Promoting Fairness and Sustainability of Pension Systems in East and Southeast Asia

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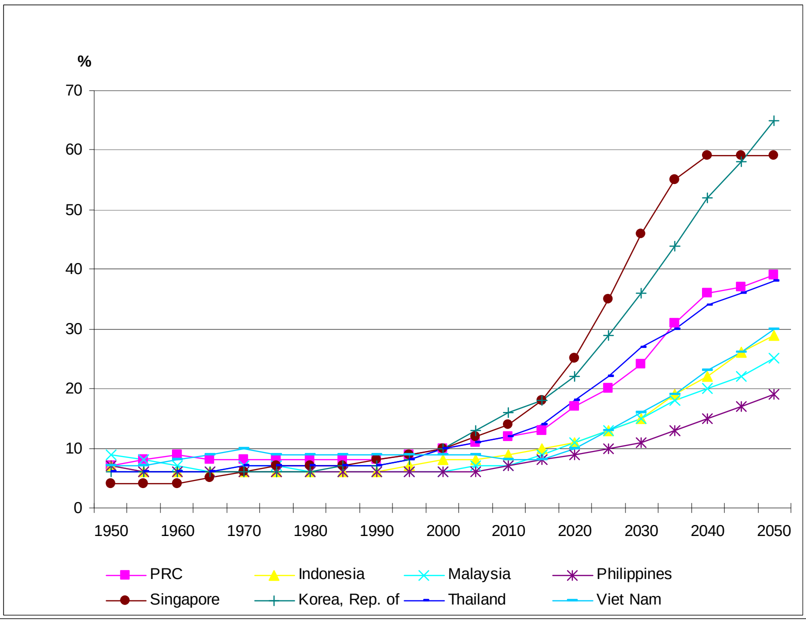
Introduction

- Demographic change poses two huge socio-economic challenges for developing Asia
  - Sustain rapid growth in the face of less favorable demographics
    - Demographic dividend is set to decline
  - Deliver affordable, adequate and sustainable old-age economic security
    - Region's fast-growing elderly population makes this imperative
  - The two strategic objectives sometimes come into sharp conflict with each other, and necessitate tough trade-offs
    - For example, expansion of public transfers to the elderly will reduce fiscal resources for health, education and infrastructure which affect growth

Ratio of elderly to working—age population, 1950-2050



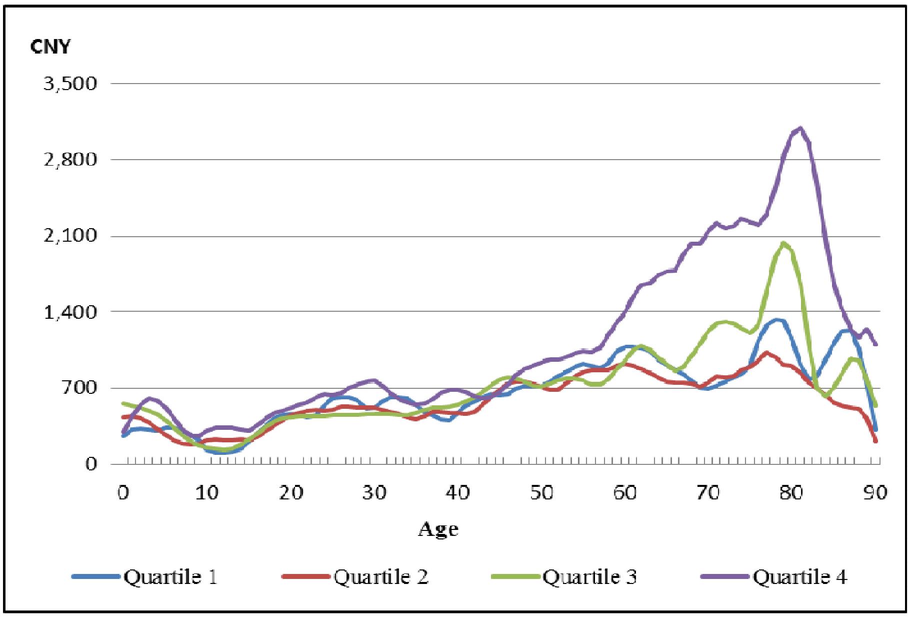
Basic structure of pension systems

Country	Pension Age (Years)	Difference Between Life Expectancy and Pension Age (Years)		Defined Benefit or Defined Contribution	Element of Income Redistribution
		Male	Female		
China	60 (55)	11.3	19.8	Defined Benefit, Defined Contribution, and Notional Defined Contribution	Yes
Indonesia	55	13.7	17.7	Defined Contribution	No
Korea	65	10	17.2	Defined Benefit	Yes
Malaysia	55	17	21.7	Defined Contribution	No
Philippines	65	4.5	8.9	Defined Benefit	Yes
Singapore	62	16	19.9	Defined Contribution	No
Thailand	55	11.5	20	Defined Benefit	No
Vietnam	60 (55)	12.3	21.2	Defined Benefit	No

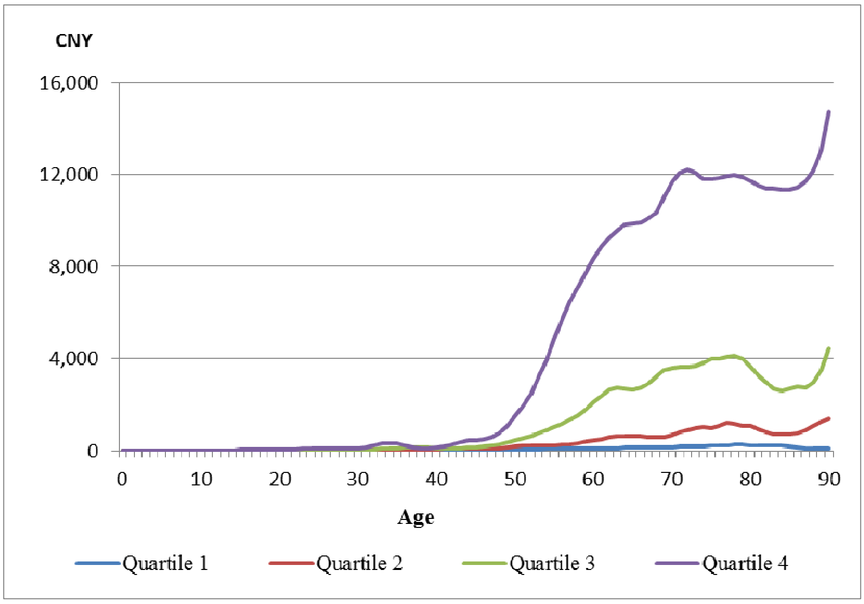
Fairness

- There is a great deal of disparity in terms of coverage, level of net benefits, and retirement age.
- For example, to attract personnel into the civil and the military service, their pension benefits are often more generous than those of the rest of the population.
  - In some cases, beneficiaries contribute relatively little into these systems further enhancing their net benefits to the extent that they can pose a risk to fiscal sustainability
- Another major disparity is between urban and rural areas
- Intra-generational disparities also arise between the formal and informal employment sectors

Per capita public spending on health by income quartile



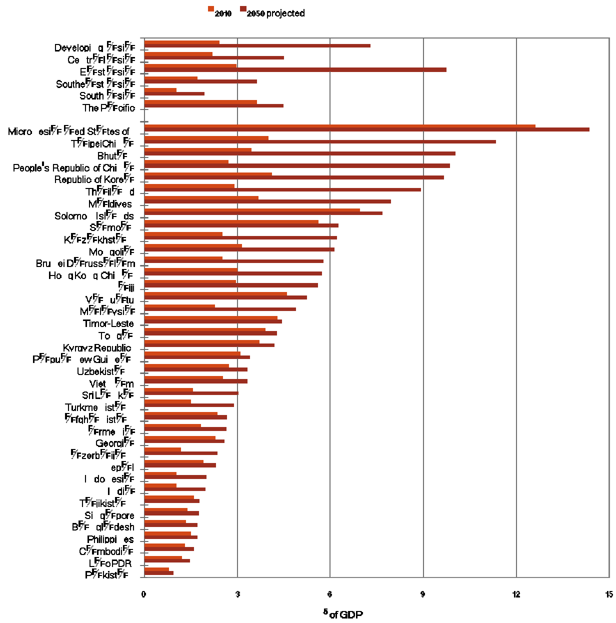
Per capita public spending on pensions by income quartile



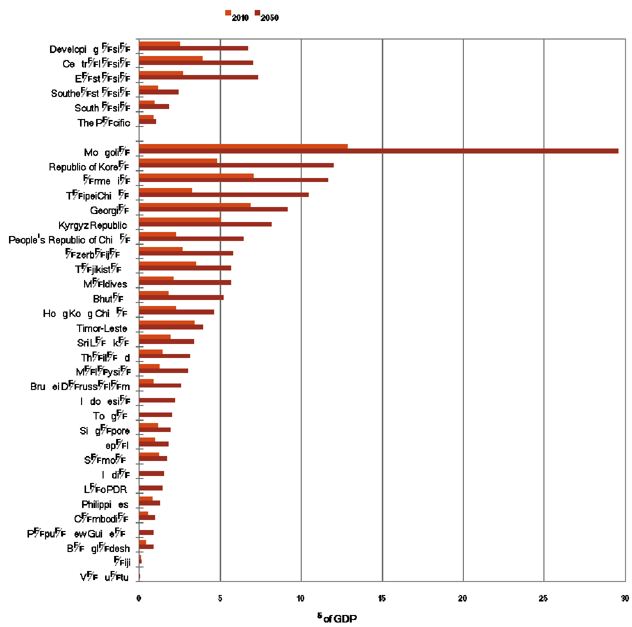
Sustainability

- If fairness deals with intra-generational disparities, sustainability addresses inter-generational disparities.
- In Asia, as in other parts of the elsewhere, defined benefit pension schemes tend to be pay-as-you-go and are not sustainable in the long run
  - Little or no link between contributions and benefits
- Without far-reaching reforms, the financial burdens of these schemes on future workers may become politically unacceptable
  - Fundamental reforms include raising retirement ages to reflect rapidly increasing longevity and raising contribution rates

health



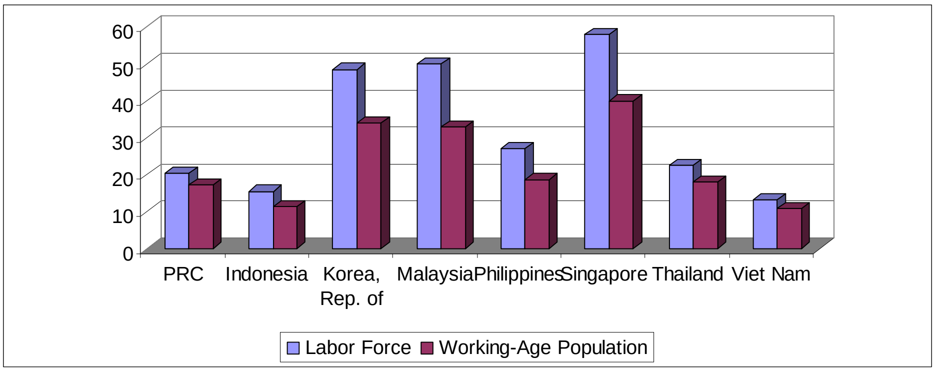
welfare



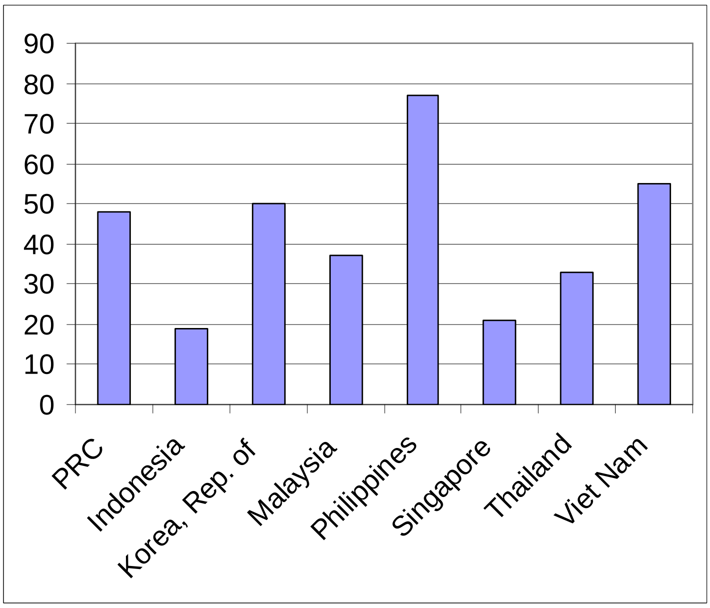
Adequacy

- The biggest failure of Asian pension systems is inadequate coverage - they *cover only a limited part of population*.
  - The share of the labor force which is covered by pension systems ranges from 13.2% to 58%.
  - The coverage rate for working-age population ranges from 10.8% to 40%.
- Asian countries also perform poorly with respect to the replacement rate, or the ratio of retirement income to pre-retirement income.
  - Replacement rate is a widely used measure of the adequacy of pension benefit as a source of post-retirement income.
  - Pension experts generally recommend a replacement rate of between 66 to 75%, adjusted for both longevity and inflation risks.

Share of population and labor force covered by pension system



Replacement rate



Investment returns on pension assets

- Overall, there is significant scope for improvement of the investment returns performance of developing Asia's pension systems
  - In Asia, as elsewhere, realizing higher returns on the assets of pension systems provides a relatively painless avenue for boosting adequacy
- Weak prudential frameworks that fail to inspire public