Provident Fund Systems in Asia – Challenges and Reform Directions

Richard Wolf

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Provident Funds around the globe



The role of provident funds is changing – from wealth accumulation to income generation.

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Multipillar pension systems allow for diversification of risks and retirement income sources

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Pension pillars	Function	Risks	Design options
Public pillar	▪ Redistribution ▪ Insurance	• Political • Inflation • Demography	• Pay-as-you-go • Tax-financed
Occupational pillar	▪ Accumulation of savings ▪ Capital accumulation& financial market development	• Behavioral biases • Inflation • Employer insolvency • Longevity • Investment	• Mandatory/voluntary • Defined Benefit/ Defined Contribution
Personal pillar	▪ Additional savings for financial security	• Behavioral biases • Inflation • Investment • Longevity	• Tax advantages • Guaranteed/not guaranteed products

Total retirement income adequate?

Stable and reliable pension systems need several pillars to balance out risks of the respective and arrive at an acceptable level of overall risk

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Provident Funds and their objectives

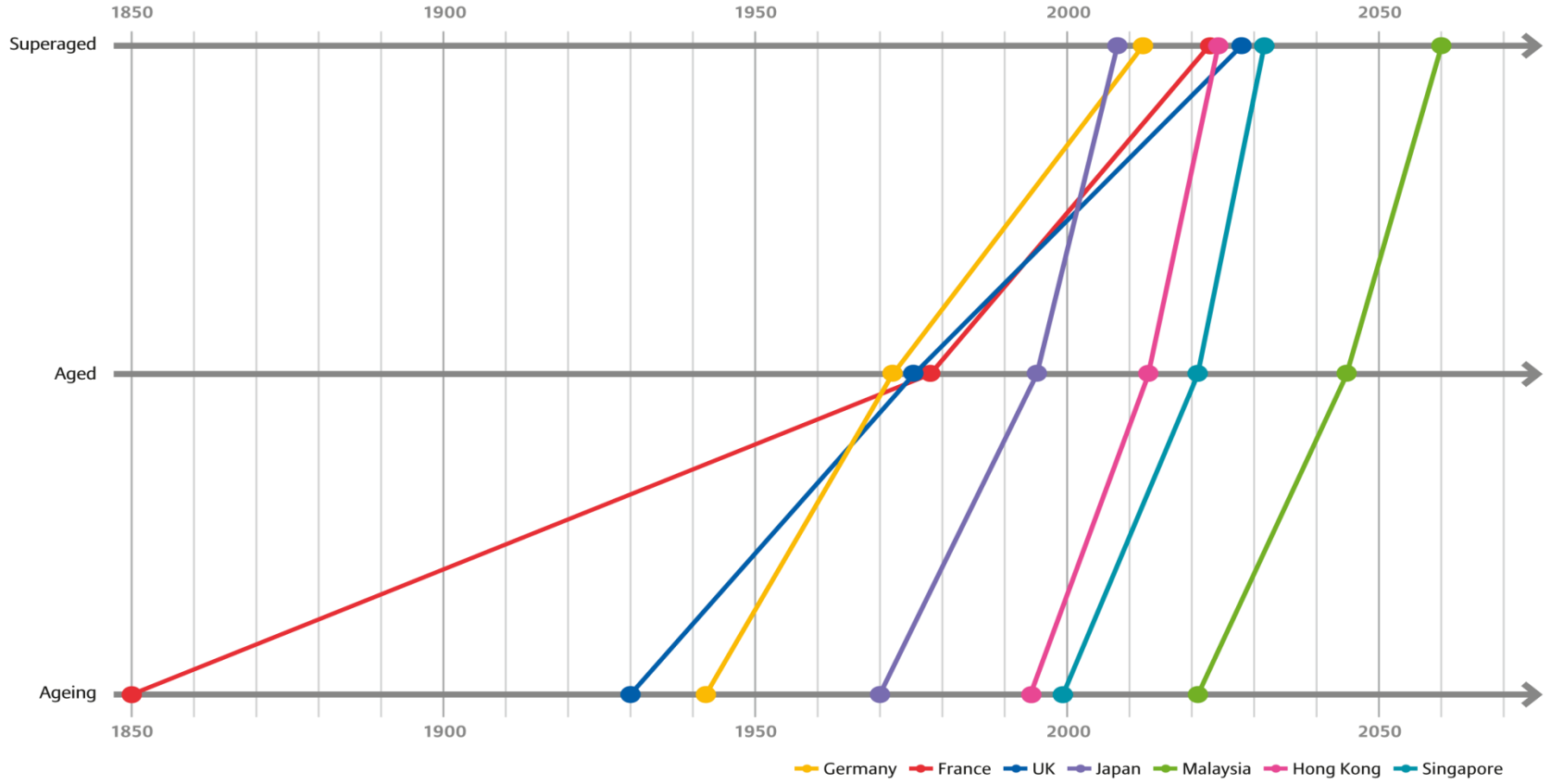
	Retirement	Health	Housing	Education	Other
Singapore	X	X	X	X	Dependant insurance, Asset enhancement
Malaysia	X		X	X	Hadj
India	X	(X)	X	X	Marriage
Hong Kong	X				

Asias mandatory Provident Fund institutions have a social security rather than an sole retirement savings objective.

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Demographic Change is happening faster in Asia

Demographic change in Asia will be faster and stronger in magnitude than in developed countries



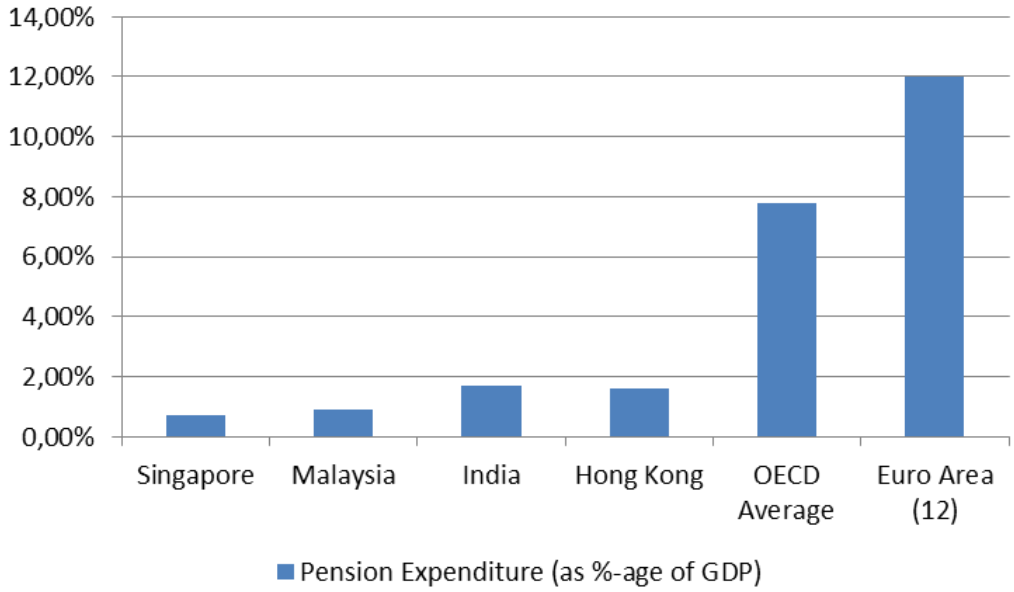
Sources: United Nations Population Division, US Census Bureau, Statistisches Reichsamt, Kisella and Gist, Mirkin and Weinberger, Allianz, International Pensions

Asian countries will have a shorter time period to adapt social security institution to the challenges of demographic change

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Funded pension systems result in fiscal sustainability

In constrast to most developed countries, fiscal sustainability is not a major concern



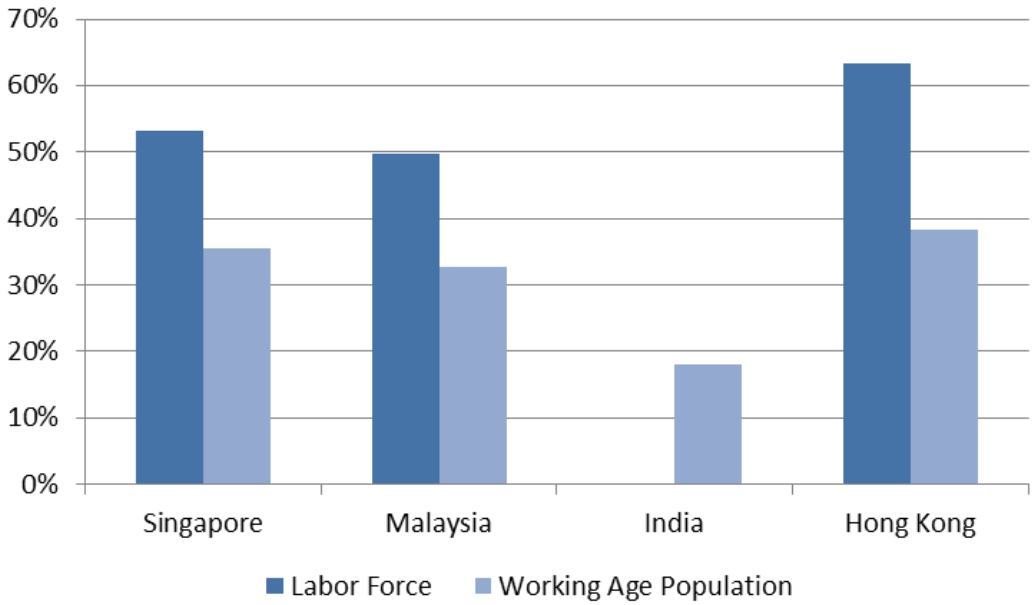
Source: OECD

- Asian funded pension are fiscally sound

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Informal workforce – informal pensions?

Formal pension coverage via Social Security Saving Systems



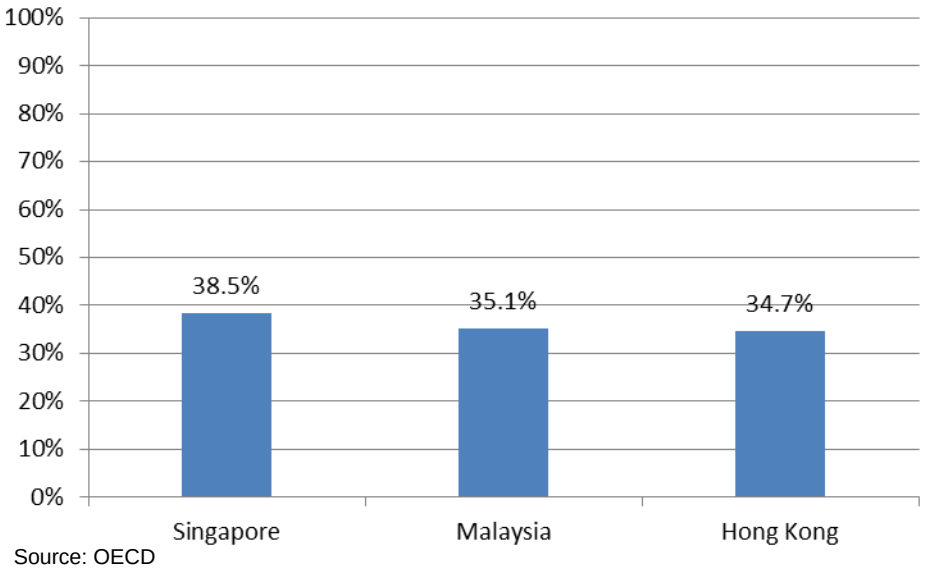
Source: ADB, own calculations

- Accounting for self-employed, civil servants and expatriates, pension system coverage approaches universal levels in Singapore, Malaysia and Hong Kong
- Coverage of formal pension provison remains a problem in developing countries

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Are retirement savings sufficient for an adeuate retirement income?

Gross Theoretical Replacement Rates



Source: OECD

- The OECD considers rule of thumb replacement level of 60-70% adequate for retirement.

- Singapore: 50% of CPF participants at age 55 do not have the required minimum sum (SGD 148,000)
- Malaysia: Only 23.4% of EPF members at age 54 fulfill the basic savings target (RM 173,000)

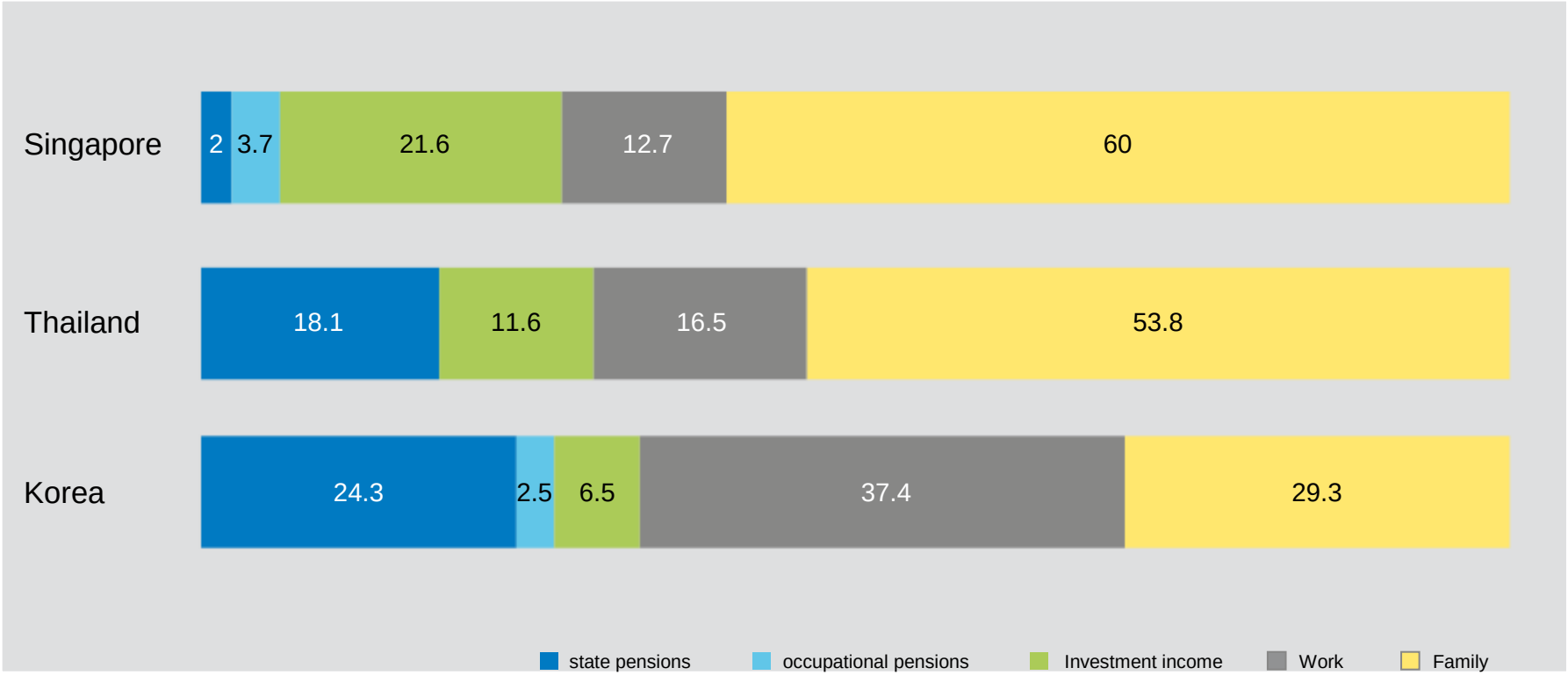
Generating an adequate retirement income remains a major issue.

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Family support is a major source of old age income in Singapore and Asia

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Importance of retirement income sources in % of retirement income; around 2010

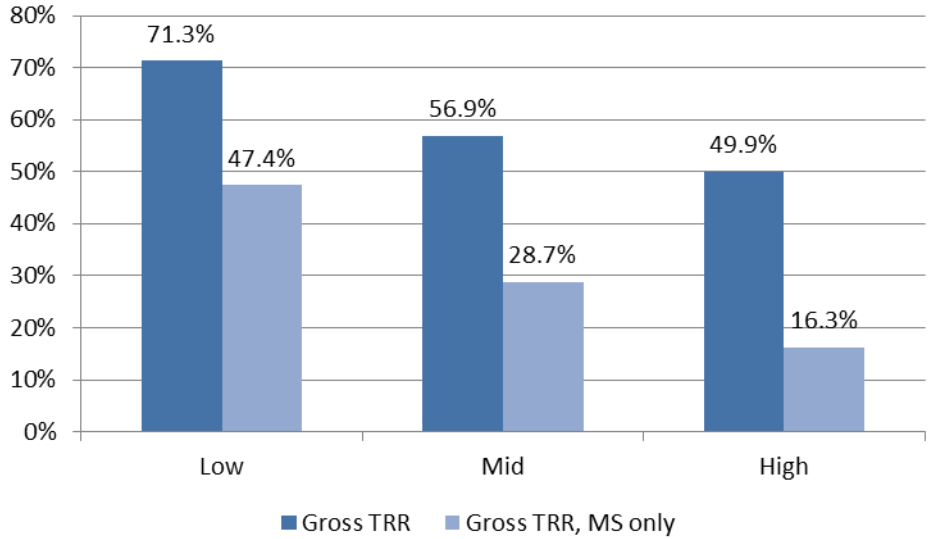


Sources: National statistics, Allianz International Pensions 2012

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Singapore – Will the CPF deliver an adequate retirement income?

TRR for full and Minimum Sum annuitization, male by income group



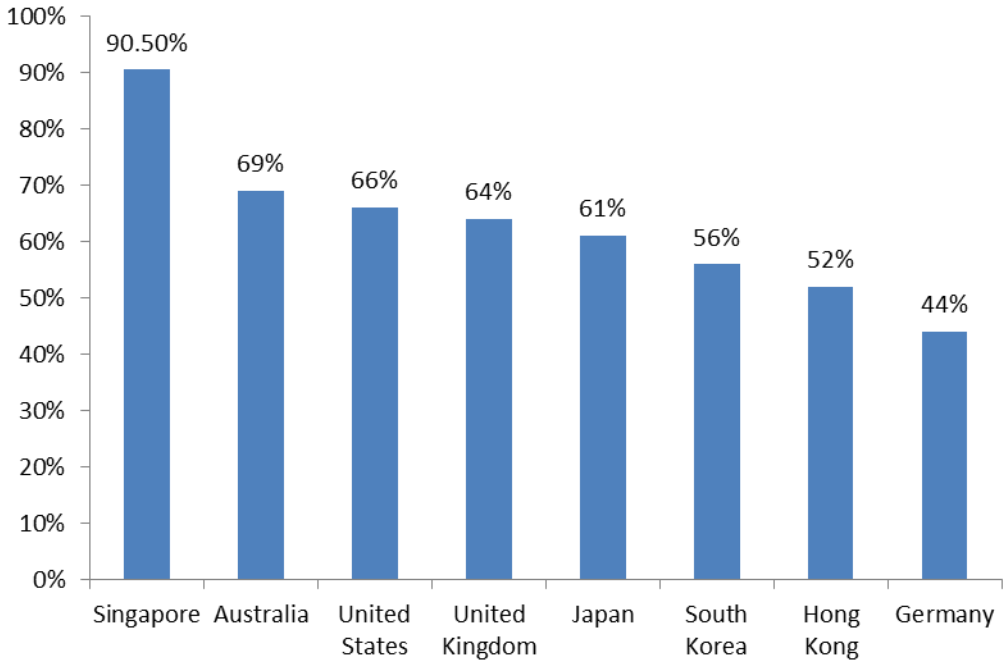
Source: C. Choon, A. Tsui; Adequacy of Singapore's Central Provident Fund;
Low , Mid, high refers to 30-,50 and 70-percentile of the income distribution

- If only the minimum sum is annuitized, people run a considerable risk to have a too low income later in live
- Although Singapore was the first provident fund to move from a wealth to a consumption frame, longevity risk is still a major source of risk.

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Singapore: Asset rich – cash poor?

Home ownership rates across countries



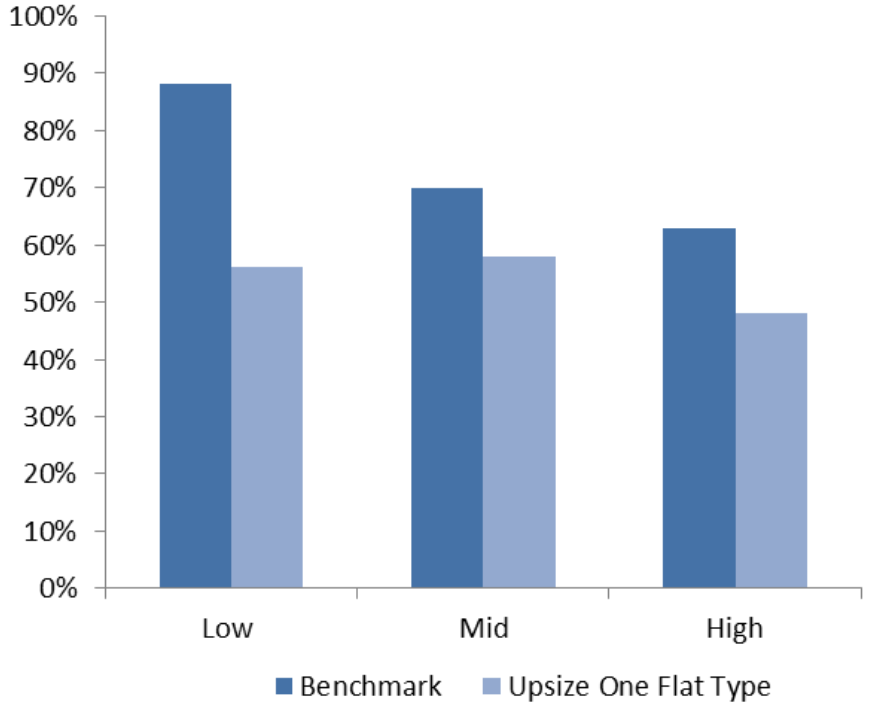
Source: Koh, Ministry of National Development

- Potential ways to monetize housing assets: Subletting, downsizing, reverse mortgages, lease and buy-back

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Impact of housing on retirement income

Net TRR, given different housing choices, by income group



Source: C. Choon, A. Tsui; Adequacy of Singapore's Central Provident Fund
Upsize: Low: from 2 to 3 rooms; Mid: from 3 to 4 rooms, High from 5 to executive

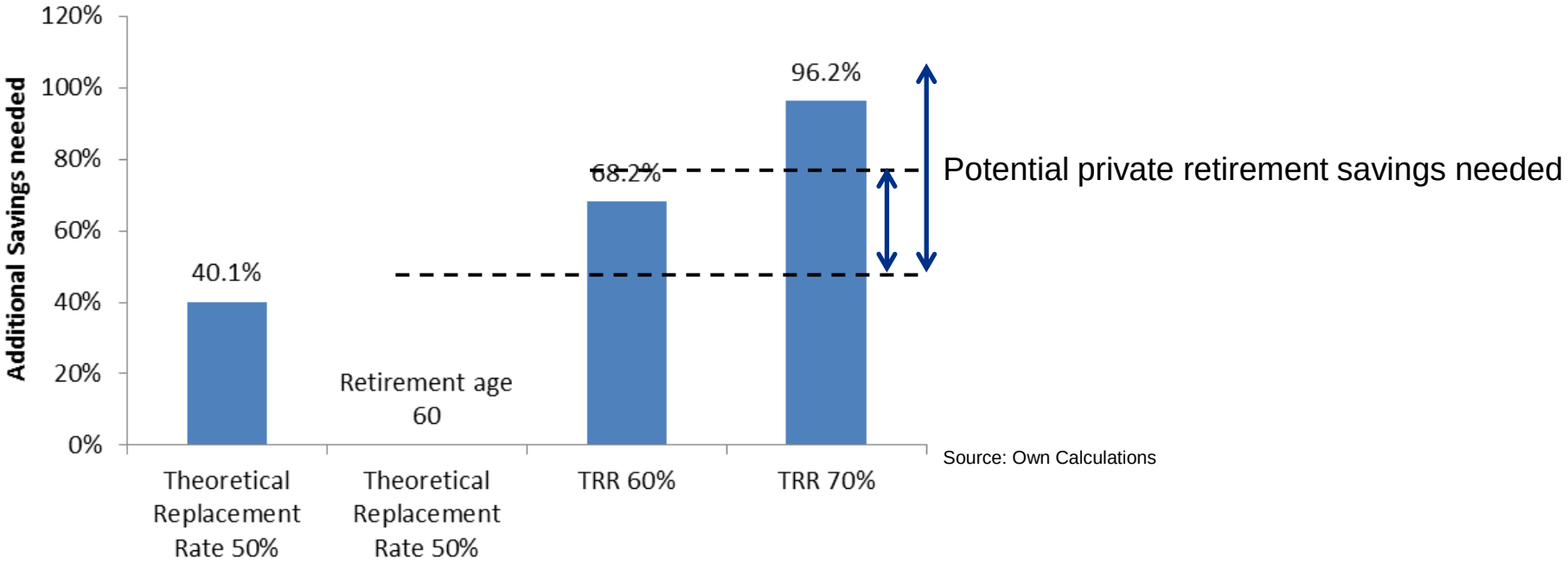
Housing is a retirement decision

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Working longer, saving more for an adequate retirement

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Case Study Malaysia



Source: Own Calculations

- Under the current framework, providing an adequate replacement rate from EPF savings alone seems unattainable
- An EPF replacement rate of 50% LDS could be achieved by increasing the retirement withdrawal option to 60 years
- Additional savings would then increase retirement income to replacement levels of 50% plus

Missing longevity protection remains an issue

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Summary

- Ageing and resulting socio-economic developments are happening fast in Singapore
- Demographic change will not lead to fiscal strains but put the family as a traditional old age income source under pressure.
- In contrast to other Provident Funds system, where considerable non-parametric reforms were introduced, Singapore relies on reforms within ist established pillar.
- Among Asia‘s Provident Funds, Singpore was the first to gradually introduce decumulation measures and to partially shift its focus fo lifelong retirement income
- Nevertheless, longevity and inflation remain an obstacle to retirement income adequacy
- In addition, the high share of illiquid housing wealth in the retirement portfolio, further increases the risk that spending needs cannot be met during retirement.
- In face of increasing longevity, Singaporeans have to prepare to work longer or to save more

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Thank you

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