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Public Opinion about the Pension Reform in Albania

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Abstract:

The aim of this paper is to analyze the impact of the information of the public opinion on the political support for pension reform in Albania. An opinion poll on a representative sample suggests that the level of knowledge about the public pension scheme is important for the political support of the pension reform. People who are more informed about the functioning of the pension system are more willing to accept reforms.

In Albania, the level of knowledge about pension scheme is very low. This is because, the pension system is public one and it is a DB pension plan. Shifting from DB pension plan into multi pillar pension system will require increasing public information about the reformed pension scheme.

Key words: pension reform, survey, Respondent-Driven Sampling, probit estimation

Introduction

Albania inherited from communist regime a pension system which was Defined Benefit scheme. Under this scheme, the

current contributions paid by the persons who are working now, are used to pay the current pensioners and it is known as pay as you go (PAYG) plan. This system functions very well when number of contributors is much higher than the number of pensioners. It is based on the idea that the number of employed persons, consequently the number of contributors will increase with the same ratio of natural growth of the population. The Albanian pension system has many problems and now the government is planning to reform it according to the World Bank recommendations. The main aim of this paper is to show that: informed individuals are more willing to accept pension reforms because of their better information about the costs and consequences of the pension system.

If valid, this conclusion would have important policy implications. To increase public support for pension reforms, governments in countries with large and unsustainable public pension systems ought to devote more effort and resources to inform citizens about the basic functioning of pay-as-you-go pensions, about its actual costs, and the net position of individual contributors. But media coverage, by itself, may not be sufficient to inform citizens. If Albanian government seriously wants to improve citizens' knowledge about the consequences of public pensions should find other ways for this.

Literature review

Although employer pension programs vary in design, they are usually classified into two types: defined contribution (DC) and defined benefit (DB). Under a defined contribution (DC) plan each employee has an account into which the employer and the employee make regular contributions. Benefit levels depend on the total contributions and investment earnings of the accumulation in the account.

On the other hand, the inter-generational risk sharing to smooth wealth and consumption among different generations is eliminated because pension benefits for each individual depend

on their own lifetime contributions. Owing to the fact that low-income workers appear to experience greater risks of unemployment, the accumulated funds of these individuals will be both more uncertain and lower than those of high-income workers.

However, there is a significant body of academic research showing that individuals often have limited financial knowledge, and in particular know little about the characteristics of their pensions, including how much to expect (and how much they need) in retirement benefits. A possible reason for this lack of knowledge is that learning about pensions is difficult.

Solutions

Governance in DC pension schemes provides the structures and processes to ensure safeguarding and investing of pension assets in the best interest of the scheme members.

Government must provide a framework for allocating decision-making and monitors responsibilities between the relevant parties, ensuring asset protection, and promoting transparency and disclosure.

Respondent-Driven Sampling

RDS consists of an enhancement of network or "snowball" sampling, in which data on who recruited whom and the extensiveness of network connections provide the basis for calculation of relative inclusion probabilities, population indicators of minimal bias, and the variability of these indicators (Heckathorn 1997, 2002, forthcoming, Salganik and Heckathorn 2004, Volz and Heckathorn forthcoming).

RDS theory is based on two observations (Heckathorn 2002). First, if referral chains are sufficiently long—that is, if the chain-referral process consists of enough cycles of recruitment, or *waves,*—the composition of the final sample with respect to critical characteristics and behaviors will

become independent of the seeds from which it began. After a certain number of waves, the sample composition becomes stable and all members of the target population have a non-zero probably of selection that is independent of seed composition (Heckathorn 2002, Salganik and Heckathorn 2004). Therefore, an important design element in RDS involves methods of increasing the length of referral chains (Heckathorn 1997).

While the final RDS sample composition is independent of seed composition, choice of seeds can affect the rate at which equilibrium is reached and the speed with which sampling will occur (Heckathorn 2002). Recruitment in RDS is often dominated by large recruitment chains initiated by respondents who can be termed "super seeds" (e.g. Heckathorn 1997, Heckathorn et al. 1999, Heckathorn et al. 2002, Ramirez-Valles et al. 2005a). This need not reflect special characteristics of the individual, because it results from a positive feedback process in which, the larger a recruitment chain grows, the greater is the number of respondents working to make it grow even larger, so a "rich-get-richer" dynamic is produced in which the larger chains grow ever more quickly than the smaller chains. Hence, any reasonably productive seed stands a good chance of becoming a "super seed."

Our goal is to estimate an equation of the following type:

$$Y_i = F(X_i , I_i) + e_i \qquad (1)$$

Where Y_i is a binary variable that measures the policy opinions of individual i, X_i denotes his general attributes (such as age, education, gender, and so on), I_i is a measure of how informed he is about the costs and the functioning of the pension system and e_i is an unobserved error term. We are interested in the effect of information on policy preferences.

We view information as determined by an equation of the following type:

$$I_i = G(X_i , Z_i) + u_i \quad (2)$$

Where Z_i is a set of additional observable individual features that determine the information possessed by each individual, and u_i is an unobserved determinant of information.

Methodology of the survey

The target population of this survey is the population 25-64 years old, who is working, with at least university diploma and lives in Tirana. The aim of this research is to collect and analyze the knowledge and the opinion about the pension system in Albania of this group who are well educated and since they are working they participate in the pension scheme as contributors.

Albania inherited from the communist regime a PAYG pension system and like in all other socialist countries this scheme was public and obligatory and still continuous to be.

According to the last census conducted by INSTAT (National Statistical Institute of Albania) in October 2011, the population with tertiary education is 10.7 percent of the population 10 years and over. Based on the same data, population 24-65 years old, who live in urban part of Tirana and have at least university diploma represent 27.9 percent of the population in the same age group.

733 people participated in this survey and they represent about 1 percent of the target population.

This survey is based on snow ball theory and the interviews were conducted via the Internet by using a web application.

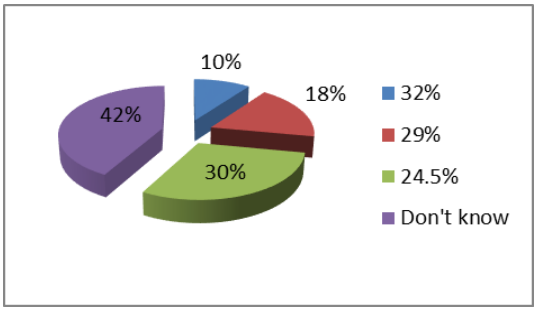
Main findings

A considerable part of the respondents do not know how the Albanian pension scheme is functioning. 42 percent of them do not know the percentage of their salary, which goes for the

social insurance. On the other hand 78.1 percent of them know that the vesting period to be entitled for full pension rights is 35 years. 91.1 percent of the respondents agree that the pension system needs to be reformed.

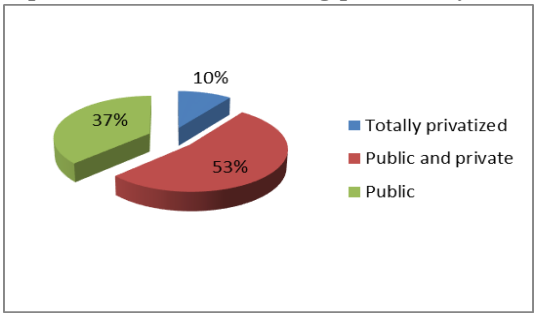
Knowdelge about pension scheme: as it can be noticed from the graph below 42 percent of the persons interviewed neither do not know the percentages of the monthly salary that they pay for social insurance.

Percentages of the monthly salary paid for social insurance



A dominant majority of the persons interviewed about 90,3 percent said that the Albanian pension scheme should to be reformed. Perception reform comes as consequence of the low level of pension benefit, while the contribution rate is high. Regarding the fact that how should be reformed, about 90 percent of them think by improving the parameters of the current public pension scheme, or should be combined private and public by giving the possibility to the individual to decide which one they prefer.

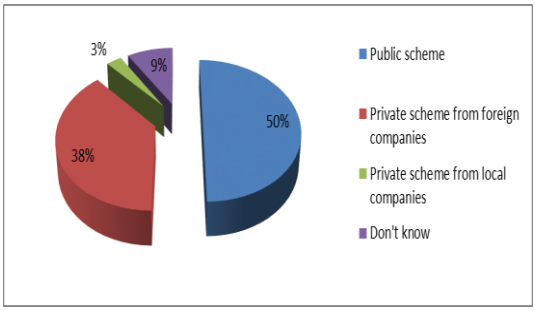
Opinions about reforming pension system



Regarding the question if the liberalization of the insurance market which pension schemes would they prefer, 50 percent of respondents would prefer the public scheme and 38 per cent would prefer the private one, but by foreign companies. This high preference regarding the public pension's scheme even though the profit provided may be lower is related to the guarantee that the state offers.

Distrust pronounced for private schemes is related mostly for the negative experience from the '97 pyramid schemes.

Preferences for pension schemes



Only 14.2 percent of the respondents agree that the retirement age should be increased. On the other hand 74.9 percent think the retirement age should be mandatory, so that young people may have the possibility to be employed. This is related to a high unemployment rate, which recently is estimated to be about 18 percent (INSTAT- National Statistical Institute of Albania) and youth unemployment is estimated to be even higher.

Only 23 percent think the retirement age for women should be equal to that of men. According to the current pension scheme inherited from the old communist system, women retirement age is 5 years lower than the man.

Most respondents about 67.3 percent think that it is necessary to establish a social pension for all those who for many reasons have not paid contributions during the working age even though it means increasing the fiscal burden.

Public opinion on pension reform

Retirement age should be increased	14.2%
The retirement age should be the same for both men and women	23.0%
The retirement age should be mandatory	74.9%
Persons who do not have paid contributions, when they reach 65 years of age should receive a minimum pension	67.3%
Pension benefit should be based on the amount of contributions paid throughout whole contributive life	78.5%
The vesting period should be decreased	60.7%

Opinions on pension reform (the variable *Y* above) are summarized in a single variable. We exploit two questions eliciting opinions about hypothetical reforms via an increase of the retirement age or liberalization of the insurance market. The dummy variable *reform* equals 1 if the respondent is *either* in favor of increasing the retirement age *or* of or liberalization of the insurance market, independently of the answer provided to the other question. *Reform* takes the value zero instead if the respondent is strictly against one of the two reforms *and* does not approve the other.

Info_1 a dummy variable equal to one if the respondent is aware of the fact that the pension system should be reformed and zero otherwise. This variable is available for all respondents.

Finally, *Info_rate* is a dummy variable equal to one if the respondent is aware of the percentage of her/his wage that goes to pay pension contributions, adding up the contributions paid by employer and employee. All the respondents were asked for this question since they all are employed.

Biprobit estimation

Our first method to cope with the joint determination of information and policy opinions is to rely on functional form restrictions. In particular, we jointly estimate equations (1) and (2) by maximum likelihood methods, exploiting the fact that we can measure both policy opinions and information as binary variables. Identification is achieved through a functional form assumption: we assume that the error terms in (1) and (2) are

jointly normally distributed, and that the equations $F(.)$ and $G(.)$ are both linear. To estimate with probit, we need to measure information as a binary variable.

Once more, informed individuals are more likely to favor reforms, and the effect of information is statistically significant. The coefficients are larger and the standard deviations smaller compared to the simple probit regression and the propensity score matching estimators, a further confirmation that the estimates that assume exogeneity are biased downwards.

Concluding remarks

- Knowledge of people associated with the current pension scheme are very limited:
- Due to the negative experience of the pyramid scheme of '97, today's contributors may feel more confident in the public scheme and would prefer to be part of it. On the other hand they would like reforming this scheme, referring to the low level of retirement benefit.
- Given that the unemployment rate is very high, especially among young age groups, persons interviewed are against raising the retirement age and equalizing the pension retirement age between men and women.
- Most of those interviewed were in favor of the social pension, giving to persons who have not paid contributions, an opportunity to have a minimum pension.
- The level of financial knowledge regarding the functioning of a pension scheme is limited

The main result of this paper is the finding that more informed individuals are more willing to accept reforms that reduce the generosity of the pension system. The correlation between information and willingness to reform does not seem to reflect unobserved joint determinants of information and policy opinions.

This result has a simple but important policy implication. Pension reforms are politically very difficult. One reason why they are so difficult is also because of sheer ignorance by citizens at large about the costs, sustainability and basic functioning of the pension system. To create consensus in favor of reforms, governments ought to devote more effort to spread information about the consequences and costs of public pensions.

The negative results about the effect of media exposure on information suggest that this task cannot just be delegated only to the media.

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Variables in the Equation

		B	S.E.	Wald	df	Sig.	Exp(B)
Step 0	Constant	-.757	.071	112.991	1	.000	.469

Block 1: Method = Enter

Iteration History[a,b,c,d]

Iteration		-2 Log likelihood	Coefficients			
			Constant	info_1	info_2	Age
Step 1	1	784.967	-.509	-.980	2.818	-.297
	2	733.539	-.309	-1.982	4.018	-.496
	3	719.307	-.223	-2.942	5.007	-.561
	4	715.407	-.212	-3.756	5.824	-.569
	5	714.631	-.211	-4.308	6.376	-.569
	6	714.567	-.211	-4.526	6.595	-.569
	7	714.566	-.211	-4.554	6.622	-.569
	8	714.566	-.211	-4.554	6.622	-.569

Omnibus Tests of Model Coefficients

		Chi-square	df	Sig.
Step 1	Step	422.983	3	.000
	Block	422.983	3	.000
	Model	422.983	3	.000

Model Summary

Step	-2 Log likelihood	Cox & Snell R Square	Nagelkerke R Square
1	714.566[a]	.372	.521

Step	Chi-square	df	Sig.
1	28.959	7	.000

Variables in the Equation

		B	S.E.	Wald	df	Sig.	Exp(B)
Step 1[a]	info_1	-4.554	1.008	20.408	1	.000	.011
	info_2	6.622	1.011	42.925	1	.000	751.523
	Age	-.569	.132	18.683	1	.000	.566
	Constant	-.211	.245	.739	1	.390	.810