colombia, where the government spends 3.4 percent of GDP subsidizing PAYG pensions and where 70 percent of these subsidies are captured by households in the top 40 percent of the income distribution. But they are also large in Mexico where about 75 percent of the value of PAYG pensions is subsidized, resulting in subsidies of 1.6 percent of GDP, also concentrated in the upper deciles of the income distribution.[7] Jamaica exemplifies two additional situations that affect the redistributive impact of pensions: indexing rules and special regimes for public sector workers (box 5.4).

[7] Scott (2014); Altamirano Montoya et al. (2018).

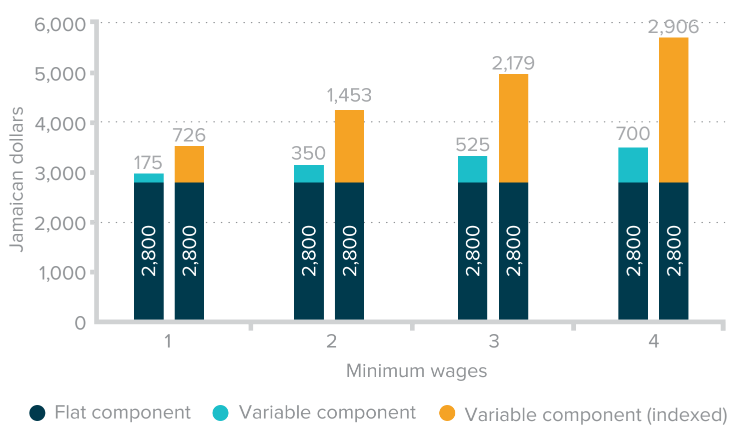
Box 5.4: Redistributive effects of Jamaica's indexing rules and special pension regimes

In Jamaica, private sector workers participate in the national insurance scheme. Because they must contribute at least nine years to qualify, two workers in five do not receive a pension and lose all their contributions. For workers who qualify, the pension has two components, one at a flat rate that is equal for all workers and indexed to inflation and one that is variable and depends on worker income, but is not fully indexed to inflation.

Figure B5.4.1 describes the erosion in the real value of pensions up to 2016 among those workers who had retired in 2001, a period during which the average annual inflation rate was 9.7 percent. For each wage level, the first bar reflects the actual value of the pension in 2016, and the second the value that would had been observed had the variable component been fully indexed. Workers who retired with a pension of one minimum wage lost 16 percent of the real value of their pensions; those with a pension of two minimum wages lost 26 percent; those with a pension of three minimum wages lost 34 percent, and those with a pension of four minimum wages lost 39 percent.

Figure B5.4.1: In Jamaica, the real value of pensions decreases over time

Inflation and pensions in Jamaica



Source: Mera 2021, Background Paper of the UNDP LAC RHDR 2021.

The combination of formal-informal transitions, eligibility rules and indexing rules implies that the impact of the national insurance scheme on inequality in Jamaica is contradictory. Workers who do not qualify for pensions—mostly lower-wage workers—are taxed 100 percent of their contributions, which is clearly a regressive outcome. Among workers who qualify, the higher-wage workers are taxed more, given that, for them, the variable component of the pension is more important.

In parallel, in Jamaica, public sector workers receive pensions through the public sector pension scheme which, as opposed to the private one, is almost fully funded by the government because, until recently, workers barely contributed. There was thus a huge gap between the actual and the actuarially fair contribution. The resulting subsidies are quite large, 1.7 percent of GDP. Workers in the top 20 percent of the income distribution capture 0.75 percent of GDP, and workers in the bottom 20 capture only 0.11 percent. Altogether, on average, workers in the public sector receive pensions that are almost five times higher than pensions in the private sector, 1.9 minimum wages in the first case versus 0.4 minimum wages in the second case, making the public sector pension scheme probably the most regressive social protection programme in the country (in contrast to the national health system).

Jamaica is not the only country in the region in this situation. Separate pension regimes for public sector workers are also used in Brazil and Mexico, and, in relative terms, they are generous, particularly if workers in public enterprises, development banks and other public institutions are considered. And, in the case of these two countries, the amounts involved are also significant. In Brazil, for example, subsidies to contributory pensions among public sector workers are 2.9 percent of GDP. This is similar to the subsidies for contributory pensions among private sector workers, 2.8 percent, except for the fact that there are 10 times more private sector retirees.[8]

The shortcomings of contributory pension programmes have led many countries to introduce non-contributory programmes, which vary in form. The simplest scheme is a flat pension for everybody as in Bolivia and, more recently, Mexico. The amounts spent differ, 1.1 percent of GDP in the first case and 0.6 percent in the second, but, regardless of the amounts, these pensions are highly redistributive in both countries:

---

[8] Minimum wages can also affect the redistributive impact of pensions. In Colombia, pensions are indexed to inflation, but must be at least equal to the minimum wage so that de facto the minimum pension is indexed to this wage. This is relevant considering that, in the last 15 years, accumulated inflation was 77 percent, while the accumulated increase in the minimum wage was 130 percent. As a result, minimum pensions have increased in real terms, but not the higher-value pensions. The pension distribution has been compressed, while the average real pension has increased. This is in contrast with Jamaica, where indexing rules have also compressed the pension distribution, but lowered the average real pension.

all households finance them in proportion to their incomes through income or consumption taxes, and all receive the same amount (as in Brazil and Jamaica's health programmes). In parallel, these pensions contribute to avoid old-age poverty and help the elderly manage the risks of longevity. Furthermore, they have the great advantage of being wholly independent of any previous participation in the labour market, avoiding any impact on the contribution decisions of currently active workers.

In other countries, however, non-contributory pensions are limited either only to poor households or to workers who do not receive a contributory pension. Because of this and because, in general, the pension is small, the resulting redistribution is not significant, with the added complication that the conditions imposed can affect behaviour. Colombia, for example, restricts its non-contributory pension to poor households and sets the pension to one 10th of a minimum wage. As a result, it spends only 0.1 percent of GDP. Brazil spends more, 0.4 percent of GDP, but other countries spend substantially less: 0.35 percent in Ecuador, 0.11 percent in Peru, 0.10 percent in Jamaica, 0.009 percent in Dominican Republic, and 0.0007 percent in Honduras. These shares compare unfavourably with subsidies to contributory pensions that tend to favour higher-income households.

Argentina and Chile have intermediate schemes that may be characterized as semicontributory. Rather than relying on separate contributory and non-contributory pensions, the schemes complement worker and/or firm contributions to the former with government subsidies to increase the value.

In Chile, pensions are under a defined contribution modality, but the government provides subsidies to ensure that nobody receives a pension lower than a defined threshold, the basic solidarity pension, even if some workers have never contributed to individual accounts. These subsidies are set on a declining scale as the pension obtained through a worker's own resources increases in value up to another threshold, the maximum pension with solidarity support. The mechanism is progressive because, even if workers have the same spells of formality during their lifetimes, lower-earnings workers would, in absolute terms, accumulate less than higher-earnings workers and thus receive larger subsidies. Workers never lose their contributions, and pensions increase with individual savings. In terms of incentive design, the Chilean model is interesting for the region (box 5.5). However, the parameters of the scheme are not too generous, and, altogether, the government allocates 0.70 percent of GDP to subsidize these pensions for 1.4 million retirees, which contrasts with 1.35 percent in subsidies for 773,000 retirees under the old PAYG modality and 2.20 percent in subsidies for the national health fund for 13.8 million individuals, though these parameters have recently changed, and spending will increase.

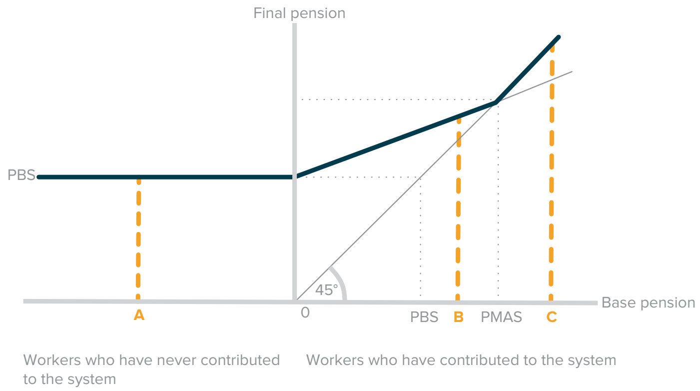
Box 5.5: Solidarity pensions in Chile

In 2008, Chile enacted a pension reform that introduced an important modification to the pension system: it created the solidarity pillar. This non-contributory component is financed through general taxes and seeks to introduce a greater solidarity component to a system that, until then, included low coverage of non-contributory pensions. The benefits are delivered to people ages over 65 who belong to the bottom 60, considering the per capita income of the household group. The two main benefits are the basic solidarity pension and the solidarity pension payment. The basic solidarity pension corresponds to a monthly monetary transfer of US$150 (one third of the gross minimum wage) as of 1 July 2019 and is delivered to people who do not have a self-financed pension (that is, they have accumulated zero in their individual accounts). The solidarity pension payment is an amount of money that complements the pensions of individuals ages over 65 who have contributed to the pension system, but are unable to self-finance a pension greater than a threshold, the maximum welfare pension (equivalent to US$450 or around 1.2 minimum wages). This transfer decreases as the pension that the person manages to self-finance at retirement increases.

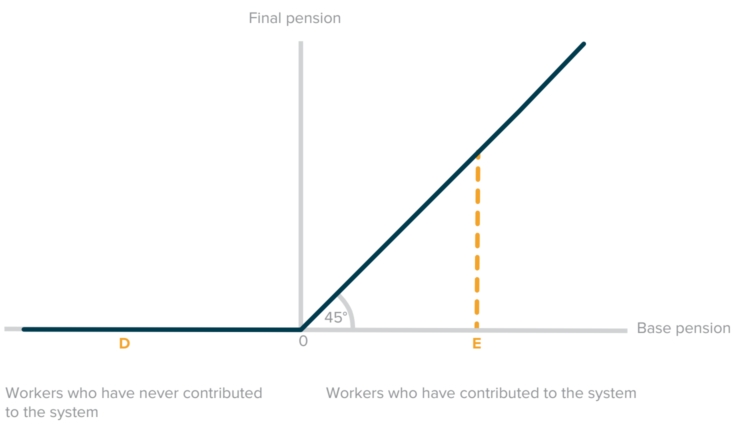
Figure B5.5.1 shows the layout of the basic solidarity pension and the solidarity pension payment; panel a describes the situation of retirees in households in the bottom 60, and panel b describes the situation of retirees in the top 40. Point A indicates individuals who have never contributed (that is, they have a self-financed pension equal to zero) and who therefore receive the basic solidarity pension benefit. Point B indicates individuals who have saved little during their active lives in such a way that the self-financed pension they obtain (without the existence of the solidarity pillar) is below the maximum welfare pension threshold. The final pensions of these people would be at the blue line (not the 45-degree line), which corresponds to the sum of the self-financed pension and the solidarity pension payment. In this case, the solidarity pension payment is the vertical difference between the blue line and the 45-degree line and decreases as the self-financed pension grows. Point C indicates people who have saved in such a way that their self-financed pension is above the maximum welfare pension, and they do not receive any aid from the government. Thus, the final pension equals the 45-degree line. Panel b illustrates how the system works for people in the top 40. Point D indicates that, if individuals have not contributed and do not have a self-financed pension, their final pension will be equal to zero. Point E indicates that, if the individuals have contributed and have self-financed pensions valued at more than zero, then the final pension equals the 45-degree line. Thus, the blue lines in both panels of the figure correspond to the final pensions of retirees in Chile.

Figure B5.5.1: Solidarity pillar design

a. Solidarity pension for people in the bottom 60



b. Solidarity pension for people in the top 40



Source: Morales and Olate 2021, Background Paper of the UNDP LAC RHDR 2021.
Note: PBS = basic solidarity pension. PMAS = maximum welfare pension.

While the values of solidarity pensions increased in 2020, the mechanism by which they are granted was not modified.

Formal-informal transitions and links between health and pension programmes

Transitions reduce the efficacy of programmes to protect households against risks. Combined with eligibility rules, they limit the coverage of retirement pensions and, at times, result in regressive distributional impacts. In addition, in some cases, such as Ecuador, Honduras and Mexico, transitions also impact contributory health programmes because they operate under a PAYG design: the contributions of active workers finance health services for retired workers. However, coverage is limited to retired workers who qualify for a contributory pension or at least to those who have contributed for a minimum number of years. But, because of transitions, many workers will not qualify. If they work formally, they finance health services for retired workers, but, when they retire, they will not have access to such services. In Mexico, for instance, workers must contribute for 15 years before they gain the right to health services upon retirement. One worker in two will not have that right; instead, such workers will obtain health services from lower-quality non-contributory programmes.

This is worrisome in terms of protecting the elderly against health risks; but it is also worrisome from a distributional point of view because lower-wage workers are more likely to fail to qualify for pensions given their shorter spells in formality. They end up cross-subsidizing higher-quality health services for higher-income retirees with pensions, while they have no pension and receive lower-quality health services.

Summing up

The mix of contributory and non-contributory pension and health programmes across the region, coupled with transitions between formal and informal status, asymmetries in the time spent in formality between low- and high-wage workers, and, at times, capricious rules and conditions for access, generates two outcomes:

- Reduced efficacy of insurance
- Contradictory impacts on inequality

Identifying the total impact of these programmes on inequality is complex. The same worker may sometimes pay for benefits through a contributory programme and sometimes receive free benefits through a non-contributory programme. Workers with identical characteristics (age, education) and almost the same accumulated years of formality may end up with different outcomes, some obtaining subsidized pensions, and some losing part or all of their contributions. Workers with similar careers can receive health services that differ in quality when they retire. There may also be intertemporal effects that impact the real value of pensions, and so on. Embedded in these programmes are implicit systems of taxes and subsidies that redistribute income among workers along the income distribution, between workers and firms, and between worker households and other households. The taxes and subsidies may change over time, are not neutral across income levels, and do not necessarily favour lower-earnings workers. Often the data required to identify and measure these taxes and subsidies are not available, even in countries with reasonable household surveys, in part because the surveys seldom have sufficiently long panels to gauge dynamic effects, for instance, workers who contribute, but fail to receive contributory pensions or health services.

A regionwide assessment of the impact of social insurance on inequality is difficult especially because programmes that superficially look similar across countries can be quite different once indexing rules, conditions of access, and labour market dynamics are taken into account. The discussion above therefore should be read less as an overall assessment and more as an examination of the wide range of outcomes that are observed in LAC, given the region's dual social insurance architecture.

Overall, non-contributory programmes tend to be more redistributive than contributory programmes, even if their quantitative impact in many cases is small because the budgetary resources involved are not large. Meanwhile, health programmes tend to be more redistributive than pension programmes because contributory programmes usually involve cross-subsidies from high- to low-wage workers and because the budgetary resources allocated to non-contributory programmes are larger than those allocated to non-contributory pensions. Within pension programmes, contributory ones are the most problematic because, in many cases, they redistribute income in the direction opposite to what is desired, a situation that is aggravated when these programmes require government subsidies that exceed those allocated to non-contributory pensions, sometimes by a significant margin.

Considering the erratic protection against risks and the ambiguous impact on inequality, it is hard to argue that social insurance programmes currently make a large contribution to social protection in the region. This is not to say, of course, that they should be removed; but to say, rather, that substantive changes are required if these programmes are to make the contribution to reducing inequality that the region needs.

Social assistance

Income transfers

Policies to help the poor in LAC can be grouped into two groups. The first includes income transfers through exemptions to consumption taxes for food and other basic items or through direct or indirect subsidies for transportation, fuel, and basic services. Many of these transfers are generalized and disassociated from any behaviour by households (other than consuming whatever is subsidized). Most of these transfers are justified on poverty reduction grounds. However, if their size is proportional to consumption, non-poor households usually receive larger transfers in absolute terms than poor ones, making the transfers an inefficient mechanism to redistribute income to poor households.

The second group of policies includes targeted transfers, which can be in kind or in cash. Among the transfers in kind is, for example, the distribution of milk or other staples. Among the transfers in cash are monetary transfers that are often conditional on investments by households in their human capital. These CCT programmes were a Latin American innovation in the mid-1990s. Price subsidies for the consumption of basic services—water, sanitation, electricity, internet—that are granted to poorer households also fall within the category of targeted transfers, although they are not directly in cash.

Table 5.2 contrasts government spending on generalized fuel subsidies with CCT or non-contributory pension programmes targeted on the poor for a sample of countries and, in both cases, expressed as a share of GDP. Because fuel subsidies fluctuate depending on the world price of oil, the data are the averages for each country between 2008 and 2014.

Table 5.2: Generalized transfers represent a much higher share of government spending than targeted transfers

Fuel subsidies and direct transfers targeted on the poor as a share of GDP

	Argentina	Colombia	Ecuador	Honduras	Mexico	Peru
Energy	3	1.4	6.4	1.9	1.9	1
Transfers	0.6*	0.3	0.8	0.2	0.4*	0.2

Sources: Marchán, Espinasa, and Yépez-García 2017; Levy and Cruces 2021, Background Paper of the UNDP LAC RHDR 2021.
Note: *Excludes non-contributory pensions that are not targeted on the poor.

Clearly, there is a large imbalance between generalized and targeted transfers, and the former are several multiples of the latter. This imbalance, combined with the fact that targeted programmes sometimes have important exclusion errors, mean that many poor households receive little income support. This partly explains why poverty rates in LAC are high relative to the region's average income, although the barriers faced by poor workers in accessing more productive jobs are also an important part of the explanation.

Targeted transfers have an inevitable trade-off. From a fiscal point of view, they are substantially less costly and more effective than generalized transfers. If only 25 percent of the population is poor, there seems to be little point in including the other 75 percent who do not need them. However, any targeting mechanism involves an implicit tax because the poor lose the transfer if they earn additional income that lifts them above the threshold stipulated in the targeting mechanism to qualify (the horizontal dotted line in figure 5.2). The net income from their efforts is then the additional income earned, less the value of the transfer forgone. If the transfer is high, the implicit tax is high, and poor households near the thresholds may be caught in a poverty trap.[9] This is an important issue, which speaks to the potential pitfalls of overreliance on targeted transfers.

This does not mean that targeted transfers should be phased out; they should not, but their value and the eligibility rules need to consider their interphase with CSI and NCSI programmes and their impact on worker employment decisions. From the point of view of poverty reduction, much would be gained by lowering generalized fuel subsidies and redirecting resources towards the poor. Some of these resources should be channeled to expanding the coverage of targeted transfers in countries in which poor households are currently excluded. But some should be directed to improving infrastructure services (water and sanitation, internet connections, roads), the quality of publicly provided services (such as education), and, critically, the functioning of labour markets and the access of poor workers to more productive jobs.

Income transfers versus insurance

Like all other workers, poor workers experience idiosyncratic shocks. They fall seriously ill, lose their jobs, suffer permanent disabilities, and die. The income transfers they may obtain through targeted programmes, when they receive them, are not effective in protecting them against these shocks. Poor households therefore need income transfers and insurance, not one or the other. Indeed, poverty measures at times fail to capture the impact of the greater security offered through coverage by CSI programmes on the welfare of the poor, even if the coverage is not reflected in monetary incomes.

Many non-poor households in LAC are also in vulnerable positions. About 37 percent of all households have incomes between US$5.50 and US$13.00 a day.[10] Some enter and exit poverty regularly.[11] Living at the edge of poverty, a positive idiosyncratic shock can place these households further beyond the edge, but a negative shock can as easily push them over the edge.[12] For these households, insurance is key. The absence of insurance implies that, if a household suffers a large shock, such as falling prey to COVID-19, worker livelihoods may become wholly dependent on government transfers. Being left out of the protections provided by an effective social insurance system is a major problem. Targeted transfers are a mediocre solution. Rather than acting ex ante to prevent poverty, policies typically react ex post to address poverty.

---

9 See Besley and Kanbur (1991).
10 Busso and Messina (2020).
11 Vakis, Rigolini, and Lucchetti (2016).
12 Cruces et al. (2011) find that, over a 15-year period, 10 percent of households in LAC fell into poverty every year.

Interphase between social insurance, a minimum wage, and social assistance

Income transfers for the poor should not be conditional on labour status. In some countries, they are. Poor households receiving benefits from Ecuador's CCT programme (Bono de Desarrollo Humano) lose them if they obtain a formal job, as if access to CSI programmes eliminated their need for additional income support. This increases informality rates among poor workers, who, for taking a formal job, face a de facto tax equivalent to the value of the CCT benefits forgone. Argentina's CCT programme (Asignación Universal por Hijo) was initially only compatible with informal work, unemployment (but not associated with a formal job), or non-participation in formal employment, reinforcing incentives to be informal. In these cases, CCTs, rather than creating a poverty trap, may inadvertently create an informality trap.[13]

CSI and NCSI regulations, interacting with the minimum wage, can also make it difficult for poor workers to enter formality, even if CCTs are neutral to labour status. Countries that do not require self-employed workers to contribute to CSI programmes give them the option to do so voluntarily. However, contributions must be based on at least the minimum wage, even if earnings are below that threshold, a relevant consideration in countries such as Ecuador, Honduras and Peru, where the majority of the self-employed earn less than the minimum wage. Colombia is an interesting case. Self-employed workers are required to contribute, but only if their earnings are equal to or above one minimum wage, a relevant consideration because 50 percent of all workers earn less than the minimum wage. Under these conditions, self-employed workers would have to allocate a large share of their earnings to participating in the CSI programmes, thereby de facto excluding them from coverage (box 5.6).

In Brazil, poor workers do not automatically lose the benefits of their CCT (Bolsa Família) if they obtain a formal job, as in Ecuador or Dominican Republic, but the programme rules imply that they probably will. A formal job must pay at least the minimum wage. This may place the household above the poverty line used to select households into the CCT, particularly if it has fewer than six members, which is the case of 96 percent of households in the programme's registries. In addition, poor workers may also be reluctant to obtain a formal job if they consider it to be shortlived because getting back into the programme's registry is difficult. This is one of the factors that explains why almost 93 percent of all poor workers in Brazil are informal.[14]

---

[13] Araujo et al. (2017) find that, in Ecuador, conditioning CCT benefits on informal status lowered rates of formal employment among women. In Brazil, de Brauw et al. (2015) find substantial reallocation from formal to informal work. Bérgolo and Cruces (2021) find that Uruguay's CCT (Asignaciones Familiares) generates incentives to informal work and disincentives to formal work. Garganta and Gasparini (2015) find similar results in Argentina.

[14] See Firpo and Portella (2021).

Dominican Republic is also an interesting example. As in Colombia, the self-employed must also contribute to CSI programmes if they earn more than a basic income of at least one minimum wage. From 2003 to 2019, the growth performance of the country was one of the best in the region, more than doubling the average income per capita; in parallel, average years of schooling increased by 26 percent. The poverty rate fell from 32 percent to 21 percent. But informality increased slightly, from 54 percent to 55 percent, as did the share of workers who are self-employed or who work in firms with up to five workers, from 51 percent to 52 percent. Many poor workers escaped poverty, but almost none escaped informality.

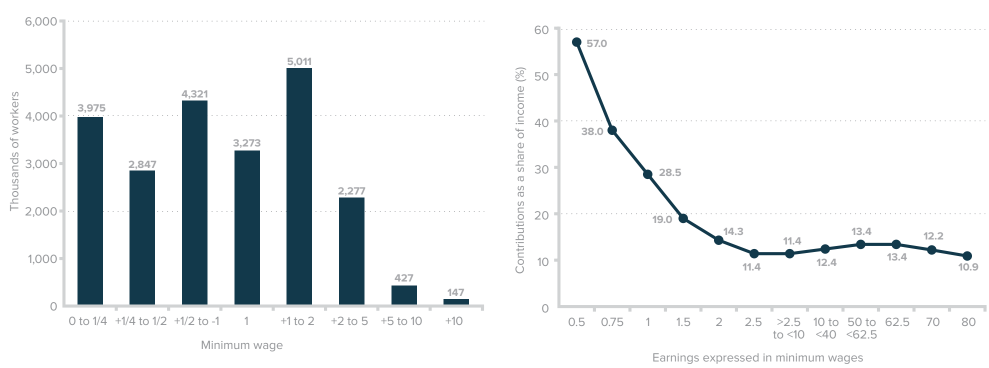
Box 5.6: The minimum wage in Colombia

The use of the minimum wage as the minimum income for participation by the self-employed in CSI programmes excludes a large share of the working population from the most important social protection programmes in Colombia. Figure B5.6.1, panel a, shows the distribution of workers by labour income, with ranges expressed in minimum wages, confirming that at least half the Colombian labour force earns less than one minimum wage.

Figure B5.6.1: The interphase between the minimum wage and CSI and NCSI programmes in Colombia induces many self-employed into informal employment

a. Workers, by labour income

b. Contribution, by labour income



Source: Alvarado, Meléndez, and Pantoja 2021, Background Paper of the UNDP LAC RHDR 2021.

Workers earning less than the minimum wage are not obliged to contribute, but may do so as long as they pay a contribution equal to that mandated for earners at the minimum wage. Figure B5.6.1, panel b, shows, however, that voluntary participation among this group would be costly because they would have to pay 28.5 percent of a minimum wage in contributions, 12.5 percent for health care, and 16.0 percent for pensions. Among workers earning half a minimum wage, contributions would represent 57 percent of their earnings, and among those earning three fourths, 38 percent. If these workers wanted to be formal, they would have to devote at least a third of their earnings for health care and pensions, leaving two thirds or less for all other needs. On its own, this would seem a sufficient reason for them not to contribute. But two factors strengthen that decision. First, if they do not contribute, they have free access to health benefits of the same quality, and, second, if they do contribute, they need to do so for 22 years to qualify for a pension under the defined contribution modality or 25 years under the PAYG modality. Unsurprisingly, they are informal.

The alternative route for poor workers in Colombia to become formal is to be hired as dependent workers by a firm. But, in that case, the firm must pay the minimum wage, plus part of the contributions to the CSI programme that cannot be shifted back to workers in the form of lower wages because of the minimum wage, and the firm bears the contingent costs of job stability provisions. Because this is not profitable for most firms, the result is that most poor workers are self-employed; or work in firms that can elude the obligation to contribute because the relation of dependency is ambiguous or that can evade the obligation by taking advantage of weak enforcement.

Permanent versus transitory targeted transfers

Poor households need income transfers while they work their way out of poverty. Ideally, workers in these households should see their earnings increase over time either because their wages rise if they work in firms that are gradually more productive, or because their own firm become more productive. Targeted transfers should therefore be transitory. (Insurance, meanwhile, needs to be permanent because households may experience negative shocks regardless of their income.) But, if the incomes of poor workers stagnate because they are working at permanently low-productivity firms or because they cannot increase their own productivity or that of their own micro-firm, targeted transfers become a permanent necessity.

CCTs were introduced in the region over two decades ago with the goal of transferring income to the poor, while investing in their human capital, and of helping new cohorts of workers obtain more productive formal jobs through their increased human capital. The evidence indicates that, by and large, they have achieved the first objective:

consumption rose, undernutrition fell, morbidity decreased, and schooling indicators such as attendance and progression rates improved.[15] But the same cannot be said of the second goal. Poverty rates have fallen in large part because households receive income transfers and not so much because earned income has risen in poor households. The poor are not gaining access to enough higher-productivity occupations because most of them continue to be self-employed or work in small firms that are low productive.

With the benefit of hindsight, it is clear that since the early 1990s, while much of the region's attention was centered on improving the human capital of poor children and youth, insufficient attention was focused on considering the kinds of firms that would employ these people when they entered the labour force. Would workers transition from working on their own to working in firms? What sort of firms? Would the firms require the enhanced human capital, offer them long-term contracts, and invest in their training? Or would they be the same small, informal, low-productivity firms that employed their parents? The data in figure 5.4 are relevant. Most of the poor are self-employed or work in small, fragile firms. They are there because laws and institutions, including those associated with social protection, induce the dispersion of economic activity and make it difficult for firms to grow.

Permanently subsidizing fuel prices and exempting some consumption goods from value added taxes help the non-poor more than the poor. The root problem—low earnings given the lack of productive opportunities—is not solved by increasing generalized consumption subsidies. And raising targeted transfers may worsen this problem if they are conditional on informal status and create an informality trap or if they are so high that they create a poverty trap.

Social assistance policies at times assume that programme target populations—see figure 5.2, quadrants III and IV—are exogenously given. But the distribution among these quadrants matters substantially. If more of the poor were in quadrant III and fewer in IV, they would have improved insurance and better jobs; it would be easier for them to escape poverty or avoid falling deeper into poverty when events are unfavourable. But whether they are in quadrant III or IV depends on what firms do. As figure 5.3 indicates, this depends on all social protection policies, not only social assistance. If social insurance programmes were unified and if access were delinked from worker status in the labour market, incomes would increase, and the need for poverty programmes would diminish. At some point, improving social insurance programmes is more effective in reducing poverty relative to increasing the generosity of targeted transfers.

[15] For a review of the evidence on the region, see Fiszbein and Schady (2009).

Governments in the region should no longer expect targeted transfers, on their own, to eliminate poverty. These transfers are useful; they certainly should not be eliminated. But they need to be better integrated with social insurance policies. Moreover, the poor need higher-productivity jobs as well as access to insurance on the same conditions and of the same quality as the insurance provided to higher-income workers. This objective will only be achieved if policymakers concerned with poverty reduction expand their perspective beyond individual targeted programmes and consider the whole range of social protection policies, particularly policies that bear on the performance of the labour market. If the belief persists that poverty can be eliminated through self-contained targeted programmes, the region will continue to trap a significant share of the population in poverty, investments in human capital notwithstanding.

5.5. Social protection and productivity

The discussion now considers the effects of social protection on the behaviour of firms and workers in the labour market, complementing the analysis of its impact on insurance and redistribution. Table 5.3 lists the costs and benefits of formality, legal informality, and illegal informality. Legal informality is only relevant in countries in which laws exclude some workers from the obligation to contribute to CSI programmes or if they exclude some firms, depending on size or the type of contract with workers. Thus, in some countries, such as Ecuador, Honduras, Mexico and Peru, the three columns are relevant, while, in others, such as Argentina and Jamaica, the middle column is not relevant (see box 5.1).

Tax on formality

Many factors influence which workers and firms are in each column in table 5.3, such as the tax regime, property rights, regulations on credit, and so on. The focus here is on the factors associated with social protection, and it is useful to begin with the first column of Table 5.3. Two factors are considered. First is the functioning of CSI programmes, which determines the balance between the benefits that workers receive and the costs. If these were equal, there would be no impact on the behaviour of firms or workers.

For many reasons, however, workers may undervalue these programmes. One is the fact that workers may not qualify for a retirement pension and lose some or all their contributions (or the fact that they may not qualify for health benefits when they retire). But, even if they receive their pension contributions back, they may still be unwilling to save in an account that cannot be pledged as collateral or used in an emergency, while paying high fees to the firm managing the account.

Another reason might be that the quality of health services is low or not much higher than that of non-contributory health services. Workers may consider there is little point in contributing for health services if they can obtain similar services free, especially if they also must contribute for a pension they may never receive.

Table 5.3: The interphase between CSI, NCSI and poverty programmes impact the decisions of firms and workers to be formal or informal

Formality	Legal Informality	Illegal Informality
Workers	Workers	Workers
Must pay a share of CSI contributions (full share if self-employed), but may not fully value the stipulated benefits	Self-employed, domestic, rural and others not required to contribute	Self-employed and others required to contribute to CSI may pay fines depending on enforcement and tacitly accepted social norms
Paid at least the minimum wage	Free NCSI benefits	Free NCSI benefits
In principle protected by job stability regulations, but access may be erratic	If poor, may also receive targeted transfers	If poor, may also receive targeted transfers
If poor, may lose targeted transfers		
Firms	Firms	Firms
Must pay their share of CSI contributions and pay workers at least the minimum wage	Not bound by CSI, minimum wage, or job stability regulations if there is no dependency relationship with workers, or if this relationship is ambiguous (particularly if the firm is small)	Pay fines if detected evading CSI, minimum wage and job stability regulations
Bear the expected costs of job stability regulations	Fuzzy border between self-employed and micro-firm, particularly if workers are unremunerated relatives	Enforcement dependent on size, at times substituted by tacitly accepted social norms

Source: Levy and Cruces 2021, Background Paper of the UNDP LAC RHDR 2021.

A third reason might be that CSI contributions in part finance activities that benefit all households or all workers, not only those contributing (so that there are cross-subsidies from formal firms and workers to informal ones). This is a serious issue in Jamaica, where approximately 47 cents of every dollar contributed do not translate into direct benefits for workers, but are instead used to finance education, training, and housing programmes for all. Because CSI contributions are 4.6 percent of GDP, this implies a transfer of 2.2 percent of GDP from formal firms and workers to everybody else. It is also an issue in Brazil, where between 3.3 percent and 5.8 percent of the formal wage bill is used to finance activities such as education and the country's land reform agency, and in Colombia, where up to 4 percent of the wages of formal workers are channelled to early child development and skill training programmes benefiting all.

Many other reasons could be cited, but they all point in the same direction: CSI programmes may not be fully valued by workers. This is problematic because it is equivalent to an implicit tax on formal employment. Firms and workers pay more than what workers get or expect to get. This tax is not legislated anywhere, nor does it generate revenue for the government, but results from the fact that, given the functioning of the institutions associated with CSI, there is a gap between statutory benefits and the real-life experiences of workers.

Another factor influencing whether firms and workers are in the first column of table 5.3 are minimum wage and job stability regulations. These regulations are bundled together with CSI programmes, and they also influence firm behaviour, including hiring decisions. Minimum wages vary widely. In some countries, such as Mexico, they are set low relative to the wage distribution, and, in others, such as Colombia, they are set high (see box 5.6). In Chile, there is a single countrywide minimum wage for workers ages 18 to 64, but, in Dominican Republic, there are three, which increase with firm size, as in Honduras, where there are four and where they also differ across 10 sectors. As a result, the extent to which they affect firm hiring decisions varies.

Job stability regulations vary as well, but they vary less than minimum wages. All countries have provisions limiting the conditions under which firms may dismiss workers. In a few, such as Chile and Jamaica, they allow firms to reduce their labour force if demand falls or if there is a labour-saving technical change. But most countries limit the just cause for a dismissal to worker misbehaviour (shirking, stealing, and so on). Exogenous shocks faced by firms are not accepted as just cause, and, if workers are dismissed for an unjust cause, they can sue the firm and be entitled to be reinstated in their jobs or receive compensation proportional to the time spent at the firm. Actual results depend on the labour tribunals interpreting these provisions and the institutions enforcing the rulings of the tribunals.[16] Practices are varied, and laws intersect with court rulings. In some cases, as in Peru, these rulings de facto impede firms from dismissing workers with a permanent contract (which helps explain why only 10 percent of all privately employed workers in Peru have permanent contracts).

These provisions increase the expected cost of hiring workers formally because firms know that, at some future date, they might face a negative shock. Accordingly, they respond in many ways. They may limit formal hiring, shorten the length of labour contracts, subcontract some tasks to independent workers (if they can be hired under a commercial contract), or hire informally. Whatever the exact mix, the result is the same: formal employment is deterred.

[16] The protection that workers covered under these provisions actually receive depend on many factors: the monetary or reputational costs of suing firms, the length of court proceedings, and the ability to collect compensation from firms, which usually depend on the size of the firms. Few countries collect sufficient data to make a proper assessment. In the case of Mexico, Kaplan, Sadka, and Silva-Mendez (2008) find that few dismissed workers collect the full compensation to which they may be entitled.

Subsidy to informality

Consider the second column of table 5.3. In countries in which some form of informal participation in the labour market is legal, informal employment is subsidized by NCSI programmes. Workers receive free benefits that they would have to pay for if their jobs were formal. Recall that not all informal workers are poor, and some earn more than formal workers, as exemplified by the overlap between the formal and informal earnings distributions in Ecuador and Peru (see figure 5.5). The subsidies rise with the generosity of NCSI programmes and may be enhanced if social assistance programmes for poor workers are conditional on informal employment.

The border between a self-employed worker and a micro-firm is fluid: a situation facilitated if those participating in the firm are relatives. In this case, the relation of dependency between the firm owner and firm workers is ambiguous, and social norms sanction the not necessarily illegal non-compliance of such a firm with minimum wage and job stability regulations. The firm may be informal without necessarily breaking the law. In fact, some of these firms may not even pay wages; rather, the firm's surplus is distributed among participants through rent-sharing agreements or cultural norms.[17] This situation may not hold if the firm grows, but, while it is small, this offers the firm great flexibility in its hiring and remuneration decisions and in its ability to adjust to shocks. Because workers and owners in these firms benefit from NCSI programmes, they are also subsidized by them.

Consider the third column of table 5.3. Workers and firms are, in principle, breaking the law. But their response to this situation depends on the interplay of factors pulling in opposite directions. On one hand are the subsidies of the NCSI programmes and, in the case of firms, lower labour costs and flexibility in remunerations and adjustment to shocks. On the other hand are fines and sanctions.

Institutions in charge of enforcement play a central role in this case. These institutions vary across LAC. Sometimes, they work on their own; sometimes, they work in tandem with the tax authorities. In general, however, fines depend on the size and sector of the firm. Economic activity in medium and large firms and higher-income self-employed workers are more likely to be sanctioned and thus less likely to be in the third column. But micro- or small firms are less likely to be detected. Workers and firms in these cases can safely be in the illegal column and benefit from NCSI programmes. This is even more so if tacitly accepted social norms sanction their behaviour. Few expect a two-person firm in Ecuador to be fined for not enrolling its workers with the Ecuadorian Social Security Institute or not complying with minimum wage and job

[17] This helps to explain the large number of workers who appear as non-remunerated in household or employment surveys (for example, 10 percent in Peru). Some living and consuming in the household may be paid in kind.

stability regulations; few expect rural workers in Jamaica to be sanctioned if they fail to contribute to the national insurance scheme.

The interplay of the factors listed in table 5.3 varies across the countries in LAC. There are differences in the laws on who should participate in CSI programmes, the rules on eligibility for benefits and the quality of services; in the coverage, generosity, and rules of NCSIs and targeted transfer programmes; in the regulations on minimum wages and job stability; in the institutions charged with enforcing the rules; and in the circumstances under which social norms replace laws and allow de jure illegal behaviour to persist. These issues are discussed in the background papers for this report that examine social protection in 10 LAC countries, although some factors are difficult to quantify.[18] Altogether, they are part of the explanation of the heterogeneity across countries in the formal-informal composition of the labour force, the legal-illegal composition of informal employment, and other labour market outcomes that are critical to social protection outcomes in the region.

But, overall, based on the country studies and the discussion above, it is possible to state, mutatis mutandis across individual countries, the following:

- Social protection policies tax formality and subsidize informality.
- The tax on formality increases as the actual benefits derived by workers from CSI programmes fall short of the costs to the workers and firms.
- The subsidy for informality increases with the generosity or quality of NCSI programmes (and social assistance programmes conditional on informal status).

This does not imply that informal economic activity in LAC arises only because of social protection policies.[19] The behaviour of firms and workers also depends on tax, credit and other policies. Nonetheless, social protection policies contribute to informality.

Special regimes

Many countries in LAC have special tax and social insurance contribution regimes for small firms or self-employed workers. These regimes have multiple objectives, including to reduce income inequalities by subsidizing low-income entrepreneurs, to facilitate the incorporation of self-employed workers in CSI programmes, and to provide administrative facilities so small firms and the self-employed are able to comply with their tax and social insurance obligations. These special regimes are varied. In some cases, such as Argentina, contribution rates are lower for self-employed workers and are merged with personal income taxes.[20] In others, they apply to firms. Sometimes,

---

[18] UNDP LAC Working Papers 14–23.

[19] Informal economic activity is defined as the activity of those firms and workers excluded from CSI programmes, regardless of whether this is because of evasion or legal exclusions, that is, table 5.3, columns 2 and 3.

[20] This is the monotributo regime. Brazil has a similar regime, the microempreendedor individual, although the microempreendedor can have one additional employee (thus, a two-person firm). In addition, Brazil has a separate regime, Simples, for firms with sales below a set threshold.

as in Mexico, there is only one special regime, but, sometimes, as in Ecuador and Peru, there are two. In all instances, either income taxes or contributions for CSI and other mandated benefits, or both, are reduced based on thresholds associated with income (workers) or sales or number of workers (firms).

These regimes are important in that, in some countries, most firms and workers are covered by them. They are motivated by social protection objectives, but, like CSI and NCSI programmes, they have a direct bearing on the behaviour of firms and workers and thus on social protection outcomes.

Table 5.4 illustrates the case of Peru, where firms are classified by size into three groups: micro, with sales up to US$180,000 a year; small, with sales up to US$2,000,000; and large. Large firms are under the general regime of CSI and minimum wage and job stability provisions, and micro and small firms are under special provisions if they have fewer than 10 workers. In addition, firms face different income tax regimes depending on size, although the definitions are different and involve more thresholds (and are therefore not shown here).

Table 5.4: Contributions to CSI rise with sales, increasing the labour costs of firms

Special regimes for firms in Peru

	Micro	Small	Large
Contributions to CSI as a share of the firm's payroll			
(share of wages, including additional mandated benefits)	18	36	50
Severance pay (months of salary by tenure)			
1 year	0.3	0.7	1.5
2 years	1.7	3.3	7.5
3 years	3	4	12

Source: Ñopo 2021, Background Paper of the UNDP LAC RHDR 2021.

These regimes make it difficult for Peruvian firms to grow. CSI contributions double or triple as sales expand, increasing the labour costs of firms. In parallel, the contingent costs of labour also increase because severance pay when workers without a permanent contract are dismissed also increases sharply with sales (while those with a permanent contract cannot be fired). Furthermore, if growing implies employing more than 10 workers, firms no longer qualify for the regime, even if sales are below the thresholds. While the regimes seek to facilitate firm and worker formality, they have little effect, in part because they interact with the factors listed in table 5.3 that also bias the decisions of firms and workers towards informality (but also with other elements in the business environment, such as the imperfect enforcement of contracts or property rights). The result is that six micro- or small firms out of seven in Peru do not comply with the obligation to offer formal employment and that those that do comply face sharp barriers to growth.

There are also two special regimes for firms in Ecuador. In one, the Régimen Impostivo Simplificado Ecuatoriano (Ecuadorian Simplified Tax System), if sales are below US$60,000 a year, a firm can consolidate the value added tax and corporate taxes in a single payment that depends on the sector of activity and the value of sales. In addition, for every worker hired formally, the firm receives a 5 percent discount on the consolidated payment, cumulative up to 10 workers, so that, at that point, the tax burden is reduced by half. However, if the firm hires an additional worker, it no longer qualifies for any discount. The result is that the cost of the 11th worker is extremely high because it implies a doubling of the firm's tax burden. Yet, if sales exceed US$60,000, but are less than US$300,000, the firm can no longer qualify for the simplified tax system, but can qualify for the second regime, whereby it pays corporate taxes at 2 percent of sales; beyond that, it pays 22 percent of profits under the general regime. Clearly, these regimes are part of the reason why, in Ecuador, more than three fourths of all workers are self-employed or employed in firms with up to 10 workers (but with an average of 2).

Special regimes have many implications, including for tax collection. Here, only three are highlighted that are relevant to social protection. First, workers may receive subpar protection from risks because they or the firms that employ them are exempt from participation in some CSI programmes (such as life and disability insurance) or job stability regulations. Second, the regimes allow low-productivity firms to survive because their labour costs or tax burdens are lower, at times by large margins. Third, the regimes may impede the growth of firms that are small, but that exhibit higher productivity because their after-tax profits may be lower if they no longer qualify for the regimes. These regimes do promote entrepreneurship and job creation, but the firms and jobs involved o broader social protection or more well paying opportunities.[21]

The implications for productivity and growth

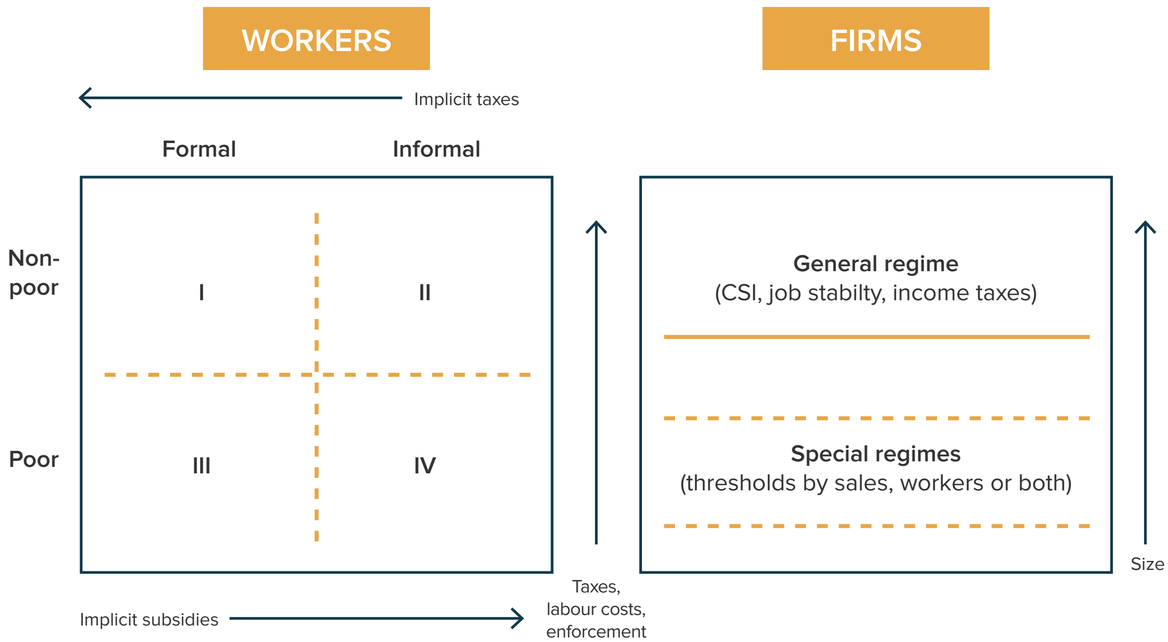
Special regimes interact with regulations on CSI, minimum wages, and job stability and with NCSI and social assistance programmes. Figure 5.6 presents a stylized

[21] For the case of Mexico, Levy (2018) finds that firms captured in the economic census that have annual sales under US$100,000—the threshold to qualify for the special regime, in which taxes are 2 percent of sales versus the 35 percent of profits in the general regime—employ 52 percent of all workers and account for 25 percent of the capital stock. The majority are below the 25th percentile of the productivity distribution. But among firms with high productivity and sales close to, but below the threshold, after-tax profits fall if an increase in sales moves them beyond the threshold. Thus, these high-productivity firms are better off staying small.

description. Panel a shows the same classification of workers by labour status and income presented in figure 5.2, with the addition of the arrows above and below that summarize the discussion of the tax on formality and the subsidy for informality. Panel b shows that the tax burden on firms increases with firm size as a result of special regimes and enforcement efforts that are also proportional to firm size.

Figure 5.6: Special regimes punish productivity because they encourage informality and smallness

Interaction between social insurance, social assistance, and special regimes



Source: Levy and Cruces 2021, Background Paper of the UNDP LAC RHDR 2021.

A central result follows from figure 5.6: social protection policies, including special regimes, bias the allocation of resources—labour, capital, risk-taking, talent—towards informality and smallness.

Informal self-employment is promoted because informal workers may not be required to contribute, and, even if they are required to contribute, they are unlikely to be sanctioned if they do not. It is also promoted because, in both cases, they receive free NCSI benefits. Small complying firms are promoted because they face lower labour costs and tax burdens from special regimes. For them, growth may reduce after-tax profits as they abandon the protective umbrella of the regimes. Small non-complying firms are promoted because they have substantially lower labour costs and more flexibility, while their workers receive free NCSI benefits. For these firms, growth may require that they change their contractual structure and hire dependent workers, with the associated costs and risks, or that they increase their exposure to sanctions in case they have already hired dependent workers. In both cases, growth implies losing free NCSI benefits and paying for CSI benefits that their workers may not fully value. The fact that most firms in the region are small and do not comply with labour market, tax and other regulations and that self-employment is substantial and mostly informal is evidence that the factors captured in figure 5.6, no doubt interacting with others outside the domain of social protection, are quite powerful.

Firms that do not comply with labour market and social insurance regulations are substantially less productive than those that do comply. In Peru, for instance, firms with up to 5 workers and mostly non-compliant are 94 percent less productive than firms with more than 50 workers and mostly compliant. More generally, many studies have documented that, in LAC, economic activity that relies on informal work arrangements is less productive than activity that does not rely on such arrangements.[22] It is the condition of informality more than the condition of size that accounts for differences in productivity. In Mexico, for example, firms with up to five formal workers are between 20 percent and 50 percent more productive than their counterparts of the same size with informal workers. However, there are 16 times more firms in the latter category than in the former. That is why low productivity, informality and smallness are conflated.[23]

What is worrisome from the point of view of productivity is not that not that firms have different sizes, but that resources are allocated to firms of very different productivities. If all firms exhibited similar productivity, size would not matter much; reallocating resources among them would leave aggregate productivity basically unchanged. Pernicious to productivity is the fact that substantial resources are allocated to small, low-productivity firms and to informal self-employment and that small firms compliant with the regulations are impeded from growing and attracting more resources. The forces depicted in figure 5.6 play an important role in these outcomes.

Informality is a problem for social protection because informal workers are less well protected from risks and generally have access to lower-quality services relative to formal workers and because poor informal workers face more difficulty escaping from poverty and, if they do escape, to avoid falling back into poverty. Equally important, informality is closely associated with lower productivity, which is a critical factor in determining worker earnings and an equally critical factor in determining long-term growth.

The current architecture of social protection policy in the region thus results in a problematic trade-off. There is a clear need to improve social insurance and redistribute more towards workers who are informally employed, particularly if they are poor. But, if this is accomplished through better NCSI programmes and more generous targeted transfer programmes, the productivity of the economy is punished; so is long-term

---

[22] See Pagés (2010), Lederman et al. (2014) and CAF (2018) for regional studies, Ulyssea (2018) on Brazil and Levy (2018) on Mexico.

[23] Levy (2018).

growth potential; and, indirectly, the opportunities for workers to obtain more well paying jobs. Even if this course of action were fiscally sustainable over the medium term, which in many countries is not the case, it is clearly not the route towards more rapid economic growth and more equal societies.

5.6. Where do we go to from here?

This report is motivated by the observation that LAC is simultaneously one of the most unequal and most slowly growing regions in the world. Chapters 3 and 4 offer some explanations for this unfortunate outcome, which is associated with deeply rooted problems, such as the inability of governments to provide public security and reduce violence; or the persistence of groups in society—usually associated with large firms, but, at times, with powerful unions—that extract rents, while inducing inefficiencies that limit growth.

This chapter provides a complementary explanation. With variations across countries, the region's social protection policies segment the labour market, provide erratic risk protection to households, do not redistribute income sufficiently towards lower-income groups and sometimes redistribute income in the opposite direction, and bias the allocation of resources in ways that punish productivity and long-term growth.

This is worrisome because social protection is a key tool for mitigating inequalities and fostering social inclusion. It is difficult to think of a strong social contract in any society without a well-functioning social protection system. Indeed, the absence of such a system in some countries in LAC may be central to understanding the weakness of the social contract in these countries and the persistence of violence, distrust of the law, and perceptions of inequity documented in this report. The costs of an ineffective social protection system can be large and spill over into beyond the social domain.

Looking back

To chart a path for the future, understanding the path to this point is essential. Two moments stand out in the development of LAC's current social protection architecture. The first was passed more than 75 years ago when countries began the construction of social protection systems, by and large imitating the Bismarckian models of social insurance in Europe: wage-based contributions earmarked for a bundle of health care, pension, and other benefits; income floors through minimum wages; and job stability provisions to ensure that workers were always protected regardless of the vagaries of the labour market.

The second moment was passed in the early 1990s when countries emerged from the lost decade of the 1980s with large poverty rates and most workers excluded from the combination of CSI programmes, minimum wages and job stability provisions established a half century earlier. Rather than coming to grips with the underlying flaws in this architecture, governments introduced a mix of non-contributory programmes, mostly for health care and pensions, coupled with targeted programmes for the poor, often involving CCTs. The specificities of these programmes varied across countries, but, overall, the expectation was that the need for them would gradually subside. Macroeconomic stabilization, investments in education, and other efforts would accelerate growth, reduce informality, and raise incomes, increasing the share of the workforce covered by the protections associated with formality. In parallel, inequality would narrow because of the combination of more education and more encompassing social protection.

This expectation was only fulfilled in part, although the results varied by country. In most countries, poverty rates did fall, and this is certainly an achievement. But inequality fell substantially less, has reverted in some cases, and, in most, persists at unacceptable levels (even before accounting for the expected effects on inequality of the COVID-19 pandemic). Despite three decades of effort, the majority of workers in the region are still informally employed, working on their own, or active in small fragile firms, with erratic access to insurance and insufficient opportunities to exploit their additional years of schooling. And growth has been far from stellar.

This chapter argues that the complex and, in the end, ineffective architecture of social protection in the region is one of the reasons for these outcomes and, in some countries, perhaps the main reason. One may find the root of the problem in the articulation of social protection around worker status in the labour market and in the combination of programmes that sometimes offer workers entitlements to social benefits and sometimes not; that are at times paid for through general revenues, at times through contributions by firms and workers, and at times from out-of-pocket expenditures; that are associated with services of varying quality and capricious rules of access; and that, mutatis mutandis across countries, sometimes discriminate by type of labour contract, by region, or by the size of firms.

With the benefit of hindsight, it is now clear that socially inclusive growth can hardly occur if the main social protection programmes segment the labour market and induce behaviours by firms and workers that are pernicious to productivity. And, if the response to the low incomes associated with low productivity is more social protection programmes that, while they may improve some social protection outcomes, deepen the forces that punish productivity.

Stronger, more effective social protection is needed in LAC: more inclusive and redistributive, and friendlier to growth. Based on the region's experience, it is unlikely that this will occur only if taxes are raised and more is spent on the same or similar social protection programmes. The articulation of programmes around worker status in the labour market, the sources of financing, and the rules of access must also be reconsidered.

Universal social protection

One cannot expect social inclusion if institutions and policies segment employment and the labour market. Looking forward, a key guiding principle for social protection in the region must be universality with respect to the relevant population, understood in three complementary dimensions, as follows:

- The entire population exposed to a given risk needs to be covered through the same programme.
- The source of financing should be the same for each programme, based on the type of risk covered.
- If programmes provide benefits in kind, the quality should be the same for all.

These principles have different implications for programmes in health care, life insurance, disability, and retirement pensions, as well as for protections against the loss of employment and for poverty. In health care, for example, workers face the risk of illness regardless of the type of contract they may have with a firm, the size of the firm, or their transitions between working for themselves and employment at a firm. If they are to be protected equally all the time and to avoid a bias in their occupational decisions, or in firm size or contractual structure, access and quality need to be delinked from labour status, as does financing. This can only be accomplished if the same health programme covers all and is financed through general revenues, implying the elimination of wage-based contributions for health care and the distinction between contributory and non-contributory programmes (as in Brazil).

More generally, the principle of universality with respect to the relevant population provides a guide for evaluating who should be covered by each programme and which programmes should be financed through general tax revenues, contributions by firms, or worker contributions. It also provides a guide for the evaluation of proposals for new policies, such as a universal basic income.[24] A social protection system built around this principle offers the region a route to increasing spending on social protection while strengthening the foundations of long-term growth, as well as a route to enhancing social inclusion.

---

[24] See Levy and Cruces (2021).

Universality also opens new avenues to combating poverty. The poor would have access to insurance under the same conditions as everybody else, including services of equal quality. As important, the obstacles stemming from existing social protection policies restricting their access to better jobs would be removed. The road out of poverty would be widened by more productive opportunities; and the road back to poverty narrowed by better insurance. The bulk of the redistributive effort would derive from universal transfers, some in kind and some in cash. In this context, targeted income transfers, aside from playing a secondary role, would more likely be transitory.

Universality would represent a major change in social entitlements. For the purposes of social protection, the norm would be equality under the law. Social protection would contribute to phasing out the formal-informal segmentation of the economy, perhaps the single most important factor in the generation of exclusions and inefficiencies in LAC.

The principle of universality with respect to the relevant population is not a rigid blueprint to be followed everywhere. There are variants and combinations of policies, as well as specific parameter values for each, the pros and cons of which depend on the characteristics of individual countries, including political preferences for taxation and social solidarity.

Universality is impossible without an increase in the tax burden. However, if the OECD countries are taken as reference, there is space in almost every country in LAC to increase the tax burden through higher taxes on income, property and activities harming the environment and through a reconsideration of special tax regimes; in some countries, also through higher consumption taxes or lower generalized subsidies, particularly for fuel and, in all, through lower evasion rates (which go hand in hand with less informality). The specific combination will differ across countries. But, over such routes, taxation could make three key contributions to social protection: fund programmes, reduce income inequality directly, and facilitate productivity growth.

A complex political economy must be dealt with, and many will stand in the way of more taxation. However, societies may also reject more taxes because of low-quality services. In these cases, universality may be the driving force for an effort to renew the institutions delivering the services, particularly in health care. Universality can open a path to escape from the vicious circle of low quality in services and lack of willingness to pay taxes.

Constructing universal systems of social protection should be considered a process, not a once and for all event; a process during which, inevitably, there will be unexpected exogenous shocks, as well as resistance from groups affected along the way, but also a process that may create winners, change the balance of power, and open opportunities for further reforms. From this perspective, a vision of the desirable social protection system is indispensable to helping policymakers navigate successfully through choppy waters, and universality in the three dimensions listed above can provide this vision.

From this perspective, independently of whether individual reforms are carried out rapidly or slowly, compatibility and proper orientation are critical. The transition from the status quo to more universal systems will be complex in all countries, but different in each. Initial conditions differ as well as administrative capabilities; the same holds for social priorities. But when opportunities for change appear, clarity is essential in the aim of policymakers. If social protection is to be more inclusive and redistributive, fiscally sustainable, and friendlier to growth, it needs to be more than a set of outdated laws and disjointed collections of programmes financed from whatever combination of taxes and contributions can be assembled. It needs to ensure that everybody is protected; that income is redistributed towards those in need, that the policies deployed to achieve these goals provide incentives to firms and workers to increase productivity, and that the sources of revenue are sustainable.

The crisis associated with COVID-19 may be a third moment in the history of social protection in the region. This crisis is different from the debt crisis of the 1980s. The former is a truly exogenous event caused by a virus; the second was in large measure endogenous, caused by poor macroeconomic management. Yet, there is one dimension in which the current crisis may be similar to the crisis of the 1980s: it may be followed by substantive changes in social protection and taxation, as countries struggle to contain the social damage, restore fiscal balance, and resume growth. In this sense, the response of the 1990s to the lost decade that preceded it offers LAC an extremely valuable lesson. Under the current social protection system, raising taxes to fund more social spending will not result in shared and sustainable prosperity. Under a universal system, the result would be different: the region would be less unequal and could grow more rapidly.

References

Altamirano Montoya, Álvaro, Solange Berstein, Mariano Bosch, Manuel García Huitrón, and María Laura Oliveri. 2018. *Presente y futuro de las pensiones en América Latina y el Caribe*. IDB Monograph, 649 (November). Washington, DC: Inter-American Development Bank.

Alvarado, Francisco, Marcela Meléndez, and Marcela Pantoja. 2021. "El sistema de protección social en Colombia". UNDP LAC Working Paper, 14, 2021, Background paper for the *Regional Human Development Report for Latin America and the Caribbean 2021*, Bureau for Latin America and the Caribbean, United Nations Development Programme, New York.

Alzúa, María Laura, and Ana Pacheco. 2021. "Proteccion Social, Formalidad y Subsidios Cruzados: Evidencia para Argentina". UNDP LAC Working Paper, 16, 2021, Background paper for the *Regional Human Development Report for Latin America and the Caribbean 2021*, Bureau for Latin America and the Caribbean, United Nations Development Programme, New York.

Araujo, María Caridad, Mariano Bosch, Rosario Maldonado, and Norbert R. Schady. 2017. "The Effect of Welfare Payments on Work in a Middle-Income Country". IDB Working Paper, IDB-WP 830, Inter-American Development Bank, Washington, DC.

Barinas, Sócrates, and Hugo Rolando Ñopo. 2021. "Políticas de protección social y laboral en República Dominicana". UNDP LAC Working Paper, 18, 2021, Background paper for the *Regional Human Development Report for Latin America and the Caribbean 2021*, Bureau for Latin America and the Caribbean, United Nations Development Programme, New York.

Besley, Timothy J., and Ravi Kanbur. 1991. "The Principles of Targeting". In *Current Issues in Development Economics*, edited by Vudayagi N. Balasubramanyam and Sanjaya Lall, 69–90. Current Issues in Economics Series. New York, Macmillan.

Bérgolo, Marcelo, and Guillermo Cruces. 2021. "The Anatomy of Behavioral Responses to Social Assistance When Informal Employment Is High". *Journal of Public Economics*, 193 (January): 104313.

Bhalotra, Sonia R., Rudi Rocha, and Rodrigo R. Soares. 2019. "Does Universalization of Health Work? Evidence from Health Systems Restructuring and Expansion in Brazil". IZA Discussion Paper, 12111 (January), Institute of Labor Economics, Bonn, Germany.

de Brauw, Alan, Daniel O. Gilligan, John F. Hoddinott, and Shalini Roy. 2015. "Bolsa Família and Household Labor Supply". *Economic Development and Cultural Change*, 63 (3): 423–457.

Busso, Matías, and Julián Messina, eds. 2020. *The Inequality Crisis: Latin American and the Caribbean at the Crossroads*. Washington, DC: Inter-American Development Bank.

CAF (Corporação Andina de Fomento, Development Bank of Latin America). 2018. *Instituciones para la Productividad: Hacia un Mejor Entorno Empresarial.* October. Caracas: CAF.

CAF (Corporação Andina de Fomento, Development Bank of Latin America). 2020. *Los Sistemas de Pensiones y Salud en América Latina: Los Desafíos del Envejecimiento, el Cambio Tecnológico y la Informalidad*. Caracas: CAF.

Castañón Ibarra, Vicente, and Olaf Froylan Ferreira Blando. 2017. "Densidades de Cotización en el Sistema de Ahorro para el Retiro en México". Boletín Centro de Estudios Monetarios Latinoamericanos, 63 (3): 213–235.

Correa, Alejandra, Maite García de Alba, Elizabeth Alejandra Martínez, Cynthia Martínez, and Annabelle Sulmont. 2021. "El sistema de protección social en México y su contribución a combatir las desigualdades". UNDP LAC Working Paper, 23, 2021, Background paper for the *Regional Human Development Report for Latin America and the Caribbean 2021,* Bureau for Latin America and the Caribbean, United Nations Development Programme, New York.

Cruces, Guillermo, Peter F. Lanjouw, Leonardo Lucchetti, Elizaveta Perova, Renos Vakis, and Mariana Viollaz. 2011. "Intra-generational Mobility and Repeated Cross-sections. A Three-Country Validation Exercise". Policy Research Working Paper 5916, World Bank, Washington, DC.

de Castro, Marcia C., Adriano Massuda, Gisele Almeida, Naercio Aquino Menezes-Filho, Monica Viegas Andrade, Kenya Valéria Micaela de Souza Noronha, Rudi Rocha, et al. 2019. "Brazil's Unified Health System: The First 30 Years and Prospects for the Future". *Lancet* 394 (10195): 345–356.

Firpo, Sérgio Pinheiro, and Alysson Portella. 2021. "Informal and Small: How Labor Market Regulations, the Social Protection System and Special Tax Regimes Impact Formalization, Inequality, Income Volatility, Firm Size and Labor Productivity in Brazil". UNDP LAC Working Paper, 22, 2021, Background paper for the *Regional Human Development Report for Latin America and the Caribbean 2021*, Bureau for Latin America and the Caribbean, United Nations Development Programme, New York.

Fiszbein, Ariel, and Norbert R. Schady. 2009. *Conditional Cash Transfers: Reducing Present and Future Poverty*. With Francisco H. G. Ferreira, Margaret E. Grosh, Niall Keleher, Pedro Olinto, and Emmanuel Skoufias. World Bank Policy Research Report Series. Washington, DC: World Bank.

Flabbi, Luca. 2021. "Implications of Minimum Wages Policies in Labor Markets with High Informality and Frictions". UNDP LAC Working Paper, 25, 2021, Background paper for the *Regional Human Development Report for Latin America and the Caribbean 2021*, Bureau for Latin America and the Caribbean, United Nations Development Programme, New York.

Garganta, Santiago, and Leonardo Carlos Gasparini. 2015. "The Impact of a Social Program on Labor Informality: The Case of AUH in Argentina". *Journal of Development Economics*, 115 (July): 99–110.

Ham, Andrés, and Sergio Arturo Membreño Cedillo. 2021. "¿Cuán efectiva es la protección social en Honduras?" UNDP LAC Working Paper, 21, 2021, Background paper for the *Regional Human Development Report for Latin America and the Caribbean 2021*, Bureau for Latin America and the Caribbean, United Nations Development Programme, New York.

Higgins, Sean, and Claudiney Pereira. 2014. "The Effects of Brazil's Taxation and Social Spending on the Distribution of Household Income". In "Analyzing the Redistributive Impact of Taxes and Transfers in Latin America," edited by Nora Claudia Lustig, Carola Pessino, and John Scott, special issue, *Public Finance Review*, 42 (3): 346–367.

IBGE (Instituto Brasileiro de Geografia e Estatística, Brazilian Institute of Geography and Statistics). 2019. "Conta-Satélite de Saúde: Brasil 2010–2017". Contas Nacionais, 71, IBGE, Rio de Janeiro. https://biblioteca.ibge.gov.br/index.php/biblioteca-catalogo?view=detalhes&id=2101690.

Kaplan, David S., Joyce Sadka, and Jorge Luis Silva-Mendez. 2008. "Litigation and Settlement: New Evidence from Labor Courts in Mexico". *Journal of Empirical Legal Studies*, 5 (2): 309–350.

Lederman, Daniel, Julián Messina, Samuel Pienknagura, and Jamele Rigolini. 2014. *Latin American Entrepreneurs: Many Firms but Little Innovation*. World Bank Latin American and Caribbean Studies Series. Washington, DC: World Bank.

Levy, Santiago. 2018. *Under-Rewarded Efforts: The Elusive Quest for Prosperity in Mexico*. Washington, DC: InterAmerican Development Bank.

Levy, Santiago, and Guillermo Cruces. 2021. "Time for a New Course: An Essay on Social Protection and Growth in Latin America". UNDP LAC Working Paper, 24, 2021, Background paper for the *Regional Human Development Report for Latin America and the Caribbean 2021*, Bureau for Latin America and the Caribbean, United Nations Development Programme, New York.

Lustig, Nora Claudia, 2017. "El impacto del sistema tributario y el gasto social en la distribución del ingreso y la pobreza en América Latina: Una aplicación del marco metodológico del proyecto Compromiso con la Equidad (CEQ)". Tulane Economics Working Paper 1714 (August), Department of Economics, Tulane University, New Orleans.

Marchán, Estefanía, Ramón Espinasa, and Ariel Yépez-García. 2017. *The Other Side of the Boom: Energy Prices* *and Subsidies in Latin America and the Caribbean during the Super-Cycle*. Washington, DC: Inter-American Development Bank.

Massuda, Adriano, Thomas Hone, Fernando Antonio Gomes Leles, Marcia C. de Castro, and Rifat Atun. 2018. "The Brazilian Health System at Crossroads: Progress, Crisis and Resilience". *BMJ Global Health*, 3 (4): e000829.

Mera, Manuel. 2021. "Social Protection in Jamaica: Strengths and Limitations of Its Redistributive Mechanisms". UNDP LAC Working Paper, 20, 2021, Background paper for the *Regional Human Development Report for Latin America and the Caribbean 2021*, Bureau for Latin America and the Caribbean, United Nations Development Programme, New York.

Morales, Matías, and Camila Olate. 2021. "¿Qué tan eficaz es la Protección Social en Chile?" UNDP LAC Working Paper, 15, 2021, Background paper for the *Regional Human Development Report for Latin America and the Caribbean 2021*, Bureau for Latin America and the Caribbean, United Nations Development Programme, New York.

Ñopo, Hugo Rolando. 2021. "Políticas de protección social y laboral en el Perú: Una espiral de buenas intenciones, malos resultados y peores respuestas". UNDP LAC Working Paper, 17, 2021, Background paper for the *Regional Human Development Report for Latin America and the Caribbean 2021*, Bureau for Latin America and the Caribbean, United Nations Development Programme, New York.

Ñopo, Hugo Rolando, and María Alejandra Peña. 2021. "Políticas de protección social y laboral en Ecuador". UNDP LAC Working Paper, 19, 2021, Background paper for the *Regional Human Development Report for Latin America and the Caribbean 2021,* Bureau for Latin America and the Caribbean, United Nations Development Programme, New York.

Pagés, Carmen, ed. 2010. *The Age of Productivity: Transforming Economies from the Bottom Up*. Development in the Americas Series. Washington, DC: Inter-American Development Bank; New York: Palgrave Macmillan.

Piola Sérgio Francisco, José Rivaldo Mello de França, and André Nunes. 2016. "The Effects of Constitutional Amendment 29 on the Regional Allocation of Public Funds for the National Health Service in Brazil". *Ciência & Saúde Coletiva*, 21 (2): 411–422.

Scott, John. 2014. "Redistributive Impact and Efficiency of Mexico's Fiscal System". In "Analyzing the Redistributive Impact of Taxes and Transfers in Latin America," edited by Nora Claudia Lustig, Carola Pessino, and John Scott, special issue, *Public Finance Review*, 42 (3): 368–390.

Tikkanen, Roosa, Robin Osborn, Elias Mossialos, Ana Djordjevic, and George Wharton, eds. 2020. *International Profiles of Health Care Systems 2020*. December. New York: Commonwealth Fund.

Ulyssea, Gabriel. 2018. "Firms, Informality, and Development: Theory and Evidence from Brazil". *American Economic Review*, 108 (8): 2015–2047.

Vakis, Renos, Jamele Rigolini, and Leonardo Lucchetti. 2016. *Left Behind: Chronic Poverty in Latin America and the Caribbean*. Washington, DC: World Bank.