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Pensions in East Asia and Pacific: Features, Trends and Directions

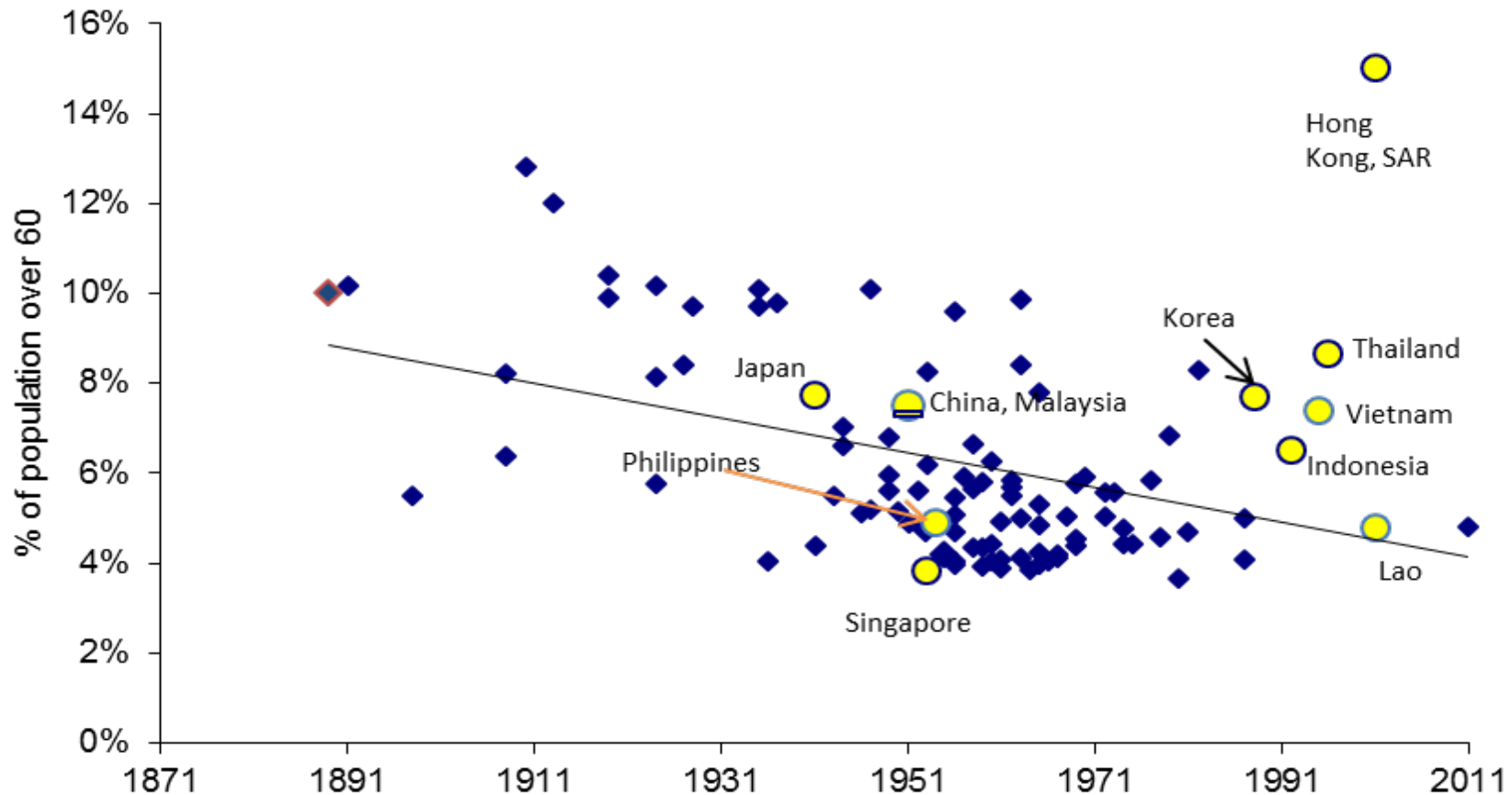
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Outline of presentation

- Quick tour of features of East Asia and Pacific pension systems
- Main challenges facing different country groupings
- Directions for the future

Some features of EAP pension systems

Most East & Southeast Asian were late starters on national mandated contributory pension systems



Pensions systems in EAP exhibit greatest design heterogeneity of any region...

▣ **Group 1: Defined contribution based systems**

- Indonesia* (planning to move to hybrid DB/DC)
- Malaysia
- Singapore
- Pacific provident funds (PNG; Solomons, Fiji, et al)

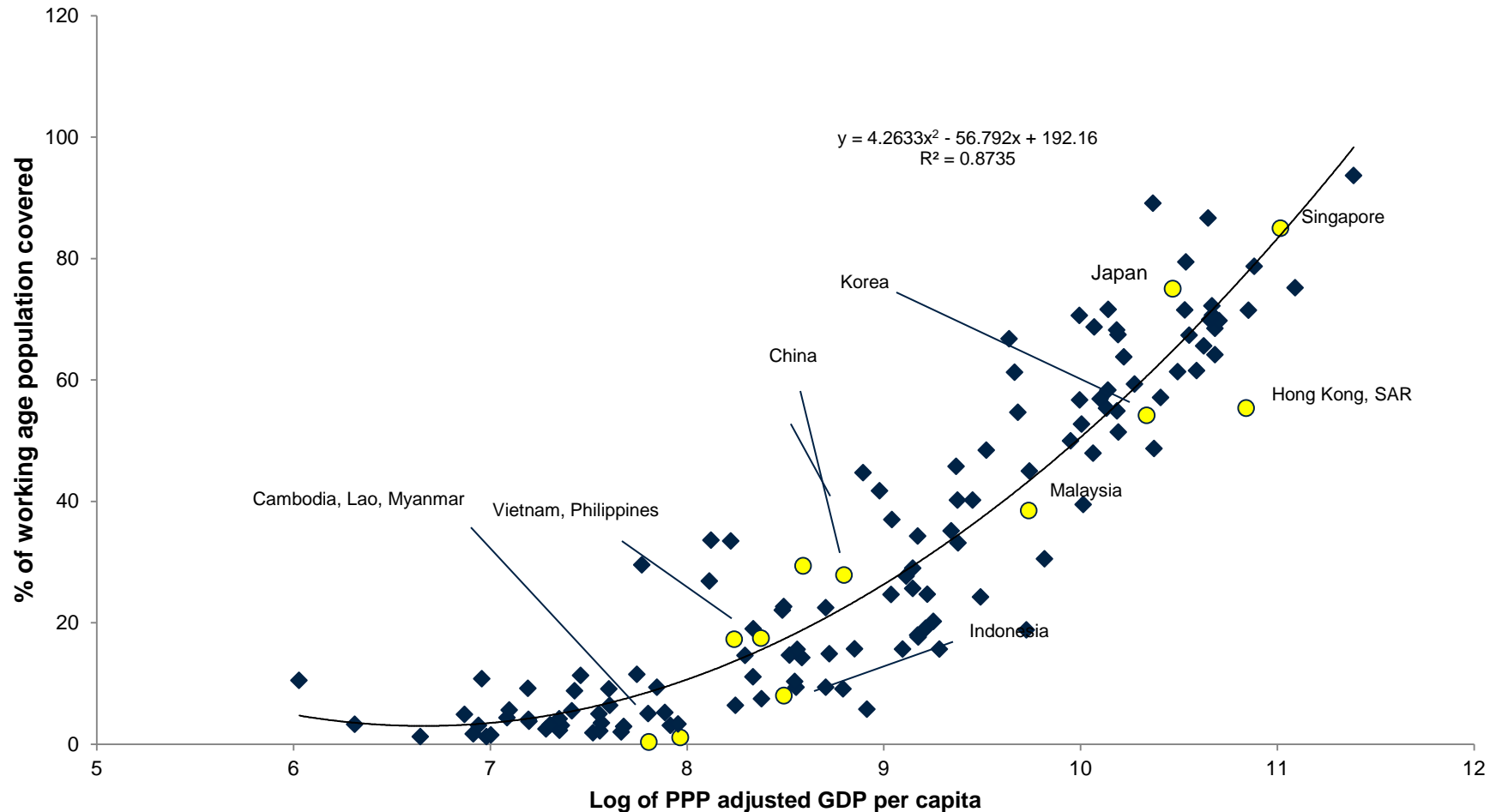
▣ **Group 2: Pay-as-you-go DB schemes**

- China (transitioning to hybrid DB/DC)
- Korea
- Japan
- Mongolia (transitioning to NDC)
- Philippines
- Thailand
- Vietnam

▣ **No mandated national scheme**

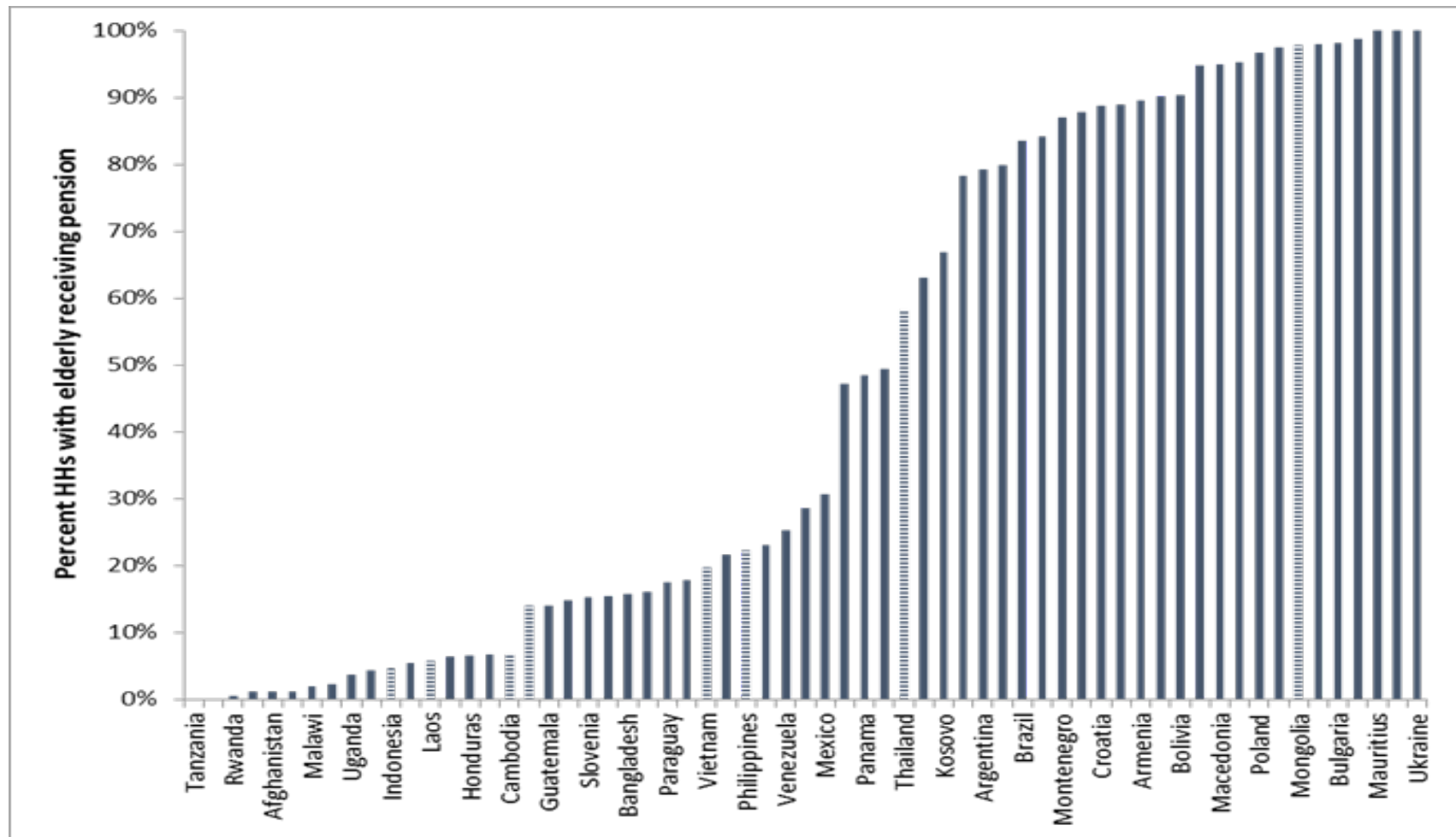
- Cambodia
- Lao (but planning to introduce in 2015)
- Myanmar (but planning to introduce in 2015)
- Timor-Leste (draft legislation)

Coverage of contributory systems around global averages for income levels but with unusually rapid pace of demographic transition...



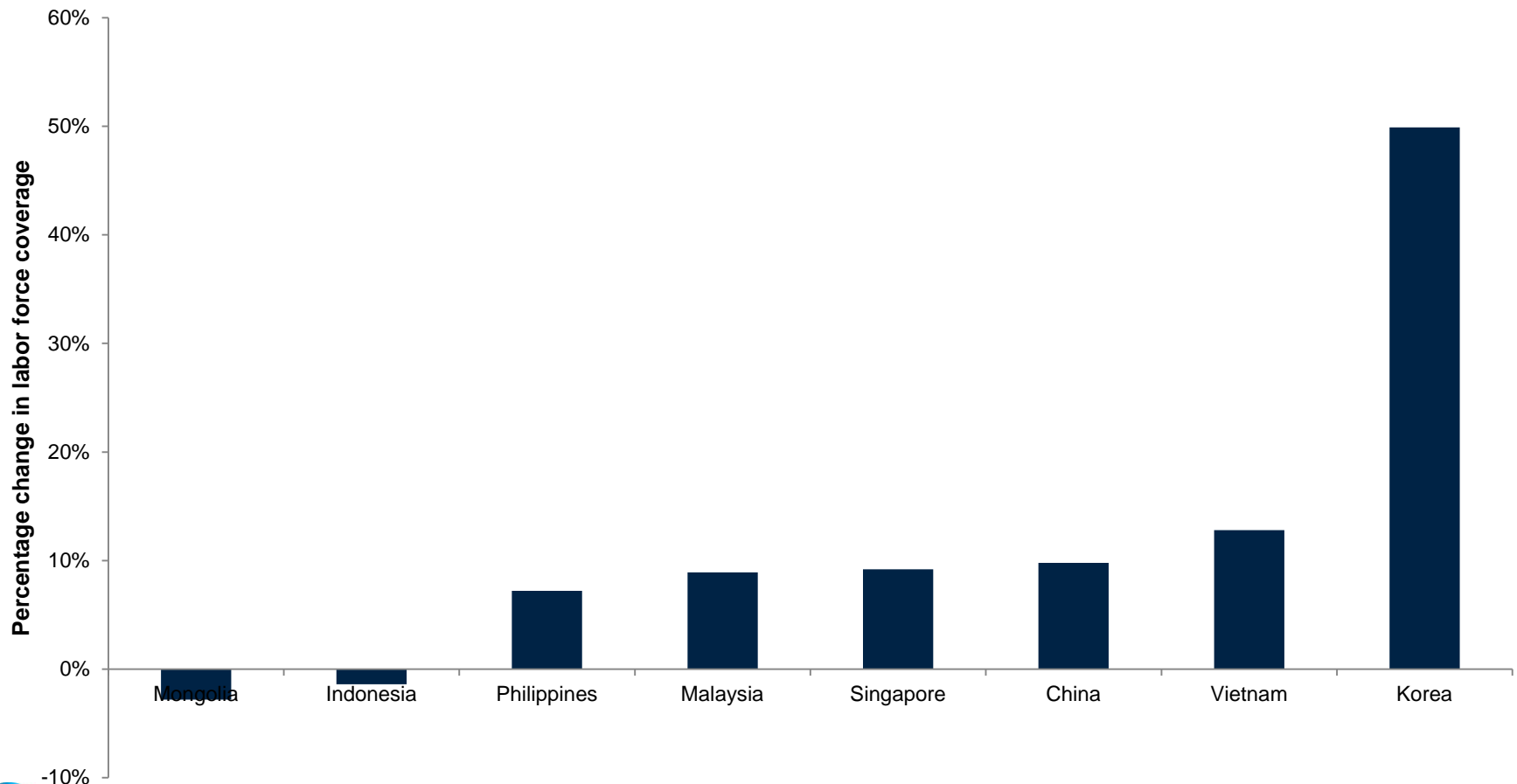
Coverage is heavily concentrated in upper quintiles of the income distribution within countries

(share of bottom 40% receiving any form of pension)

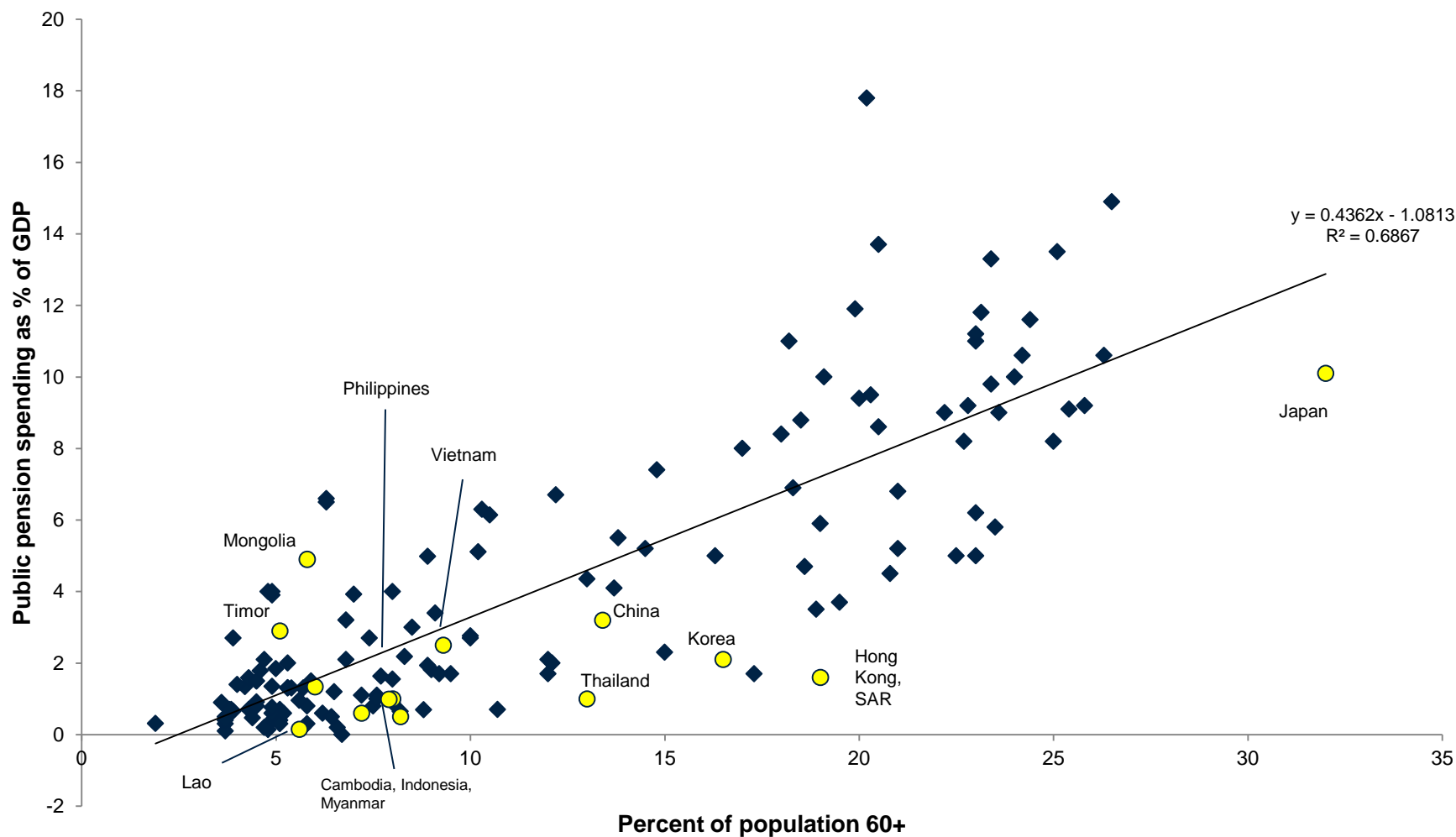


Coverage in contributory schemes has expanded slowly relative to rapid pace of demographic change

(% change in coverage 1990s-most recent)

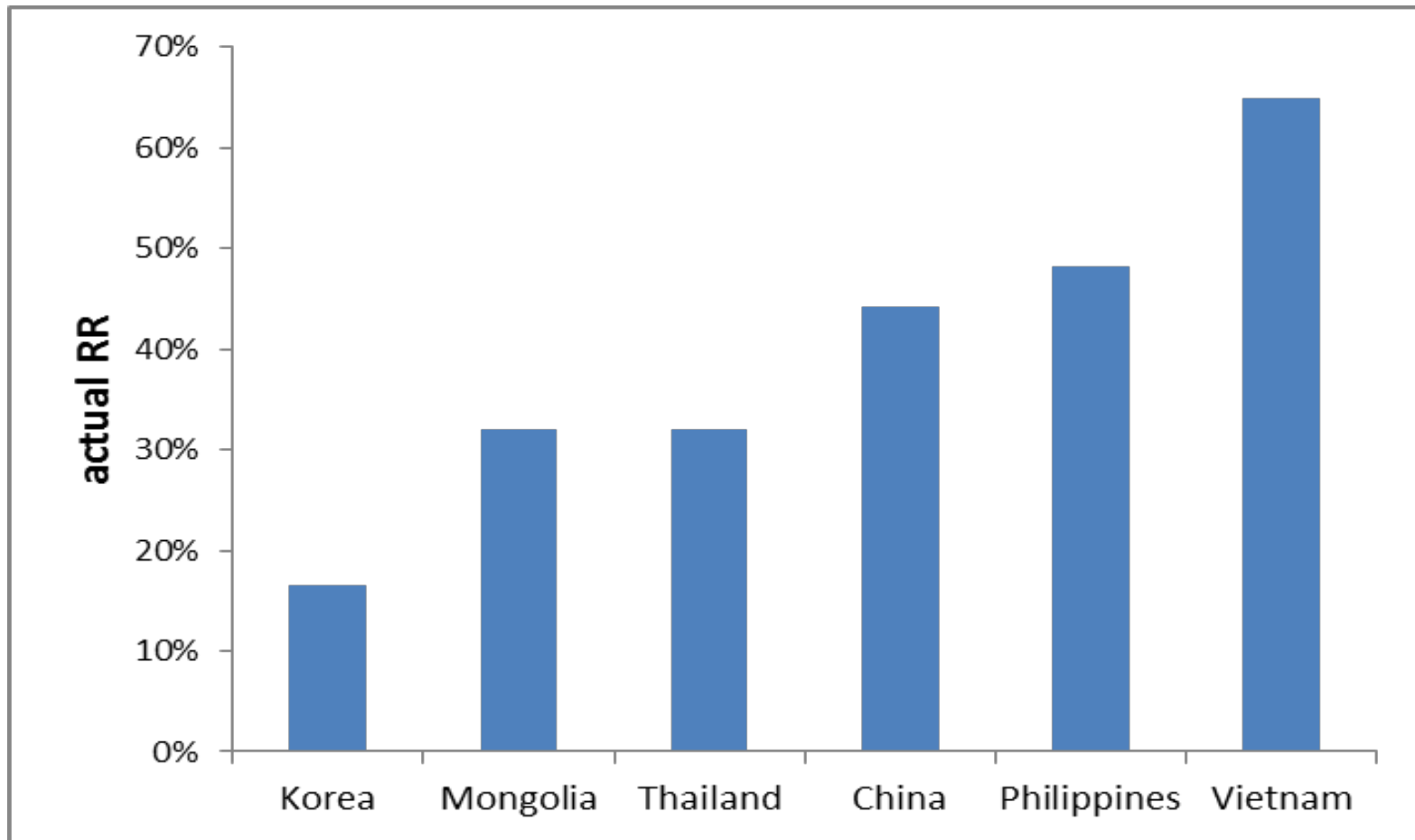


EAP pension spending largely lags global averages



In some cases because average replacement rates currently are not high by global standards

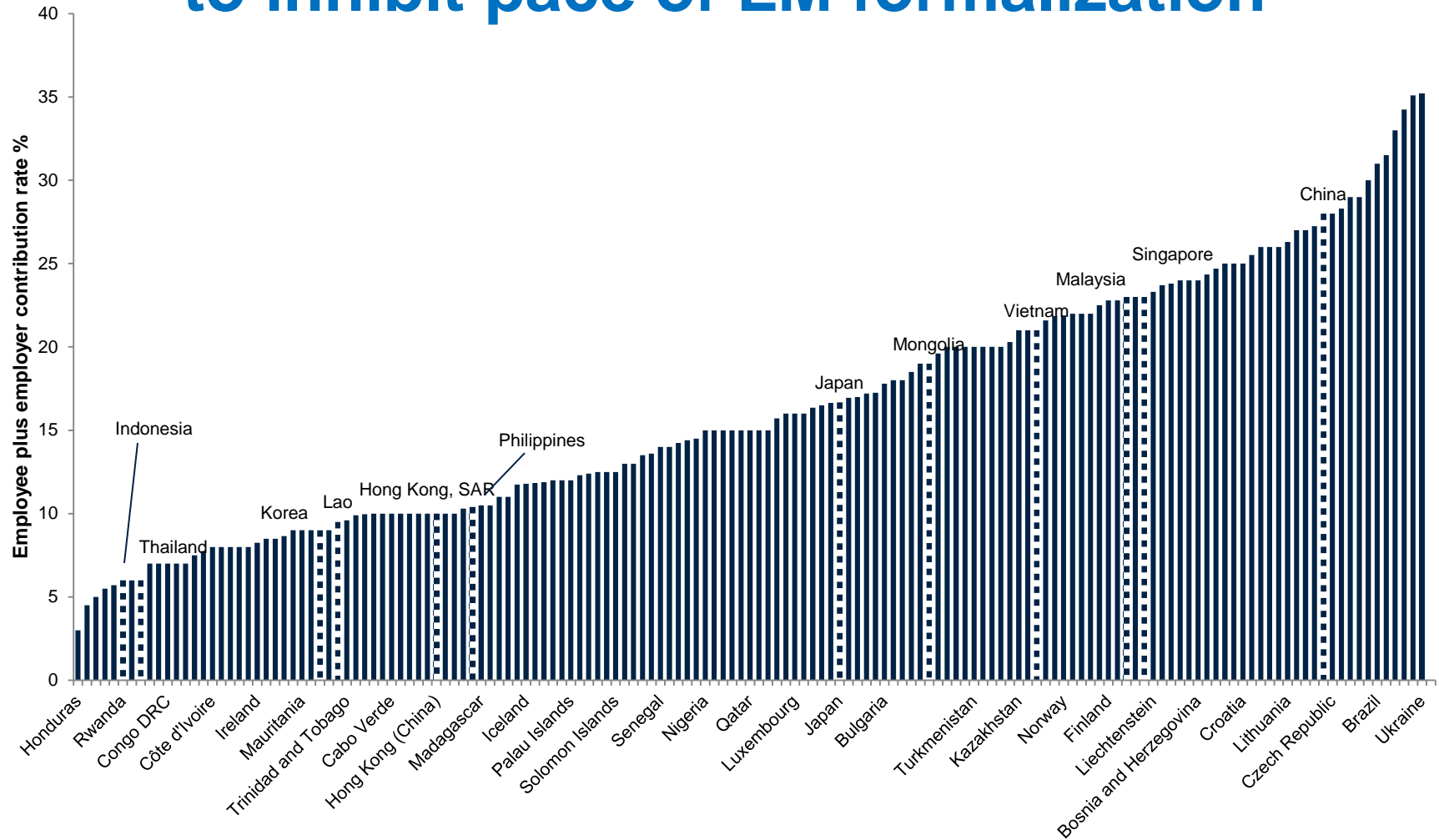
(average OA-disability-survivor pension/average covered wage)



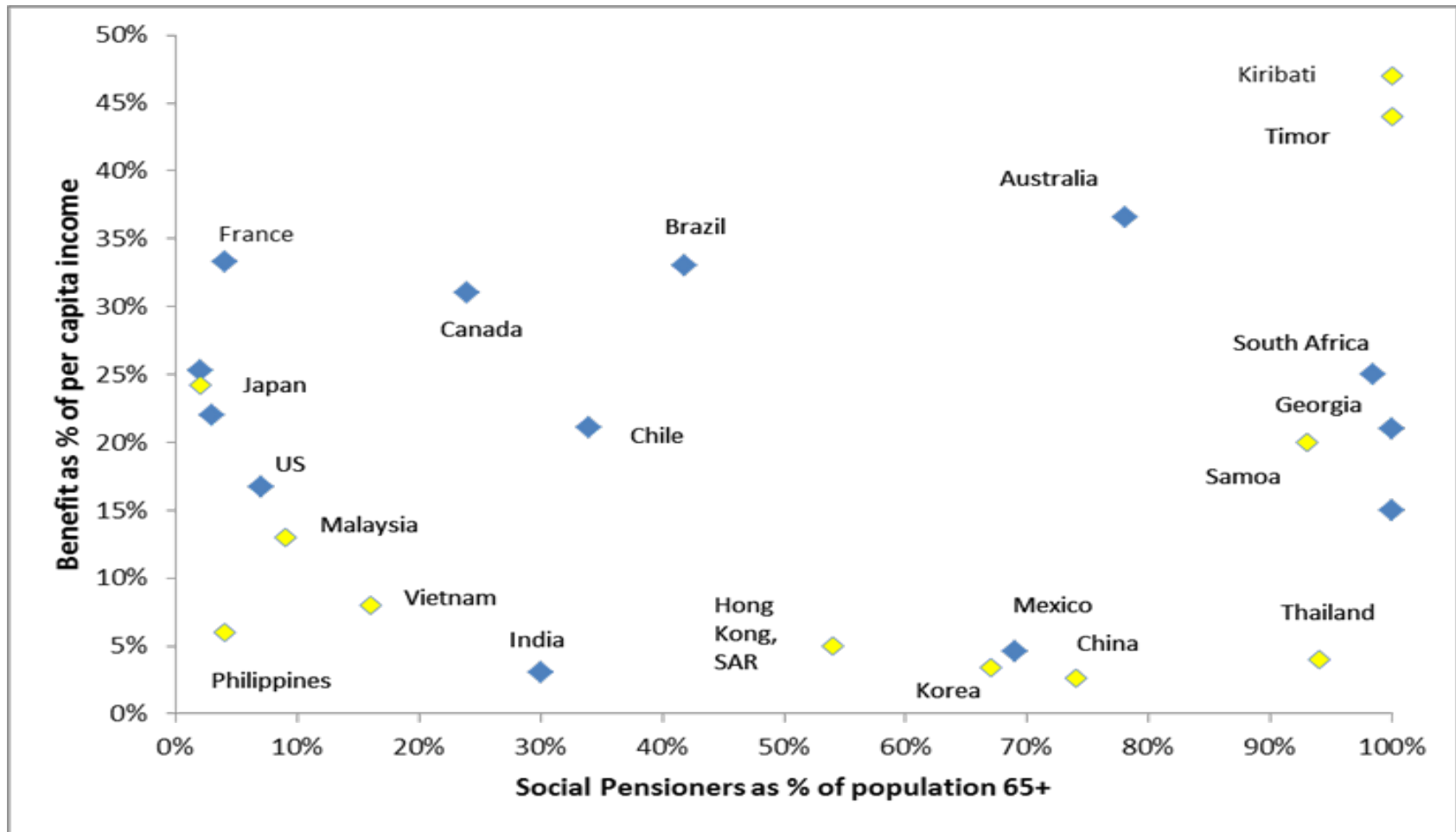
Lot of variation in target benefit levels & degree of redistribution in contributory schemes...

Country	Benefit Target	Degree of redistribution
China	High	Large
Hong Kong, SAR	Low	Small
Indonesia	Low	Small
Japan	Moderate	Moderate
Korea	Moderate	Large
Malaysia	Low	Small
Mongolia	Moderate	Large
Philippines	High	Large
Singapore	Low	None
Thailand	Moderate	Moderate
Vietnam	High	Small

Contribution rates for pensions exhibit wide variation across the region – with some likely to inhibit pace of LM formalization



More recent feature of EAP pension systems is spread of social pensions to address low coverage – often modest except Pacific



Main challenges facing different country groupings

Challenges facing EAP pension systems

The main challenges can be organized into some combination of:

- **Under-coverage**
- **Adequacy**
- **Sustainability**

Which is most salient varies across country groupings & the acuteness varies within each grouping...

Group 1 (DC & provident funds)

By definition are not concerned with sustainability, as assets = liabilities (subject to explicit or implicit guarantees)

Concern is over adequacy which depends on two parameters and one variable: (i) contribution rate; (ii) retirement age; and (iii) net rate of return on contributions minus wage growth.

None of Group 1 provides effective longevity insurance:

- retirement age has not kept up with longevity and returns have trailed wage growth causing low RoR in Malaysia and Singapore
- low contribution rate in Indonesia
- Hong Kong SAR, China has highly variable results

Group 2 – PAYGO DB schemes

Concerns over sustainability, actuarial imbalance due to initial parameters.

Country	Years till cash flow deficit
Japan	0
Mongolia	0
Korea	28
Philippines	23
Vietnam	c.10
Thailand	15
China	?

Plus several face low and slowly expanding coverage in contributory systems

Group 3 – no mandatory national schemes

Coverage the overriding challenge

and....

Sustainability an issue for unfunded DB schemes for aging civil service which squeezes fiscal space for coverage expansion

Several considering or have already passed legislation to introduce new national schemes but...

Formal sector less than 10 percent of labor force

Not integrating with civil servant pension schemes

Low capacity to administer a national pension schemes

Low capacity to manage inevitable reserves

Can they avoid the mistakes of other countries?

Shorthand summary of key challenges...

Country	Performance			Indirect impact		
	Sustainability	Coverage	Adequacy	Formal LFPR	LFPR 60+	Savings/Capital Market
Cambodia						
China						
Hong Kong, SAR						
Indonesia						
Japan						
Korea						
Lao						
Malaysia						
Mongolia						
Myanmar						
Philippines						
Singapore						
Thailand						
Timor-Leste						
Vietnam						

Minor

Significant

Major

Directions for the future

How to address the coverage gap in the face of rapid demographic transition?

In developing and ageing Asia, traditional contributory approaches are not going to do it...

Public subsidies of some form will be needed – likely with redistribution from general revenues & savings/insurance on actuarially fair basis:

- Continued expansion of social pensions for most/all (pension or affluence tested (e.g. Thailand))
- Matching defined contribution (MDC) schemes for non-poor informal (e.g. Korea)
- Innovation and hybrids (e.g. China; Mexico proposal)

Innovation and hybrids for coverage expansion...

China:

Rural and urban informal pension schemes have added 350-400 million into a pension scheme in 4 years: small MDC + basic social pension after 15 years contribution

Mexico proposal (Levy 2012):

Government contributes minimum amount to individual accounts for every adults citizen: enough to generate annuity = social pension – with phased introduction.

Each faces issues, especially with management of accumulations

Sustainability reforms in contributory schemes...

- Official **retirement ages** will need to rise & equalize for men and women in developing EAP countries – & linked to changes in life expectancy
- **Early retirement treatment** should shift from incentivizing (e.g. VN/PH) to encouraging longer working lives (JP;KR)
- **Longer career averaging** for pension calculation
- **Linear accrual schedules** to provide neutral incentives for longer work
- **Indexing** pensions to changes in prices
- **Investment policies** on accumulations and IA

Integrate civil service schemes with national private sector schemes & fund explicitly

Why?

- More open labor markets and pension portability
- Reduced administrative costs (especially smaller countries)
- Equity between public and private sector workers
- Civil servants on average older and pooling benefits
- Fiscal space needs to expand coverage

How?

- Slow transition to comparable replacement rates through adjustment of parameters (e.g. Vietnam)
- Immediate integration + supplementary occupational schemes
- New civil servants only and phased transition

Thank you