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ROLE OF INVESTMENT ON SOCIAL SECURITY AND ECONOMIC INEQUALITY

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Abstract
Social security is one of the important factors to achieve societal progress and there by achieve sustainable economic growth. One of the important measures of social security is to provide income security to individuals and households. There is a strong need for investing in systems that protect people from income insecurities. The adverse effects of income insecurity are more prominent where the income inequality exists. In each period, each person gets a different draw, of earnings or of asset returns, so that whenever differences cumulate over time, the members of any group will draw further apart from one another, and inequality will grow. Inequality at a moment of time is the fossilized record of the history of personal differences in risky outcomes. Income inequality and its economic effects have become a matter of generalized concern. Hence investment on social security is one of the ways in which economic inequality can be alleviated or reduced. Investments on social security should be made with a view to achieving a reasonable balance between security and profitability objectives. A subsidiary objective of the investment is the social and economic utility with an objective to contribute to long-term national economic growth. Investments shall be managed in a cost-effective manner and invested in such a way as to exclude any loss, achieve a reasonable return and ensure adequate liquidity.
This paper studies the relation between investment pattern in social security and its role in bringing down economic inequality. Wealth or income inequality has a negative impact on economic growth. However, little is known about the exact mechanisms that drive these detrimental effects and in which specific circumstances these effects materialize. Indeed, inequality can affect economic growth through a number of different channels, such as social unrest, redistribution or aggregate saving and investment. By investing on social security measures this paper suggests that income inequality can be reduced and there by society can achieve a better economic growth.

Keywords: Social Security, Economic Inequality, Investment Models, Economic Growth, Income insecurity, Sustainable Growth.

1. Introduction

Social security is an internationally recognized need of basic right and it plays an important role in raising living standards and supporting social and economic growth. By investing in social security not only improves the individual living standards but also it improves the broader economy; it can trigger various economic cycle that increases tax revenues, productivity, employability and overall economic growth. In general, the investments in social security generate positive returns in terms of overall economic growth. There is a strong reason for investing in systems that protect people from income securities. Existing literature shows that various positive impacts on social security investment programs such as income support programs (J. Ana, 2024). The effect of positive economy due to social security has been mentioned in (Stephen et al., 2022; David et al. 2009). Economic growth is not a core policy objective of social security, but by providing income security across different lifecycle risks, social security promotes economic growth through different channels as shown in Fig. 1.

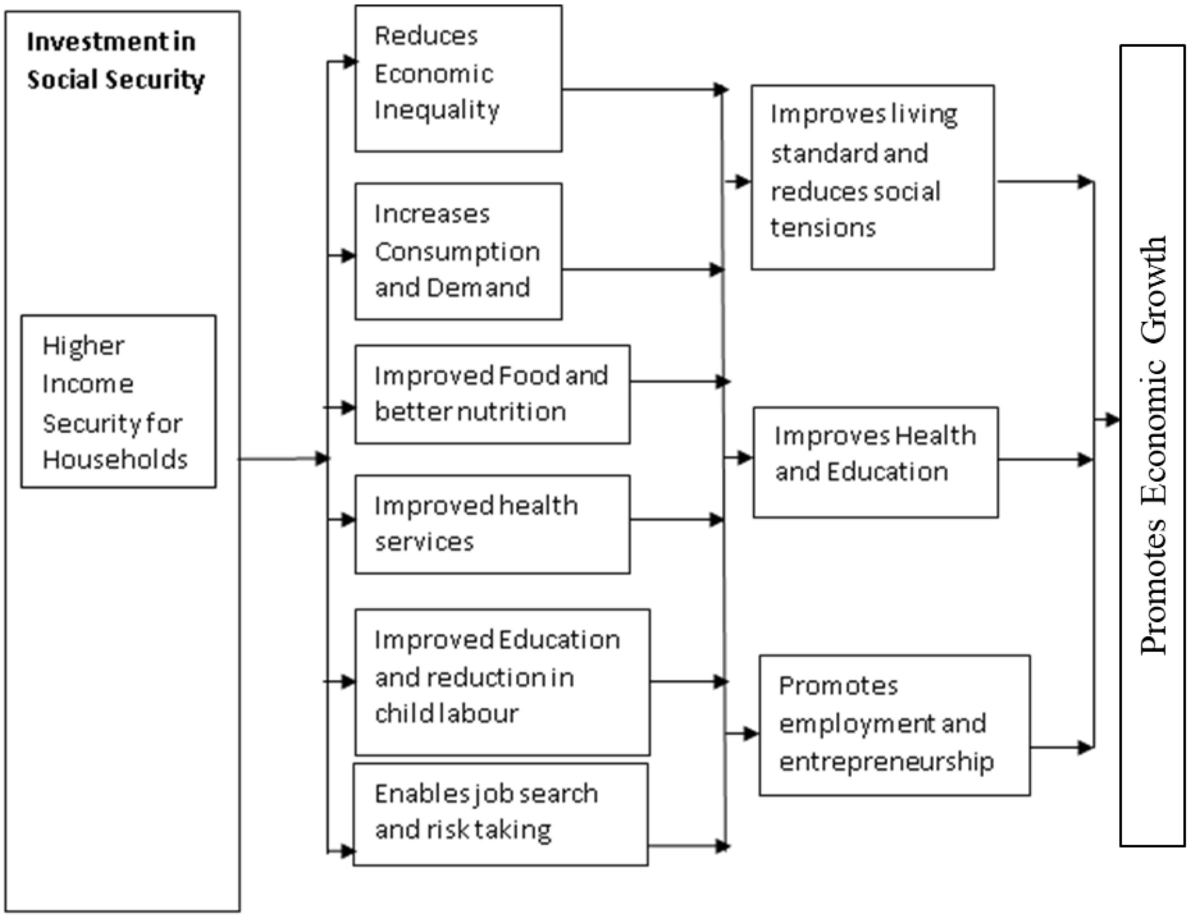

Figure 1 Investment in Social Security Promotes Economic Growth

Social security schemes that are consistent, reliable and that are of a sufficient amount allow households to invest more consistently in members' nutrition, education and health as shown in Fig.1. The ability to improve on health and education also means that households can better mitigate shocks over time. This lessens the need for households or individuals to engage in negative coping strategies, such as withdrawing children from school to provide additional income, consuming less nutritious (usually expensive) foods or the selling of productive assets. Thus, an investment in social protection is an investment in a country's human capital development and productivity, which in turn improves the employability and productivity of a country's future workforce and investments in other key sectors. It may also allow more individuals to enter the labor force or take more innovative business risks instead of relying on less secure but immediately available subsistence activities. All of these lead to more inclusive economic growth as shown as the end result in Fig.1.

In the same way, social security schemes can help prevent individuals from losing income due to shocks such as unemployment, the birth of a child or the death of an income earner. Unemployment benefits in particular allow individuals who are out of employment – and for whom it would have been costly to look for secure wage employment for longer – to look for such employment by minimizing the loss of income. Similarly, maternity benefits provide guarantees that allow women to return to the labor market after having a child whilst also minimizing the loss of household income associated with childbirth and the first few months of a child's life (David et al, 2009). In the case of the latter social protection scheme, we would also expect wider societal benefits of improved female employment and ultimately a reduction in gender income gaps as fewer women have to forgo their lifetime income as a result of not having to exit the labor market.

Other society-wide benefits result from the spillover effects in the form of better social cohesion. Better social unity can arise from people feeling more included as economically contributing members. This is especially the case for elderly members of the community who, without access to a minimum income, would otherwise rely on other family members who may also struggle with their own and dependent children's financial security. On a wider scale, social security can also reduce the level of inequality nationally and thus further entrench a more stable society, particularly given that inequality serves to undermine social structures.

Through a demand stimulus, social security can ultimately increase national economic activity through the multiplier effect, where the initial increase in household consumption expenditure results in an increase in demand for local goods and services which in turn results in increased local production and changes in the local labor markets. We would expect positive effects on the local community and markets. Such aggregate changes to household productivity ultimately have an effect on aggregate demand, especially when a country is able to engage in counter-cyclical spending during macro-level shocks, such as economic downturns, leading to a increased employment and thus government revenue through taxes.

The aggregation of the various individual and household level effects can serve to reduce income inequality at the macro level by alleviating opportunity inequality and allowing households to cope with adverse shocks better (Peter et al., 2016). A reduction in inequality can in turn lead to better social cohesion and stability, continued developments in human capital and ultimately economic growth.

2. Methods to tackle Economic Inequality and its Measure

Social security has become recognized as both a basic right and a key tool through which countries can tackle inequality and create better societies for everyone. Inequality has been tackled in general using pre-distributive and redistributive policies. Pre-distribution incorporates the provision of public services such as health and education, as well as active labor market policies, such as minimum wage legislation. These policies encourage inclusive growth by enhancing opportunities and increasing human capital while also supporting fair labor market participation. Redistribution encompasses both taxes and transfers – in other words, investment in social security – which not only transfer wealth from the rich to most of society but, by doing so, further strengthen human capital and help generate economic growth. Redistribution, in effect, reduces the inequality of disposable income through taxes and transfers while enhancing opportunities for families and individuals through demand side investments.

The reduction in inequality achieved by social security is the result of both the transfers themselves, which offer households additional income, alongside the taxation that funds the transfers. The redistribution should reduce the incomes of the wealthier members of society while increasing incomes across the majority, thereby tackling inequality.

Inequality can be measured in many ways, most often using income by an individual, household or society. The Gini coefficient is the most well-known indicator of inequality (Anjali Bhatt et. Al., 2020). The Gini coefficient is a measure of how equally income is distributed across the population, with 0 being perfectly equal (where everyone receives an equal share) and 1 being completely unequal (where 100 percent of income goes to only one person). To understand what it captures, it is useful to refer to a graphic representation of inequality, the Lorenz curve. Individuals are ranked from poorest to richest, with the cumulative percentage of the population represented on the horizontal axis and the cumulative percentage of income on the vertical axis as shown in Fig. 2.

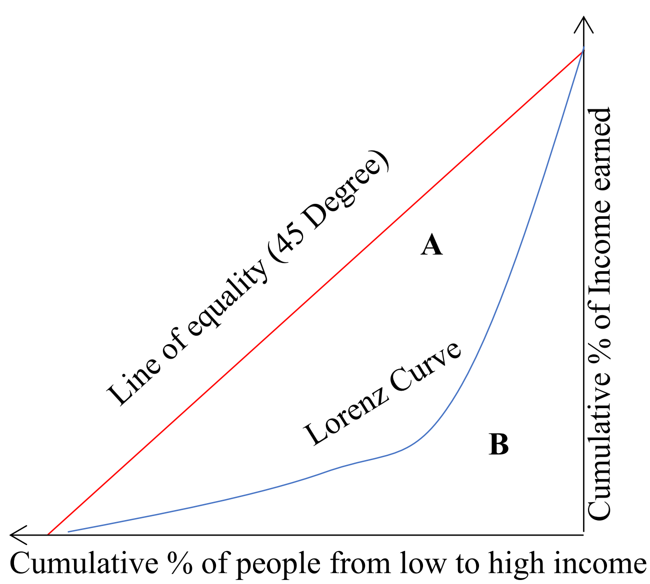

Figure 2. Pictorial representation of Lorenz Curve

If income were equally distributed, the Lorenz curve would correspond to the 45-degree line. However, in all societies, the actual cumulative distribution of income is unequal and follows a line below the 45-degree line, known as the Lorenz curve. The Gini coefficient is calculated as a ratio between area A and area A+B. The higher the ratio, the more unequal the economic inequality (Anjali Bhatt et al., 2020).

The Gini Index indicates a reduction in inequality as social transfers increases. The decline in inequality is strictly connected to the rise of income in the lowest quintiles. Since the social security agencies are public institutions, the resources mobilized by them should be invested according to criteria established for the optimum economic and social development of the country. These criteria should guide every investment decision. The funds mobilized through social security should be channeled into the pool available to the government, and tapped for investment in different projects according to national priorities in such a way that they will expand productivity and taxable capacity.

The, investment decisions should be made in the light not only of over-all development policy but also of economic trends; for example, in an inflationary situation marked by speculative movements, the investment of social security funds in buildings or in land could be incompatible with a stabilization program.

3. Driving factors of Economic Inequality

Economic inequality is a significant global challenge, characterized by disparities in income and wealth distribution within and among countries. While a Gini coefficient of 0 represents perfect equality and 1 represents absolute inequality, many countries, particularly in the Asia-Pacific region, exhibit high Gini coefficients, with some above 40, indicating substantial inequality. Understanding the multifaceted driving factors behind this rising inequality is crucial for effective policy intervention. Key driving factors of economic inequality include:

3.1 Government Policies and Institutions

Government policies are among the most important factors determining inequality levels.

Technological Change and Globalization Technology and trade liberalization have profoundly reshaped labor markets, providing disproportionate advantages to highly skilled and educated workers, thereby widening inequality. Technology has reduced the demand for low- and middle-wage workers, such as those in factory assembly lines, while increasing the demand for high-skilled, higher-paid workers (Mickael Melki 2022 & Friedrich, 2021). This shift has particularly impacted men and workers without college degrees in factory towns.

Taxation Policies: Tax policies significantly influence inequality. In many high-income countries, including the United States, taxes have become less progressive over the past five decades, leading to a decline in tax obligations for top earners and accelerating the growth of their incomes. This regressive taxation, where lower earners pay a higher relative share, places a greater financial burden on low-income families. Strengthening tax systems, making them more progressive, taxing corporations and high-wealth individuals sufficiently, ending profit-shifting schemes, and improving tax collection are identified as crucial steps to reduce inequality.

Social Protection Systems: Strong social protection systems, alongside fair taxation and labour market policies, are key instruments for addressing rising inequalities. Social security programs, particularly those financed by payroll taxes, can mobilize savings for economic development and serve social objectives. These systems can reduce income inequality by redistributing income from the better-off to the less well-off, especially when well-designed and adequately funded. Universal social security schemes, rather than targeted ones, tend to achieve the highest reductions in inequality due to higher expenditures and broader popularity, as taxpayers are more willing to support schemes from which they also benefit. **Public Education Spending:** Public education can enhance both economic growth and equitable distribution. However, education investment biased towards urban areas can contribute to widening the urban-rural income gap. Unequal access to quality higher education, with rising tuition costs, means that children from low-income households are significantly less likely to attend college.

Property Rights and Governance: The quality of institutions, particularly property rights, plays a crucial role. When property rights are poor, inequality substantially decreases investment. This can happen because the wealthy elite might engage in unproductive rent-seeking activities, such as lobbying or expropriation, rather than productive investments. Conversely, as property rights improve, the detrimental impact of inequality on investment diminishes. Good governance, transparency, and stakeholder involvement are crucial for effective social security policy.

Credit Market Imperfections Imperfect credit markets are a significant driver of inequality, particularly in developing countries. When access to credit depends on social status or wealth, higher inequality can exclude the poor from markets, thereby reducing their investment opportunities. This results in some wealthy individuals over-investing while those without sufficient money or social connections under-invest (Friedrich, 2021).

3.2 Social and Demographic Factors

Access to Opportunities: Inequalities extend beyond income and wealth to opportunities, access to services and resources, and political representation. People at the bottom of the economic ladder often lack the options to gain wealth or participate in the political system, leading to feelings of exclusion and disempowerment.

Gender and Race/Ethnicity: Inequality often goes hand-in-hand with disparities along dimensions such as gender, race, ethnicity, and disability. Women and girls are at a higher risk of poverty, often have lower access to education and healthcare, and are more likely to be in unpaid or low-paid precarious work, contributing to gender inequality. In the U.S., wealth among Black and Hispanic families has grown more slowly than in white families, highlighting persistent racial wealth gaps.

Demographic Changes: Population aging, changes in social structure, and increasing life expectancy are factors that encourage reforms in social security and can affect income distribution.

In conclusion, economic inequality is a complex issue driven by a combination of technological advancements, globalization, specific government policies related to taxation and social protection, labour market dynamics, imperfections in credit markets, and various social and demographic factors exacerbated by economic shocks. Addressing these interconnected factors requires comprehensive, multi-faceted policy interventions that prioritize progressive taxation, universal social protection, equitable access to education and healthcare, and robust labour market protections to foster more inclusive and just societies.

4. The Interplay of Social Security, Inequality, and Investment

Social security systems play a pivotal role in modern economies, serving as fundamental mechanisms for financial support across various life contingencies and significantly impacting the distribution of income and wealth. Beyond their social objectives, these systems also interact profoundly with national investment patterns and overall economic growth. This paper explores the intricate relationship between social security, economic inequality, and investment, drawing on empirical evidence and theoretical frameworks.

4. 1. The Role of Social Security in Mitigating Inequality

Social security primarily mitigates inequality through **redistribution via taxes and transfers**. These systems transfer income from wealthier individuals to the broader population, including those on lower incomes, thereby reducing disposable income inequality. The extent of this redistribution depends significantly on the specific design of fiscal policy and social protection schemes (Sylvain et al., 2022).

Effectiveness of Scheme Design: Universal vs. Targeted Approaches While it may seem intuitive to target social security transfers at the poorest members of society to tackle inequality, global evidence. The "paradox of redistribution" suggests that **universal social security schemes achieve greater reductions in inequality than narrowly targeted schemes.** This effectiveness stems from two main factors:

- **Higher Expenditures**: Universal schemes generate higher overall expenditures, which necessitate greater taxation from wealthier societal members for redistribution across the population.
- **Broader Public Support**: Taxpayers are more willing to accept higher taxation when they also benefit from the programs, leading to increased political and social will to fund these systems robustly.

Progressive Elements and Wealth Inequality: The design of social security benefits, particularly the inclusion of a **guaranteed floor** and less reliance on individual accounts, leads to lower consumption inequality and helps prevent poverty, especially when borrowing is constrained. Conversely, a shift towards individual accounts, which entail less sharing of earnings risk, generally increases consumption inequality both before and after retirement.

The progressive nature of social security can be affected by its financing. While benefits are often designed to disproportionately aid low earners, the revenue side, particularly payroll taxes, can be regressive due to earnings caps. Increasing benefits for low earners is generally more effective in reducing inequality than solely extending taxes to high earners. However, proposals to remove the maximum taxable earnings cap on wages, for example, are seen to do little to address overall wage income inequality without simultaneous changes to the benefit formula.

Broader Social and Health Outcomes Beyond direct financial impacts, social protection promotes **health equity** by reducing economic inequality, which is associated with worse health outcomes such as reduced life expectancy and higher infant mortality. Income security is highlighted as the single largest contributing factor to self-reported health. Furthermore, social protection fosters **social cohesion** by making people feel more included as economically contributing members, contributing to a more stable society (Gerhard Glomm et al., 2008).

In conclusion, the relationship between economic inequality, social security, and investment is deeply intertwined. While high inequality can impede investment and economic growth, well-designed social security systems, particularly universal schemes, are powerful tools for reducing inequality and fostering inclusive economic development. This dual role underscores the importance of strategic policy decisions regarding social security funding, design, and investment to achieve both social justice and economic prosperity.

5.Investment Strategies for Social Security Funds

Social security programs, fundamentally designed to provide financial and social support, also serve as critical mechanisms for investment and broader societal well-being. Social security funds are strategically invested to ensure long-term financial stability and to contribute to national development, balancing risk, return, and societal impact.

5.1. Societal Strategies for Social Security

Social security systems are financed through various mechanisms that generate funds for investment:

Payroll Taxes and Contributions: These are the primary sources of funding in many countries. Social insurance is financed by contributions from protected persons and employers, often complemented by general taxation..

Government Budget and Transfers: Funds from federal, regional, and local budgets are crucial government funding sources. Public subsidies, sometimes paid from general revenue, may complement social insurance contributions, especially for specific purposes like child maintenance, health care, or covering deficits from bringing elderly persons into insurance.

Accumulated Surpluses and Reserves: Significant saving mobilization is achieved by **funded programs** that set aside money which, with interest and other earnings, will cover future benefit payments (Audrius Bitinas, 2019).

Other Non-Governmental Sources: These include private pension funds, private insurance funds, non-profit organizations, and direct contributions from the population and enterprises. Donations and charitable contributions also contribute to non-state social security.

5.2. Types of Investments

Social security funds are typically invested across a range of assets, with legislative provisions often governing these decisions:

Public Debt: In many developed countries, public debt (government bonds and obligations) is the **principal type of investment** for social security institutions. Loans to central and local government authorities also form a large part of pension insurance institutions' resources.

Physical Assets: In several developing countries, social security sectors invest significantly in physical assets. These can include **hospitals and other medical facilities, apartment buildings, hotels, houses, and land**.

Financial Assets: Beyond public debt, financial assets include **mortgages, housing loans, personal loans, stocks and bonds, and cash deposits.** While direct investment in real estate occurs, indirect investments through mortgages and housing loans are also common. Investment in corporate stocks and bonds is less frequent but occurs in some nations, often channelled through development banks.

Enterprise Investments: Direct investments are made in **public and private enterprises** in several countries. This form of investment is considered highly advisable for increasing future production and exploiting a country's resources. Public utility enterprises are often suitable due to their stability in earnings (Sylvain et al., 2022).

5.3. Personal Strategies for Social Security

Individuals integrate social security into their personal financial planning, leveraging its unique features to enhance retirement security.

Integrating Social Security into Retirement Planning: Social Security is designed as a **financial foundation** to cover basic needs and is a **key part of supplementing savings and pensions**, not intended as a sole source of retirement income.

Guaranteed Lifetime Income: Social Security provides a **guaranteed stream of lifetime income, w**hich is annually adjusted to offset inflation, protecting individuals from outliving their assets.

Diversification: Relying solely on private savings or investments exposes individuals to market downturns. Social Security diversifies income sources by providing a **non-market-dependent stream of income,** reducing overall retirement plan risk (Friedrich, 2021).

Consumption Smoothing: Social security systems help individuals **smooth consumption over the life course and during times of risk**, such as unemployment, sickness, or retirement.

6. Challenges and Suggestions:

Despite the numerous benefits, the effective implementation and sustainability of social security systems face ongoing challenges.

Inflation and Policy Risk:

Erosion of Value: Inflation can lead to substantial deterioration in the real value of social security assets and investment income. This makes social security institutions reluctant to invest in unprotected financial assets in inflationary environments.

Financial Sustainability and Policy Adjustments: Social security systems, especially those with fixed benefits under inflationary conditions, face the challenge of **long-term financial sustainability** if obligations exceed funding. Addressing potential funding gaps often requires policy adjustments like benefit cuts or tax increases, which, while impacting wealth distribution, still attenuate overall inequality trends.

Political Risk: Changes in tax and benefit provisions by future legislatures, driven by demographic and macroeconomic shifts, pose a "political risk" to participants, which can be compared to "market risk" in investmentbased schemes.

Design and Funding Choices:

Optimal Design: The effectiveness of social security in tackling inequality depends critically on the **design of schemes and the overall system**. Universal systems are generally more effective at reducing inequality than targeted approaches.

Fiscal Space: Generating the necessary fiscal space for expanded social security requires concerted efforts, including strengthening national social contracts and implementing **progressive taxation strategies**, where wealthier members of society contribute more.

Investment Portfolio Choices: Decisions regarding investment vehicles (e.g., public debt, physical assets, corporate securities) and the balance between security, profitability, and social utility require careful consideration to maximize overall benefits and mitigate risks.

Financial Literacy and Trust: A sufficient level of financial literacy, trust, and engagement among the population is important for the effective functioning and public support of social security systems.

7. Conclusion

The paper concludes that **social security is a fundamental mechanism** to achieve societal progress and sustainable economic growth by providing **income security** to individuals and households. Addressing income insecurity is crucial, especially where **economic inequality** exists, as inequality negatively impacts growth. Investments in social security can **alleviate or reduce economic inequality** by promoting a better economic cycle.

Well-designed social security systems, particularly **universal schemes**, are powerful tools for **mitigating inequality** through redistribution via taxes and transfers, rather than narrowly targeted approaches. This process provides households with higher income security, enabling them to invest in nutrition, education, and health, thereby **improving human capital** and productivity.

For social security funds, **investment strategies must balance security and profitability** while contributing to long-term national economic growth. Key challenges include managing inflation, policy risks, and ensuring financial sustainability, necessitating careful design and **progressive taxation** strategies. Ultimately, **strategic policy decisions** regarding social security funding, design, and investment are vital for achieving both social justice and economic prosperity.

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