SOCIAL SECURITY POLICY AND PENSION REFORMS IN THE WESTERN BALKANS

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Abstract

Despite recent economic growth, the countries of the Western Balkans share a catalogue of social problems ranging from high unemployment, low participation rates, falling birth rates, aging populations, severe poverty, and migration of many young and skilled people. This paper tracks the similarities and differences in the various countries in response to these difficulties, with a focus on pension systems reform. It shows how social protection systems have been weakened by efforts to cut public expenditure and reduce budget deficits and how, following advice of international organisations and policy advisers, several countries have introduced partially privatised three pillar pension systems in an environment of underdeveloped capital markets. The paper discusses the features of the new reformed pension systems, and reviews the systems in those countries which have not yet adopted such reforms. It highlights the problems and risks facing the partially privatised pension schemes. The paper also considers the context for the different approaches adopted in the region. It concludes that at the present state of their economic transition and development, the late reforming countries would be better advised to focus on improving the efficiency of their existing arrangements, and on the regional coordination of their social security and pension systems, rather than engaging in radical privatisation in pursuit of uncertain benefits.

Keywords: Western Balkans; social security, pension systems; pension reforms; welfare state; economic transition

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INTRODUCTION

In the early 1990s, four new states declared their independence from former Yugoslavia: Bosnia and Herzegovina (BiH), Croatia, Macedonia, and Slovenia. The remainder of the former state reconstituted itself as the Federal Republic of Yugoslavia, which comprised the republics of Serbia and Montenegro. Within Serbia, the autonomous status of the provinces of Kosovo was rescinded in 1990 as the Milošević regime contrived to consolidate its power. Direct rule by Belgrade was imposed on the province, leading to a decade of tension which resulted in the war of 1999 which pitched NATO against Serbia. Kosovo then came under United Nations administration, but has had a provisional government since 2001 with authority over most domestic issues such as social policy including pensions, social security, health and education. Montenegro eventually declared its independence in 2006, while the final status of Kosovo remains undecided. Neighbouring Albania overturned the one-party rule of the Albanian Party of Labour (the communist party) in 1991, and has succeeded in making its transition to democracy in a context of widespread poverty, accompanied by mass internal and external migration. The EU has had a natural policy interest in the region, since it is a core European region. Slovenia became an EU member in 2004, but the other countries have so far remained outside the EU, and have collectively become known as the ‘Western Balkans’, a term invented by the European Commission to provide a framework for its pre-accession policies towards this group of countries.

3 BiH (BiH) emerged from three years of intense warfare between 1992 and 1995 with a complicated constitution which effectively partitioned the country into two entities. The Federation of BiH (FBIH) covers 49% of the territory populated mainly by Muslim and Croatian ethnic groups. It is governed under a complex federal structure based on cantons. Within FBIH the Croatian inhabited region of Herzegovina is de-facto semi-autonomous with strong economic, financial, and political links to neighbouring Croatia. The other entity, Republika Srpska (RS), covers 51% of the territory, and is mainly populated by the Serbian ethnic community. The RS has strong links with neighbouring Serbia. The central government of BiH has relatively few powers, and responsibility for social security, pensions, health and education is devolved to the entities, and within FBIH, to the cantons.

4 The Provisional Institutions of self-Government (PISG) were established in May 2001, consisting of a government, an assembly, and a presidency.
The wars in Croatia in 1991, BiH from 1992-5, in Kosovo and Serbia in 1999, and the violent civil conflict in Macedonia in 2001, destroyed much physical infrastructure and displaced hundreds of thousands of people. Albania also suffered a severe civil conflict in 1997 after the collapse of a number of pyramid savings banks wiped out the life savings of hundreds of thousands of people, leading to a popular uprising, widespread destruction of state property, and the collapse of the government (Vaughan-Whitehead 1999). The economy of the Federal Republic of Yugoslavia suffered from poor macroeconomic policies and hyperinflation, as well as the effects of UN sanctions. The 1999 NATO bombing campaign destroyed many infrastructural and industrial facilities and led to a further sharp fall in real GDP. In Macedonia, the recovery from post-independence recession which had begun in 1996 was brought to an end by the civil conflict of 2001.

Following the democratic changes that took place in Croatia and the Federal Republic of Yugoslavia in 2000, the Western Balkan economies have entered a period of more or less sustained recovery. Economic growth has been strong compared to performance over the previous decade, averaging 4% per annum from 2000-5. Albania has experienced the most rapid growth, averaging almost 6% over the same period, although this was based largely on labour export and remittance income, with little impact on employment levels. By 2003, GDP growth in region was above the EU average including the new EU member states from Eastern Europe (Sanfey et al., 2004)\(^5\). Nevertheless, the economic situation remained difficult, and by 2003 none of the countries except Albania had surpassed the level achieved in 1989\(^6\). Taking 1989 as a benchmark, by 2003 Croatia had made the strongest recovery, reaching 91% of

\(^5\) Only Kosovo experienced negative growth due to reduced international assistance and the failure to implement effective reforms.

\(^6\) UNECE Economic Survey of Europe, Geneva, 2004(2). Comparative data on the respective countries are relatively scarce although in recent years more data has been compiled by international agencies including the UN Economic Commission for Europe (UNECE, the European Bank for Reconstruction and Development, the ILO, the UNDP, the World Bank and other organisations. Data are also available online from almost all the respective national statistical agencies, although with patchy coverage. Data for BiH are most problematic, since statistics are collected by separate statistical agencies in the two entities, FBiH and RS. The capacity of the central statistical agency of BiH to reconcile these data at a national level is limited.
its 1989 level of GDP. Macedonia reached 81%, and Serbia-Montenegro reached only 50% of its previous level. It is therefore hardly surprising that some of the poorest countries in Europe are to be found in the Western Balkan region. According to World Bank data, BiH had an average income per capita of just $2,440 in 2006, while the level of per capita income was only marginally higher in Albania, Macedonia and Serbia. The exception is Croatia which has an average per capita income more than three times that of BiH, and above that of some of the new EU member states.

Even though the region has experienced rapid growth in recent years, social problems remain deep as a result of the years of stalled transition and extended conflict. Labour market outcomes are particularly problematic with high levels of unemployment, low participation rates, and large informal economies (Bartlett 2007a). Survey data indicate that the unemployment rate is highest in Kosovo, at an extraordinary 41%, followed closely by Macedonia at 37%. In BiH the unemployment rate was 22% in 2004, according to household panel survey data. In Serbia and Montenegro, labour force surveys showed that the unemployment rate increased from 12% in 2001 to 21% in 2006 as pro-market economic reforms were introduced. In Albania, unemployment peaked at 27% in 1992, following which economic growth and mass emigration reduced unemployment to an average of 16% between 1995 and 2003 dipping down to 13.8% in 2006. In Croatia, according to the labour force survey the unemployment rate in 2005 was just over 12%, having fallen for several years as economic growth began to create jobs.

Since the end of the Kosovo war, the EU has taken a more active interest in the region and the prospect of EU membership is now a real one for all the Western Balkan countries, albeit at different speeds. Two countries, Croatia and Macedonia, have become candidates for EU membership, and Croatia is expected to become an EU member state by 2010. Albania and Montenegro have signed Stabilisation and

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7 Data on GDP and related statistics is available online from the World Bank and the IMF.
8 Labour Force Surveys are carried out in most countries of the region and are available at the websites of national statistical offices. In BiH data is taken from a Household Panel Survey. Albanian data refer to registered unemployment, which is thought to be more accurate than in the case of the Yugoslav successor states where access to health insurance provides incentives for false registration.
Association Agreements with the EU, while BiH has initialled its Agreement. Only Serbia appears hesitant to move along the path of EU accession. Negotiations for a Stabilisation and Association Agreement have been stalled pending Serbia’s further cooperation with International Criminal Tribunal on the former Yugoslavia in The Hague, while the contentious issue of Kosovo’s future status is also a factor in determining the willingness of the two sides to pursue the accession option. The EU made clear its commitment to the eventual accession of the Western Balkan countries at the Thessaloniki summit in 2003 (EC 2003). Since then it has supported the Stabilisation and Association process which has provided a framework for support for pre-accession assistance to the countries of the region, backed up by substantial programmes of financial and technical assistance. This process is likely to be accelerated under the Slovenian EU Presidency in the first half of 2008.

EU accession prospects raise the issue of the coherence of social security policies with the process of EU integration. The social dimension of the EU, elaborated in the *social acquis*, focuses on labour market policy, social dialogue, gender equality, and the portability of pension and social security entitlements. Accession states must comply with these laws and regulations before entering the EU, and the development of EU-compatible social policies is fast becoming a necessary part of the preparation for the integration of the Western Balkan countries into the EU. According to the European Commission:

“As progress is made on stabilisation and status issues are addressed, the Western Balkan countries will increasingly focus on the reforms needed to approach European standards. The economic and social agenda will come to the forefront, as weak economies, high unemployment and inadequate social cohesion are major problems throughout the area. EU policies in the region should focus more on equitable and sustained development and on extending the benefits of economic growth to vulnerable groups and communities by combating unemployment, social exclusion and discrimination and promoting social dialogue” (EC 2006).

Some countries are more advanced in this process than others. For example, Croatia, has already signed a Joint Memorandum on Social Inclusion with the European Commission, covering all areas of social policy and setting out priority policy areas for combating poverty and social exclusion (Government of the Republic of Croatia 2007). The reconstruction effort and the inflow of technical advisors in almost all policy fields has resulted in the importation of new ideas about the delivery of welfare
services, including ideas about the reform of social security and pension systems. In this context, social policy developments reflect internal transition policies, policy transfer from international organisations and advisers during the period of post-conflict reconstruction and, increasingly, the influence of EU policy (Bartlett 2008).

Similar processes had taken place earlier in the EU accession states of Eastern Europe in the 1990s where a variety of external and internal agents of policy transfer influenced the shape of social policy and pension reform. Deacon (1997, 2000) and Deacon and Hulse (1997) documented the role of the World Bank in promoting a neoliberal social agenda in the region which supported the partial privatisation of pension schemes, demonstrating the differences of opinion within the organisation as to how this should be implemented. Other external agencies, such as the ILO, the Council of Europe, the European Union, and the UNDP among others, were also influential. All have had their own agenda, and the outcome has often depended on the relative influences of these external agents of policy transfer in different countries. Orenstein (2005) has emphasised the central role played by the World Bank and USAID in disseminating a three-pillar model of pension system reform based on Chilean experience to the post-socialist countries of Eastern and Southeastern Europe. The European Union had an increasing influence as the process of EU accession speeded up in Eastern Europe in the early 2000s. However, De La Porte and Deacon (2004), in a study of policy transfer to Lithuania, argued that the influence of the EU was below its potential and less than its rhetoric, due to the fragmented manner of its dissemination. Potůček (2004) revealed the weak influence of the EU in social policy reforms in the Czech Republic. Ferge and Juhász (2004) identified the relatively weak role of the EU in Hungarian social policy reform and its late involvement leaving the field open to the World Bank to ‘fully steer’ the pension system reform. Müller (2002a, 2002b) studied the implementation of pension reforms in Eastern Europe and concluded that effective policy transfer required the support of a domestic change agent to support its implementation. In the case of pension reform, the World Bank policy prescription was often implemented only when supported by domestic policy makers within ministries of finance (as in the case Hungary and Poland) and radical reform was rejected when the domestic responsibility was held by ministries of social affairs, themselves influenced by the trade unions (as in the case of the Czech Republic and Slovenia). According to Wagener (2002) political legacies from the
communist and pre-communist period have been instrumental in constraining the extent and direction of reform processes. Thus, in some cases the policy prescription of pro-market pension reform has been resisted by governments where a strong domestic advocacy coalition in favour of traditional solidarity schemes was mobilised.

All these actors and agents of policy transfer have been also active in the Western Balkans. The process there has been rather different to the East European accession states, due to the more intense nature of the policy problems at stake in the context of political instability and post-conflict reconstruction. Following the Kosovo war the European Union, supported by other members of the international alliance which had entered the conflict against Serbia, established the Stability Pact for South East Europe which sought to coordinate the policy advice of the international organisations. In practice it acted as a classical ‘policy broker’, mediating the positions of the various transnational advocacy coalitions that became engaged in offering policy advice to the governments of the region (Bartlett 2007b). It established the Initiative for Social Cohesion (ISC) with a strong input from the Council of Europe and the ILO, to engage with the coordination of policy issues such as employment, health, housing, social dialogue, and social protection. The ISC has established a project for coordination of social protection systems funded by the EU CARDS programme. However, it has had little practical influence on the design of reforms in the field of social security and pension systems, and as in the East European accession states, the field has been largely left open to initiatives from the World Bank and USAID, and to the respective positions of domestic advocacy coalitions within each country.

SOCIAL SECURITY

In the former Yugoslavia, the system of social welfare consisted of a mix of contributory and non-contributory cash benefits and a range of benefits in kind, most available on a universal basis, with some provided by enterprises to their workers (Pošarac 1993). By the beginning of the 1990s the cost of providing such an extensive social welfare system had become unsustainable. Systemic reforms transferred funding from local self-management communities of interest to centralized republican
funds for family welfare. Following the break up of Yugoslavia, each of the successor states inherited these republic-based welfare systems. In contrast, Albania under communism had a classic centralized approach to social welfare based upon full employment. After the collapse of the communist system, social welfare reforms were introduced in line with the transition to a market economy (Xhumari 2003). A means-tested social assistance programme known as Ndihme Ekonomika was introduced in 1993 for urban families with no independent source of income, rural families with small plots of land. This decentralized system relied on a subjective assessment of needs, and directed about half the available resources to the poorest fifth of the population (Alderman, 2002).

The post-communist social security systems that have been put in place are relatively weak due to lack of resources and the deterioration in the capacity of many of the institutions of public administration (Bartlett and Xhumari 2007). In BiH, although one-fifth of the population are entitled to social assistance benefits, in practice the poorer municipalities are unable to provide any benefits to the poor, and about half of the most severely disabled are not adequately protected (Council of Ministers - BiH, 2004). A large part of the resources to finance social security programmes have been provided by international donors, and in recent years a decline in donations have reduced support for the most vulnerable groups of citizens. The social welfare system in Macedonia has a wide coverage, but the level of benefits is set at just 56% of the relative poverty line (ILO 2005: 32). In countries badly affected by conflict, the social welfare of war veterans, war victims, and their families has been a contentious issue. In Croatia, war veterans and their families are entitled to more favourable levels of social security benefits than other citizens, and political support from veterans’ groups played an important role in the electoral victory of the HDZ in 2003. In BiH relatively high social benefits are also made to war veterans and their families. In Republika Srpska a specialized department of the Ministry of Veterans’ Affairs provides veterans with better social services than those available to other groups, and attempts to reduce their privileges have led to vociferous public protests. A reform of veterans’ invalidity insurance benefits was carried out in BiH in 2004 under the terms

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9 The HDZ (Croatian Democratic Union) is the ruling party in the country which was again returned to power, but with a diminished majority, in elections held at the end of 2007.
of a World Bank loan. Certificates of wounds and deaths were reviewed and means-tested disability and survivors’ benefits were reduced. However, the reform met with strong protests from veterans’ associations, which argued that they were entitled to compensation for loss of income during and after the war.

Policies to deal with high unemployment have mainly focused on passive measures to provide income support to unemployed people, while active measures to get people back into work have only recently been introduced in some countries. Due to budgetary restrictions the duration, coverage, and level of unemployment benefits are generally low. Apart from Croatia, unemployment benefit replacement rates are below the EU average, and the coverage rate (the share of unemployed receiving benefits) is low and falling due to increasing proportions of long-term unemployed (Micevska, 2004). In Albania, for example, the coverage of unemployment benefit was around 8% in the period 2000-07. Moreover, passive policies, including both unemployment compensation and social assistance, have become less generous over time throughout the region (Arandarenko, 2004).

Differences between countries in their ability to collect taxes have led to significant differences in public expenditure (see Table 1). Weak tax collection capacity in Albania and Macedonia has held back public expenditure, and a relatively narrow range of public services is provided. In contrast, BiH, Croatia, Montenegro, and Serbia have maintained relatively high shares of public expenditure in GDP. At the same time, in response to persistent weakness in international competitiveness, the IMF has advocated reductions in the level of public expenditure, in order to reduce high government budget deficits. As a result, public expenditure has fallen as a percentage of GDP in high-spending BiH and Croatia, but also in low-spending Albania (see Table 1). In Serbia and Montenegro, the share of public expenditure increased up to 2004 before falling back in recent years. With the exception of BiH and Croatia public expenditure in the region is below the EU average of 47% of GDP.

Table 1: Public Expenditure (2000-6)

<table>
<thead>
<tr>
<th></th>
<th>Total government expenditure (a)</th>
<th>Expenditure</th>
<th>Expenditure on</th>
</tr>
</thead>
</table>


Correspondingly, public expenditure on social security and social protection\(^{10}\) varies in extent throughout the region\(^{11}\). Overall, the countries are divided into a group with relatively high expenditure on social security and social protection - Croatia, BiH, Serbia, and Montenegro - and a group of relatively low spenders - Albania, Kosovo, and Macedonia. The former group of countries have relatively strong social protection although still below the average expenditure as a share of GDP compared to the EU-25. The latter countries have been the most influenced by the neoliberal approach of the IMF in seeking to reduce public expenditure. They also have high levels of informal economic activity and, in the case of Kosovo and Macedonia, very high levels of unemployment, both of which have eroded the tax base. Social security benefits and state funded pensions are therefore relatively low in these three countries (see Table 2). They also rely to a relatively large extent on an inflow of remittances from family members who work abroad to sustain income security in the absence of effective state support.

\(^{10}\) Social security is defined as cash benefits including pensions, paid sick leave, family and child allowances, unemployment benefit and income support and benefits in kind excepting health benefits. Social protection includes social security benefits plus public expenditure on health care.

\(^{11}\) Social protection expenditure covers all social transfers including pensions as well as expenditure on health care.
Weaknesses in the social security system, the limited ability of governments to increase public expenditure for the alleviation of poverty, and the high levels of unemployment have led to a drastic increase in poverty during the transition period and following the various wars and conflicts in the region. In Kosovo, a household survey carried out in 2002 showed that over one-third of the population were living below a poverty line of €1.42 per day (World Bank 2005a). About 15% of the population were living in extreme poverty with insufficient income to cover basic food needs. The incidence of poverty was greatest among families where the head of the household is unemployed, among children, and the elderly. Analyses published in Poverty Reduction Strategy Papers revealed the extent of poverty in Albania, FYR Macedonia, Serbia, Montenegro, and Bosnia-Herzegovina. Measured at a minimum poverty line of $2.15 per day, over 18% of the population in Albania lived in absolute poverty in 2005, as did 9% in Serbia and Montenegro, 6% in BiH, and 4% in Macedonia (World Bank 2005b). Taking a more realistic poverty line of $4.30 to measure vulnerability to poverty, which is more consistent with national poverty lines, as many as 71% of the Albanian population were vulnerable to poverty, 42% in Serbia and Montenegro, 35% in BiH, and 24% in Macedonia. In Croatia, absolute poverty is less severe, mainly affecting the long-term unemployed and people living in war-affected areas. According to the household budget survey, the relative poverty rate was 17% in 2003, being almost twice as high among the unemployed. Among pensioners it was 21% and twice that level among one-person pensioner households. Social transfers and pensions sustain many people above the poverty threshold which, measured before such transfers, was as high as 42%.

**PENSION REFORMS**

As shown in the previous section, even though the region has experienced rapid growth in recent years, social problems remain deep as a result of the years of stalled transition and extended conflict. Labour market outcomes are particularly problematic with high levels of unemployment, low participation rates, and large informal

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economies (Bartlett 2007a). Participation rates have fallen as many of the workers laid off from old socially-owned and state-owned enterprises, especially women and older people, dropped out of the labour market. Early retirement was widely used to reduce employment levels of over-staffed enterprises. Informal economic activity is widespread. Many employers avoid paying social insurance contributions, depriving governments of resources for social programmes and putting pay-as-you-go pension systems under strain.

Pensions are the largest item of social protection expenditure throughout the region due to both demographic change and to the widespread practice of early retirement that has accompanied privatization and enterprise restructuring. Although the demographic dependency ratio does not vary much (the range is 45-55%), the ratio of children to the elderly differs widely, from 3.4 in Albania and 3.0 in Montenegro, to 2.0 in Macedonia and around 1.0 in Croatia and 0.9 in Serbia (ILO 2005: 15). Pension system dependency ratios are also unfavourable ranging from 1.78 contributors for each pensioner in Montenegro to as low as 0.74 in Republika Srpska (ILO 2005: 69). This raises the question of the sustainability of pensions in the light of demographic prospects in the latter countries. Only Albania, Kosovo and Montenegro have demographically youthful populations, although due to the low employment rates and high levels of informality in the economy, the funding of pensions is problematic in those countries also. The ratio between pensioners and employees is unfavourable in most countries, and is especially low in Republika Srpska where there are more pensioners than active pension scheme contributors.

Furthermore, the pension systems are under severe strain due to low employment rates and a poor record of contribution collection. High contribution rates, typically

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13 By 2004, participation rates ranged from 46% in Kosovo to 68% in Serbia compared to over 70% in the EU-15, the relatively high participation rate in Serbia being due only to its delayed transition. Albania also has a relatively high participation rate due to massive out-migration of active workers in search of work abroad (ETF, 2006).

14 Recent estimates indicate that Albania has the highest share of informal economic activity with 52% of household income being undeclared, while Kosovo and Macedonia also have a high share at 45% and 39% respectively (Christie and Holzner, 2004).
above 20% of gross wages, have stimulated the growth of the informal economy, while even companies in the formal economy often fail to pay contributions on behalf of their employees, or pay with a delay, so that many employees have gaps in their pension contribution record. Kosovo is an exception since the basic pension is paid from general taxation, and only the fully funded pension pillar is paid through payroll contributions. Due to failures in collecting contributions, most state pension funds have deficits which must be supplemented by governments’ already stretched budgets, reducing resources for other items of social expenditure. Pressure on government budgets has been especially severe in Croatia, Montenegro and Serbia where pension expenditures account for a relatively high share of GDP (see Table 2).

Table 2: Pension benefits and expenditures, 2004

<table>
<thead>
<tr>
<th></th>
<th>Average monthly pensions (€)</th>
<th>Replacement rate (%) (a)</th>
<th>Pension/poverty line (d)</th>
<th>Pension contribution rates (%) (e)</th>
<th>Share of pension expenditure in GDP (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Albania</td>
<td>50</td>
<td>33.0</td>
<td>132</td>
<td>29.9</td>
<td>5.0</td>
</tr>
<tr>
<td>BiH</td>
<td>100</td>
<td>-</td>
<td>-</td>
<td>24.0</td>
<td>-</td>
</tr>
<tr>
<td>Croatia</td>
<td>257</td>
<td>34.0</td>
<td>122</td>
<td>20.0</td>
<td>14.0</td>
</tr>
<tr>
<td>Macedonia</td>
<td>-</td>
<td>42.0</td>
<td>56</td>
<td>21.2</td>
<td>9.0</td>
</tr>
<tr>
<td>Montenegro</td>
<td>90</td>
<td>51.0</td>
<td>-</td>
<td>24.0</td>
<td>17.0</td>
</tr>
<tr>
<td>Serbia</td>
<td>124</td>
<td>61.0</td>
<td>193</td>
<td>22.0</td>
<td>12.0</td>
</tr>
<tr>
<td>Kosovo</td>
<td>40</td>
<td>-</td>
<td>-</td>
<td>10.0</td>
<td>-</td>
</tr>
</tbody>
</table>

Source: ILO (2005); Statistical Yearbook of Serbia (2007); Croatian Office for Pension Insurance online data; Kosovo Pension Savings Trust online data.

Notes: (a) average replacement rate to gross wages, (b) average replacement rate of newly awarded pensions to gross wages, (c) replacement rate of guaranteed minimum to average gross wages, (d) average pension to official poverty line, (e) pension contribution rates in relation to gross wages.

As a consequence of the limited financing ability of the government run pension funds, pensions in all the Western Balkan countries are low in relation to subsistence needs, with minimum pensions around one fifth of average gross wages in each country. The average replacement rate of pensions has decreased over time in most of the countries, and ranges from a low of 33% in Albania to a high of 61% in Serbia (see Table 2). The ratio of the average pension to the official or semi-official poverty
line is lowest in Macedonia where pensioners are least effectively protected from poverty.

In response to these difficulties in financing the growing cost of pension expenditures, several countries in the region have introduced pension system reforms, which have however varied widely in their scope\textsuperscript{15}. Pro-market reforms have been introduced in Croatia and Macedonia. In these countries, the inherited universal systems of pensions have been partly transformed into selective systems in which the redistributive element that was predominant in the previous regime has been replaced by a contributive principle which no longer guarantees a specific level of income in old age. They are based on a diminished ‘first pillar’ state pension element, and the introduction of a ‘second pillar’ fully funded private pension element, and a ‘third pillar’ additional private voluntary fund. Such three pillar pension schemes have been introduced as part of a wider global movement towards privatisation of pension systems which, as in several cases in Eastern Europe, has followed the prescriptions of the neoliberal agenda promoted by major global policy actors (Orenstein 2005). A similar pension system was created in the UNMIK administered province of Kosovo in 2002. In contrast, limited reforms to the pay-as-you-go state pension system which fall short of radical privatisation have been introduced in Serbia and Montenegro. In BiH the reform effort has focused on harmonisation of the provisions of the pay-as-you-go system between the two entities, FBiH and Republika Srpska. In the Albanian system the redistributive elements are still strong, and provide the minimum standards of living for low-income pensioners.

\textsuperscript{15} These reforms are fast moving as the region is passing through a period of large scale institutional change related to transition, post-conflict reconstruction, and EU accession challenges. While we have made every attempt to monitor the reforms to pension systems, we are well aware that there may be changes taking place as we write which are not adequately covered in the present text. However, we hope that we have presented an accurate account of the most recent developments, and have placed them in a sufficiently developed historical context and theoretical framework that will enable readers to assess future developments in a more informed perspective.
**Privatised pension schemes**

*Croatia*

During the 1990s the Croatian pension system entered into a severe crisis due to a sharp increase in the number of pensioners which by 2000 reached more than a quarter of the entire population and caused increased deficits in the state pension fund (Bartlett, 2003). In an attempt to grapple with the problem the government restricted increases in pension payments between 1993 and 1997 to the rate of price inflation.\(^\text{16}\) Reforms to the state pension system were introduced through the Pension Insurance Act of 1998 under which the parameters of the defined-benefit first pillar of the pension system were revised, increasing the pension age to 60 for women and 65 for men. The Law on Compulsory and Voluntary Pension Funds of 1999 established a private pension system which consisted of a mandatory fully-funded defined-contribution ‘second pillar’, and a ‘third pillar’ based upon private addition voluntary contributions. The Croatian decision to adopt a three pillar pension model with a strong private component was at least partly a reaction to the crisis in funding the state run pension system in the 1990s, and the acceptance by the Tudjman government of the recommendations of international organisations and policy advisors promoting that specific policy option. In particular, Chilean advisors played a role in shaping the specific form of policy transfer that took place through the offices of the East-West Institute and the World Bank (Orenstein 2005).

The new pension system was implemented in 2002 (Anusić et al., 2003). Employees who were less than forty years of age when the scheme was introduced were required to select one of the four pension funds which had been established. These employees were required to pay 5% of their gross wages into the second pillar pension funds, while continuing to pay a contribution of 14.5% into the first pillar state pension scheme managed by the Croatian Pension Insurance Fund (HZMO). Individual contributions to the second pillar funds are collected by the Central Agency of Insured Persons (REGOS), which also keeps individuals’ records. Employees over 50 continued to pay contributions of 19.5% into the state pension fund, while those aged

\(^{16}\) The ‘pensioner debt’ of the 10% of the population who were affected by the 1990s pension freeze is being gradually repaid from a special fund established in 2005.
between 40 and 50 were permitted to choose whether to enter the new partially privatised scheme. The third pillar comprises additional voluntary contributions. The private pension system is supervised by the Croatian Financial services Supervisory Agency (HANFA).^{17}

Almost one million employees joined the four private pension funds in the second pillar scheme when it was launched in 2002, and the numbers have increased by around 100,000 each year to reach 1.4 million members by the end of 2007. Only 21% had chosen a pension fund on their own, with the remaining employees being allocated to one of the four pension funds by REGOS. The size of the privately managed funds reached HRK 20 billion (€3 billion) by the end of 2007, equivalent to HRK 14,000 per member (€2,000). The small size of the Croatian capital market and the oligopoly structure of the pension fund market have enabled the private pension funds to high fees and has led to an ‘institutional degeneration’ of the private pillar (Guardiancich 2007). The second pillar pension funds charge 0.8% entry fees and, since 2003, 1.2% management fees. Dobronogov and Murthi (2005) demonstrate that such fees may significantly reduce the returns to investment for scheme members, and suggest that pension funds are overcharging for the services that they provide. Their estimates show that charges may lower an individual’s future pension capital by 22% and reduce returns by 1.25%. The fixed costs of running the schemes further reduce their effective performance, especially in small schemes and where the wage base for contributions is low. High fixed costs and low levels of contributions reduce the returns to the pension funds, and imply that they might have lower returns that those implied for state managed funds in the first pillar which have lower administrative costs and a larger client base.

**Macedonia**

The Macedonian pension reform law passed in 2002, supported by a $9.8 million World Bank loan, envisaged a three pillar pension system similar to the Croatian system.^{18} The new pension insurance system combines both pay-as-you-go and the

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^{17} Until the end of 2005 the system had been supervised by the Pension Funds and Insurance Supervisory Agency (HAGENA).

^{18} The Law on Mandatory Fully Funded Pension Insurance was approved in April 2002.
fully funded methods of financing pension schemes. It consists of three pillars. The first is a compulsory pension insurance based on pay-as-you-go model. The second pillar is designed as fully funded pension insurance. It is compulsory for individuals who took up work for the first time since January 2003 and for all new entrants to the labour market. The two compulsory pillars therefore cover all the economically active population with some special provisions for those employed in military service and ex-persecuted people. The third pillar is a voluntary fully funded pension insurance for contributors employed before January 2003. Pensioners above 65 years old are guaranteed a minimum pension when they retire, which is subsidized from the state budget if the insured person does not reach it from their employment.

The contribution rate for the state managed pension scheme is 21.2% of the gross salary for contributors who have remained in the mono-pillar system. The contributions are paid by the employer and are administered by the Pension Fund. Those who choose, or by law, belong to the two pillar system contribute 13.78% of gross salary to the first pillar state fund, and 7.42% of gross salary to a private pension fund, maintaining the same overall percentage as before. The reform of the first pillar has also involved a gradual increase in the retirement age, a decrease in the replacement rate, a change in the pension indexation method, the ending of early retirement, and a change of the pension formula. The retirement age is 64 years for male contributors and 62 years for female contributors, with a minimum insurance period of 15 years. The reduced contributions to the first pillar are expected to provide only a modest pension with an estimated replacement rate of 30%, supplemented by the pension derived from the investments in the second pillar private pension funds.

Within the second pillar, contributions for compulsory fully-funded pension insurance are invested in two new private pension funds established in April 2005, both of which are majority owned by Slovenian banks\(^{19}\). The system is supervised by the Agency

\(^{19}\) The pension company *Akcionersko drustvo za upravovanje so penziski fondovi NOV PENZISKI FOND*, Skopje manages the *NOV PENZISKI FOND*. The company was founded by the *Nova Ljubljanska banka* with 51% of the capital, and the *Tutunska Banka AD, Skopje*, which owns 49% of the capital. The pension company *KB Prvo drustvo za upravovanje so penziski fondovi AS Skopje*
for Supervision of Fully Funded Pension Insurance. By September 2007 the two second pillar private pension funds together had 90,000 participants, a very small number compared to the 1.4 million members of the four Croatian pension funds. Being relatively recently established their net assets amounted to just 2.6 billion denars (€42 million) in 2007, equivalent to €466 per member\(^\text{20}\). By design, the returns to these investments are not guaranteed, and depend upon the performance of the funds.

Given the underdeveloped state of the Macedonian capital market this is a high-risk strategy since there are few financial institutions in the country that could manage a large investment fund, and even fewer high-yielding investment opportunities in which the accumulated contributions could be placed. Regulation of the funds is tight with a maximum of 30% allowed in equities and 20% on foreign investments, so that a large part of the funds are invested in government bonds. Moreover the fees and charges imposed by the private pension funds are relatively high, with an entry fee of 7.9% compared to less than 1% charged by the Croatian funds\(^\text{21}\). Management fees are also relatively high at 0.05% per month (equivalent to an annual fee of 0.6%). Given the high fees and the relatively small size of the Macedonian funds, it seems unlikely that they will provide an eventual pension to the participants that would be greater than they would have received under a state managed system. One simulation study of the Macedonian pension system has estimated substantially lower returns to the pension fund members compared even to the Croatian system, due to a combination of high entry fees and passive fund management (CRPM 2007). An independent assessment carried out on behalf of the World Bank has raised concerns about the introduction of the privately managed second pillar pension scheme in Macedonia, on the grounds that the projections for future pensions made in designing the scheme were overly optimistic (Fornero and Ferreira 2007).


\(^{21}\) Prior to 1 July 2007 the entry fee was 8.5%.
**UNMIK-Kosovo**

Pension reform was the subject of the first law approved by the first post-war Kosovan parliament that was elected in July 2002. Kosovo has a favourable ratio between the working age population and pensioners, but there is an unfavourable ratio between pension contributors and pensioners because of the high rate of unemployment estimated at about 50%. Although the share of those older than 65 years old in the overall population is relatively low at 6%, future demographic change will place increased pressure on the pension system.

The World Bank and USAID have assisted the provisional Kosovo government in setting up a three pillar pension system. The first pillar is a publicly-managed non-contributory scheme and provides a flat rate pension of €40 to all citizens aged over 65, financed out of the government budget. This basic pension scheme is administered by the Pension Administration, which is under the authority of the Ministry of Labour and Social Welfare. In Kosovo the flat-rate pension guarantees a minimum standard of living for all elderly people financed out of the state budget.

The second pillar is based on workers individual pension accounts administered by the Kosovo Pension Saving Trust. It is a defined-contribution scheme, fully funded through a 5% payroll contribution on gross wages. The collection of contributions is carried out by the Tax Administration through the banking system. The new pension system was introduced in August 2002 for public sector employees of government and workers in socially-owned enterprises, and was extended to all workers in 2003. As a funded system, the savings in individual accounts are invested. The third pillar consists of six small occupational schemes based on the contributions of individuals.

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22 This pension was introduced because the contribution records of many Kosovar workers had been lost during the 1999 conflict, apparently due to the destruction of the pension records office by NATO bombing.

23 Opened in August 2002 for employees of government, state and socially-owned enterprises, this was become mandatory for all workers in 2003. The Border of Governing the Kosovo Pension Saving Trust has 7 members, 4 professionals, 1 representative of the Employers, (Chamber of Commerce), 1 representative of the Employees, (Union of the Independent Trade Unions), and 1 from UNMIK.

24 Employees may opt to increase their contribution rate to 15%

25 The collection of contributions started on August 2002 and all the funds have been invested abroad since March 2003.
and employers to provide their employees with an individual supplementary pension. They are licensed and supervised by the Banking and Payments Authority of Kosovo and may eventually be extended to form a comprehensive voluntary pillar of the pension system.

The private, second pillar pension fund is administered by the Kosovo Pensions Savings Trust (KPST). It began to collect contributions in August 2002. Unlike the funds in Croatia and Macedonia there are no entry charges, which are met by a subsidy from the Kosovan government. There is a 1% annual management fee\(^\text{26}\), even lower than the 1.2% charged in Croatia. Also, unlike the Macedonian scheme which restricts international investments to 20% of the total funds, the KPST has placed the entire scheme consisting of members’ individual savings accounts outside Kosovo, in mutual investment funds managed by a number of foreign banks\(^\text{27}\). By September 2007 the total amount invested on behalf of 232,000 active members had reached €262 million, equivalent to €1,130 per person\(^\text{28}\). In the early stage of the scheme the funds were invested in money market funds with ABN AMRO in the Netherlands. In subsequent years these have been diversified into indexed equity funds managed by Vanguard Investments based in Brussels, and in 2006 into actively managed fixed income funds managed by Schroders and ECM (Gubbels et al., 2007). By 2006, as much as 60% of the fund was placed in risky equities. This strategy has been criticised for failing to provide for investment in the Kosovo economy, but the KPST has argued that the level of risk is lower in international funds than inside Kosovo, where capital markets are underdeveloped. There can be little doubt that investment within Kosovo is also risky, as emphasised by the closure of one of the supplementary third pillar pension providers in November 2007.\(^\text{29}\) However, it remains to be seen whether the strategy of investing the entire fund outside Kosovo will pay off in the long run, given the potential for financial instability on globalised capital markets. The alternative strategy, reinvestment of assets in the Kosovo economy, would

\(^{26}\) The asset management fee was reduced to 0.9% in 2008.
\(^{27}\) These are the ABN-AMRO bank and the Vanguard investment fund.
\(^{29}\) The Central Banking Authority of Kosovo revoked the licence of the Supplementary Individual Pension provider ACP SPPT AK because the fund failed to comply with the CBAK licensing criteria (CBAK website, accessed 15/12/2007).
provide a much needed stimulus to growth, and would furthermore avoid the capital outflow involved in transmitting a significant proportion of Kosovan GDP abroad each month.

Reforms to state pension systems

Albania

In 1993 the social insurance system was reformed on the lines of social insurance principles replacing the previous universal state-funded system. The Albanian pension system is based on the Bismarck model, in which the level of the old-age pension is based on wage-related contributions. Since many people work in the informal economy and the unemployment rate is high, there is a danger that many elderly people will not be covered with a basic pension in the future. The low participation of the active population in the scheme reflects the low level of the pension, and the high rate of contributions for social insurance. Since employers have weak incentives to pay contributions, the government is required to subsidise the pension fund to provide a minimum level of support for pensioners. Although the rate of economic growth relatively high at 5-6% per annum, expenditure on social security is low, both in total and as a percentage of the GDP. In 2005, about 60 % of the social expenditures were allocated to pensions, and 87% of the expenditure of the Social Insurance Institute was used to support pensions. Although their level is considered low, more than 90% of pensions were at the minimum level.

The compulsory basic pay-as-you go pension system is supplemented by public supplementary insurance schemes which cover civil servants and military personnel, governed by the Social Insurance Institute under separate laws. All these schemes are based on the contributions of the economically active population, employees, employers and the state, using a pay-as-you-go model. The level of the pension (old-age, disability, survivors) is linked to the age of retirement and to individual contributions. The retirement age is being gradually increased from 55-60 years for females and from 60-65 years for males by 2024. Pensions consist of a basic pension and a wage-related component of one per cent for each year in the contribution

30 The compulsory insurance preserves all the rights of the former pension system.
period. The basic pension is set at the minimum living standard, while the maximum pension is equal to twice the basic pension. The pension system retains a strong element of redistribution, even the presence of the contributive principle on which it is based. An additional voluntary pension scheme\(^{31}\) has been established to give employers and self-employed people the right to apply for a higher pension, to enable insured persons to continue insurance contributions in the case of a temporary interruption of employment, and to enable Albanian citizens working abroad to continue their insurance contributions. Employers and self-employed people pay only a minimal contribution, corresponding to a pension of 75% of the minimum wage.

The Social Insurance Institute, a semi-public body\(^{32}\) is responsible for social insurance system administration.\(^{33}\) Social assistance, established at the same time, supports certain categories of people whom the social insurance system could not support. Social assistance is a means-tested system, based on need assessment and the level of financial resources of the central state budget. It is administered by the local authorities. Private pension schemes, seen as an alternative way of dealing with low incomes in old age at no cost to the government, were introduced in 2005.

The Albanian social security system is highly centralized. The different schemes are unified in a single social insurance system for all the economically active population, although there are some differences for employees, self-employed people and for self-employed in agriculture. However, its implementation is distorted by the widespread of informal economy. A major difficulty has been the inclusion of the rural population which covers more than half of the Albanian population\(^{34}\). A recent study by the Social Insurance Institute\(^{35}\) demonstrated that while their contribution to the economy

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\(^{31}\) The Public Voluntary Social Insurance scheme.

\(^{32}\) The Administrative Council, as the leading decision making body of Social Insurance Institute, composed of 1/2 of the members nominated by the Council of Ministers as representatives of the Government, ¼ of the members representatives of the employers organizations and ¼ representatives of the employees. The nomination is valid for no more than five years.

\(^{33}\) Actually the supplementary pensions are governed under separate laws for the civil servants and the military personnel.

\(^{34}\) There are 542,000 self-employed in agriculture out of a total of 931,000 people in employment.

has increased, their share in the solidarity funds of social and health insurance has been problematic. While employees in the non-agricultural private sector comprise 16.7% of contributors and provide 21.5% of the total contributions for social and health insurance, the self-employed in agriculture comprise 57.5% of contributors but provide only 4.3% of the total amount of contributions.

The priority issues for the further development the social insurance system are (i) to reduce the evasion of contributions, (ii) to increase the real level of benefits and the quality of services; (iii) to increase the involvement of the rural population in the contribution scheme; (iv) to extend social insurance to people employed abroad; and (v) and to carry out legislative adjustments to EU standards. The introduction of a second pillar is also a strategic priority of the government for 2007-13, even though there is little consensus on this issue.

**BiH**

In BiH, the traditional pay-as-you-go pensions are the responsibility of the entity governments, and reforms have focused on the harmonization of the two separate systems. Many disabled pensioners in BiH receive enhanced pension and invalidity insurance benefits. However, the system for assessing disability is inconsistent across the various administrative units (entities and cantons) and is open to abuse, including the practice of making informal payments to doctors to register healthy individuals as disabled. In the Federation of BiH (FBiH, the Muslim-Croat federation) the fragmented pension system was consolidated at the federal level in 2001, with the creation of a unified Federation Pension and Invalidity Fund. In the Serb administrative entity (RS, Republika Srpska) the pension system also faces difficulties, since many companies avoid paying pension contributions on behalf of their employees. In an attempt to resolve the situation the Office of the High

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36 However, this has not been very successful and an agreement on the transfer of acquired pension rights has not been observed, with the consequence that in 2004 Republika Srpska was paying the pensions of 20,000 people who acquired their pension rights in FBiH.

37 About 10% of the working population suffers from a disability.

38 The authorities had lost control of the central database of social contributions as a result of an allegedly illegal privatization in 1999, and the pension fund had to purchase its own data back from the database owner.
Representative (representing the Peace Implementation Council responsible for implementing the 1995 Dayton Peace Agreement) passed a regulation that pensions should be calculated in accordance with the capacity of the Pension Funds, rather than by established entitlements. This had the unintended consequence that, since the Republika Srpska pension fund only needs to distribute as much as it collects, it has had little incentive to enforce payment from recalcitrant employers, and has therefore failed to enforce the collection of debts through the courts. Moreover, the government has not pressured the Fund to enforce the rules, arguing that employers cannot afford to make the required payments. Due to the consequent deficit, pensions are often paid at a reduced rate, while the Pension Fund has come under criticism for its inefficient practices including the construction of luxurious offices and the padding of employees’ remuneration. As yet however, due to the unfinished process of reform, and the weak political and administrative capacity of the central government of BiH, the pension system has not been the focus of reform efforts. BiH is among the least prepared for further EU integration among all the Western Balkan countries. Although the design of pension systems are not subject to EU authority, it is likely that significant reform of the pension system in BiH will only begin when the country is more established on the path to EU integration, for example by signing a Stabilisation and Association Agreement which at present is blocked by political instability and reluctance of the ruling elites to comply with EU conditionality.

**Serbia**

Serbia retains the inherited single pillar system. The Serbian government decided against introducing a private pension reform, and has concentrated instead on the reform of the compulsory pay-as-you-go system. The Serbian pension system is split among three different funds, for employees, farmers, and the self-employed, of which only the fund for the self-employed is solvent. In recent years, the state pension fund for employees has had a deficit equivalent to about 5% of GDP, mainly because less than three-fifths of the labour force makes regular pension contributions. The farmers’ fund has also relied on transfers from the government budget. Reforms to the state

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39 The BiH Stabilisation and Association Agreement was initialled at the end of 2007, but its signature and ratification remains blocked over the controversial issue of police reform, which the Republika Srpska is unwilling to countenance.
The pension system were introduced through the Pension Law adopted in 2004. The law increased the retirement age from 60 to 63 for men and from 55 to 58 for women; changed the indexation base from wage inflation alone to an average of wage and price inflation; and fixed the minimum pension at 20% of the average wage.

**Montenegro**

In Montenegro a new pension law has envisaged the introduction of a three pillar pension system, although its introduction has been delayed due to the weakness of the pension system administration. Therefore, for the time being, the state managed pay-as-you-go pension system remains in place. The strengthening of its administrative capacity has been supported by a $5 million World Bank credit designed to build the capacity of the existing pension fund administration.

**CONCLUSIONS**

Following two decades of transition, conflict, and varying degrees of progress with EU accession and integration, the Western Balkan countries have been converging on rather different welfare models. Albania, Macedonia and Kosovo have relatively low levels of social security and social protection expenditure overall, having followed a liberal economic policy under the influence of the IMF, involving meaningful reductions in government budget deficits. In contrast, Croatia, BiH, Montenegro, and Serbia have followed a more traditional corporatist model with relatively high shares of public expenditure as a proportion of GDP (Bartlett 2008). Given the relatively low levels of development of these countries, it is not surprising that expenditure on social protection as a proportion of GDP is everywhere below the average in the EU-25. This picture is also reflected in respective shares of public expenditure on pensions. It is tempting to classify these two groups of countries into the conventional models of welfare states analysed by authors such as Esping Anderson (1990) and varieties of capitalism analysed by Amable (2003). For example, it would not be unreasonable to classify the former group of countries as liberal market economies, and the latter as more akin to corporatist Central European type of capitalist economies, as in Bartlett (2007c). However, any such classification is inevitably provisional, as by the nature of transition, post-conflict reconstruction, and EU accession processes, these economies and social systems are evolving quite rapidly over time. The main reason
why the former group have followed a more liberal market path has been the weakness of their central governments, the prevalence of the informal economies, and the extremely high rates of unemployment, and emigration in the case of Albania, which have eroded their tax bases. The latter group of countries also has significant deviations from the corporatist type model, taking account of the slow pace of economic reform and enterprise privatisation in Montenegro and Serbia, and the prevalence of the informal economy in BiH.

In addition, the proposed model types do not fully map into pension reforms. While Macedonia and Kosovo have adopted pro-market pension reforms, Albania has retained a state managed pay-as-you-go pension system. A possible explanation for the Albanian exception is its insufficiently developed capital market, and an unwillingness to adopt the risky Kosovo-style option of investing pension funds abroad. Among the corporatist-model states, while BiH, Montenegro, and Serbia have been content to maintain a reformed state pension system, Croatia has introduced pro-market pension reforms. The Croatian decision to adopt a three pillar pension model with a strong private component can be partly explained as a reaction to the crisis in funding the state run pension system in the post-conflict 1990s, the policy choices of the right-wing pro-market Tudjman government, and the influence of international organisations and advisors promoting that policy option. This is a similar set of factors to those which Müller (2002b) relied on to explain the adoption of pro-market pension reforms in Hungary and Poland, contrasting their experience with the Czech Republic and Slovenia. In particular, the discussion here mirrors Müller’s conclusion that the impact of economic factors on pension reform choices should be contextualised, and placed in the perspective of the influence of different transnational and domestic advocacy coalitions and interest groups.

The diversity of pension systems in the region has created problems of coordination between the different schemes in cases where individuals live and work in different countries. For example, Kosovars who are working in Albania and have a residence in Kosovo can benefit from a basic residential pension in Kosovo and a contributive pension in Albania. At the same time, they may easily avoid payment of contributions in Albania because they have a guaranteed basic pension in Kosovo which is approximately twice the basic contributive pension of the Albanian self-employed
In an attempt to address this issue of transnational policy coordination, the Stability Pact established the Initiative on Social Cohesion (ISC) which has promoted social policy coordination in various fields including employment, health, housing, and social protection. The ISC, supported by the Council of Europe and the ILO, has also been active in implementing the EU accession agenda. Since most Western Balkan countries are preparing for EU accession, initiatives have been introduced which address the regional compatibility of pension systems within the framework of the ISC. For example, the Council of Europe has initiated a regional project on social security cooperation and has sponsored the activities of a Social Security Coordination Network in South East Europe. In cooperation with the ILO it has recently carried out some training programs on techniques of social security coordination. The European Commission has funded a CARDS project, with the support of the Council of Europe, on Social Institutions Support designed to strengthen the legislative framework and policy making process for social protection policies, and to improve the coordination of social security systems in the region.

In addition to the typological issue of classifying countries into different model clusters, and the analysis of the influences, internal and external, on the design of pension reforms and system coordination, there is also the more important policy issue of the effectiveness of different types of pension reforms. As the country case studies have demonstrated, countries which have adopted three pillar systems have done so in the context of weak capital markets, oligopolistic competition among pension funds, consequently high levels of fees and charges, and relatively small sized private pension fund memberships. In such circumstances it is questionable whether the three pillar schemes will be able to achieve their objectives of providing better outcomes than state managed pay-as-you-go schemes. The main purpose in some cases appears to have been to take pension expenditure off the state balance sheet as
part of the macroeconomic policy to reduce budget deficits. Even the World Bank, a long-standing proponent of the pro-market reforms to pension systems, appears to be having some doubts about their effectiveness. A recent World Bank report has extolled the benefits of parametric reforms to state managed pay-as-you-go pension schemes (Chawla et al. 2007). It argues that, even in the context of worsening demographics, reforms which increase retirement ages and index pensions to prices rather than wages can offer long term solutions to the problems of financing basic incomes for the elderly based on the principle of intergenerational solidarity. Given the risks inherent to the three pillar pension systems which have already been introduced in the region, countries which have not yet introduced such schemes - Albania, BiH, Montenegro, and Serbia - may be well advised to pursue further reform cautiously, and focus on improving the effectiveness of existing state managed pay-as-you-go pension systems, rather than rushing headlong into the partially privatised systems adopted by early reformers elsewhere in the region.
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