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Ministry of Finance, Government of Bangladesh**

Global Pension Reforms Need and Approach for Inclusion

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Affiliations

- ▶ World Bank's Strengthening Public Expenditure Management Program
- ▶ Ministry of Finance, Government of Bangladesh
 - Pension Reforms
- ▶ World Pensions Council
 - Research and Development
 - Awareness and Sensitization of Stakeholders on Micro-Pensions



Flow of Presentation

- ▶ Pension Reforms – Backdrop and Concerns
 - Cost and Coverage
 - Ageing Demographics
- ▶ Need for Pension Reforms
 - Objectives and Necessity for Funding
- ▶ Approach to and Type of Pension Reforms
 - Common Themes and Challenges
- ▶ Challenges and Issues with Developing Nations
 - Context of India and Bangladesh
 - Indian Pension Reforms and Inclusion
- ▶ Way Forward



Pension Reforms – Globally

- ▶ Pension Reform is Now a Worldwide Phenomenon
- ▶ Basic Motivations are Similar But Vary With Context
- ▶ Common Approaches Have Emerged But Major Differences In Progress and Results
- ▶ Major Challenges Ahead For All
- ▶ Many Common Themes But Differences Depending On Level Of Development



Backdrop – Most Nations

- ▶ **Public Pensions** – Most important Budgetary Expenditure (rivaling with health / education or defense outlays)
- ▶ **Many Pension Systems in Deficit** and most schemes are **Financially Unsustainable**
- ▶ OECD Countries became **Rich Before Becoming Old**, Most other Countries Risk to become **Old Before Becoming Rich**



- ▶ **Pension's Current Financial Problems**
 - Result of Too High System Dependency Ratio and Too Generous Benefits,
- ▶ **Pension's Future Financial Problems**
 - Demographic Transition; Population Aging; Reduction in Fertility Rate; Increase in life Expectancy; Deterioration in Demographic Dependency Ratio.
- ▶ **Socio- economic Changes; Challenges and Opportunities of Globalization / Urbanization**
- ▶ **Pension Reform is Topical Reform item in all Countries of the World; Likely to Remain so in the Decades to come**



PUBLIC PENSION SPENDING by REGIONS

(as percent of GDP, early or mid 2000)

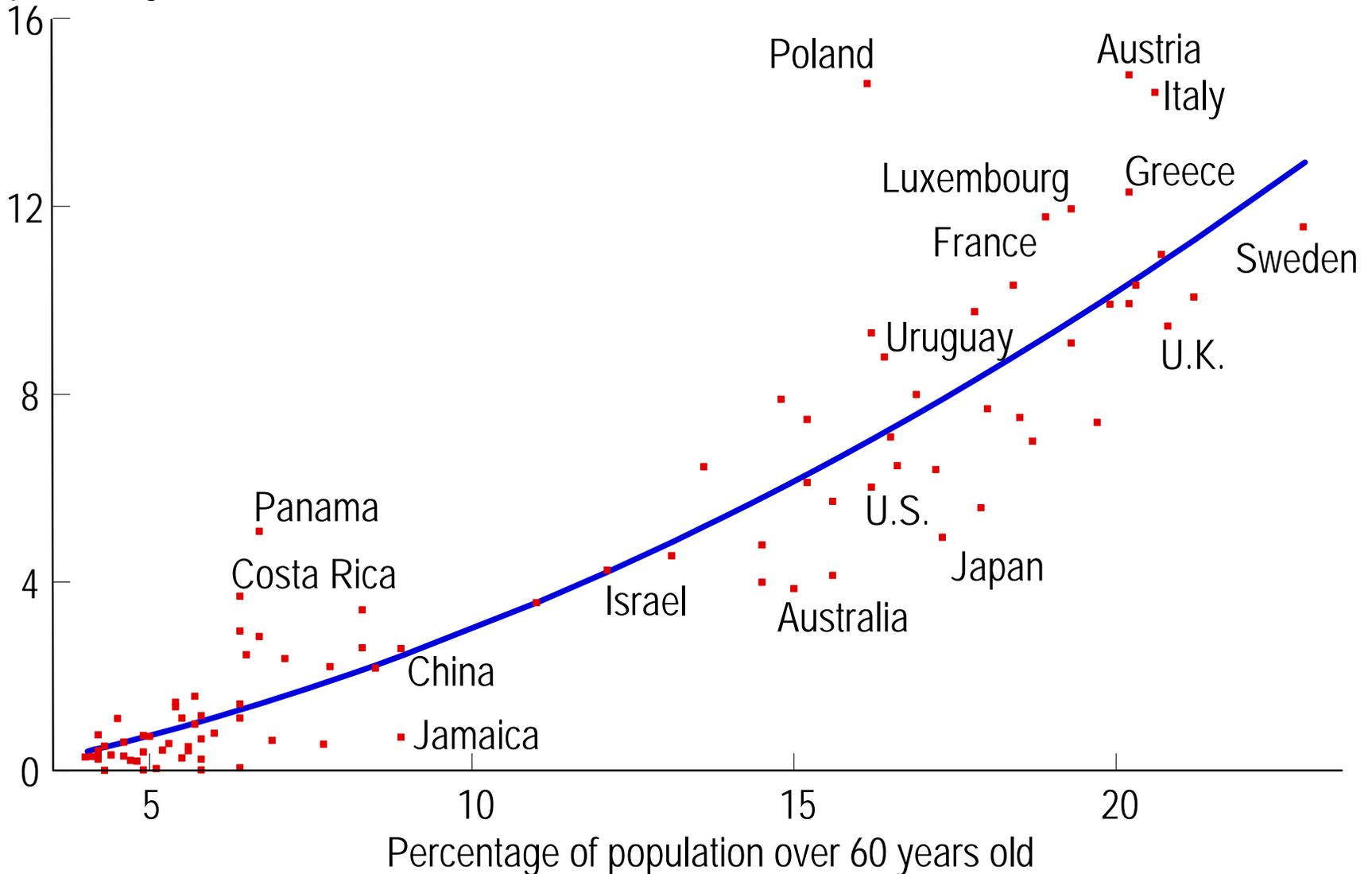
REGION	AVERAGE PENSION EXPENDITURE
OECD	10.5
EUROPE and CENTRAL ASIA	7.3
LATIN AMERICA and the CARIBBEAN	3.6
MIDDLE-EAST and NORTH AFRICA	3.2
ASIA	2.0
SUB-SAHARAN AFRICA	0.7

Implicit Pension Debt

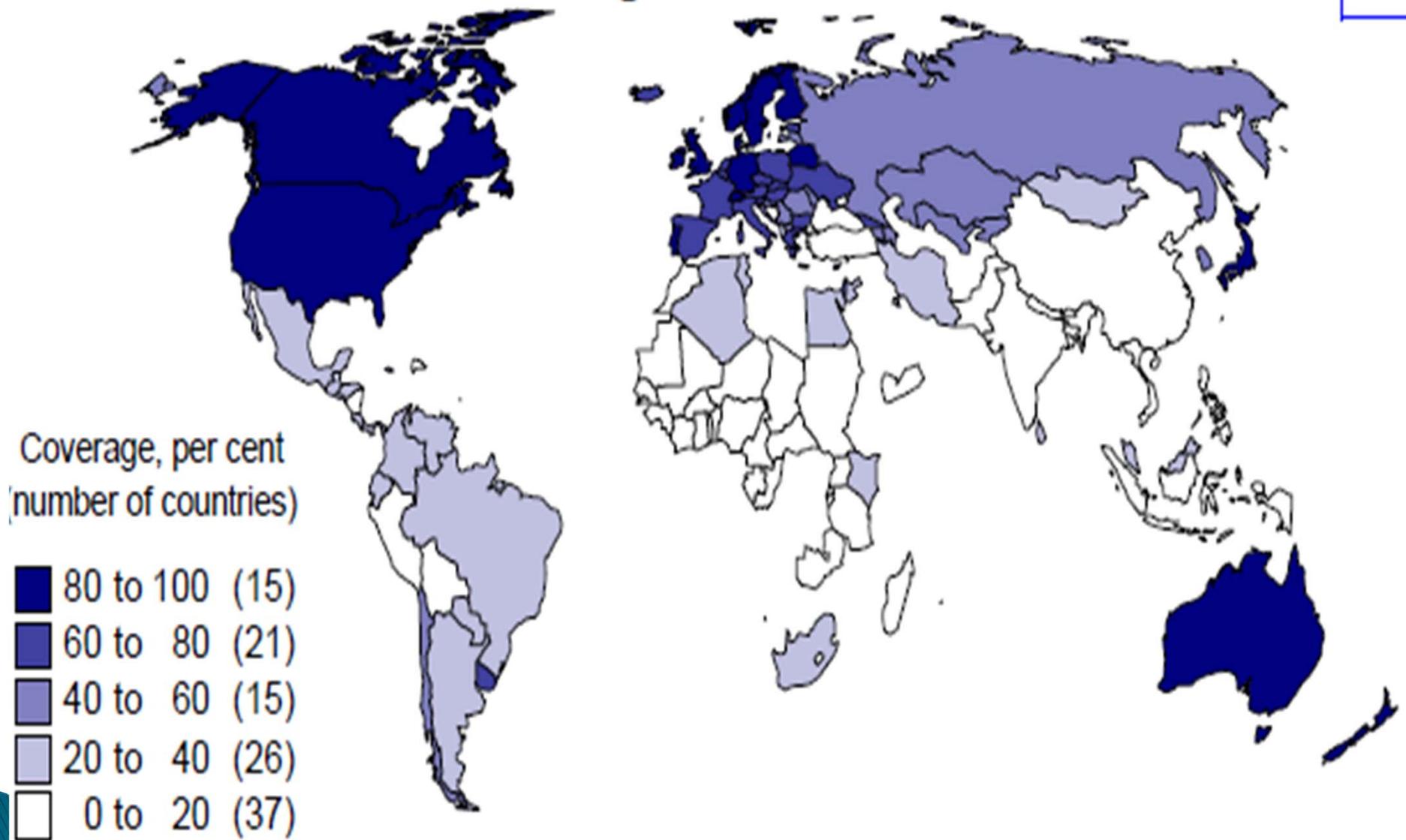
		Implicit pension debt (% of GDP)		Current spending (% of GDP)		Coverage (% of labor force)		IPD/coverage	
		Civil service	National	Civil service	National	Civil service	National	Civil service	National
Brazil	1998	92	284	1.7	6.2	2	27	46.0	10.5
Iran	2001	38	64	0.5	0.7	8	32	4.1	2.0
Korea	1995	7	33	0.2	0.3	1	23	7.0	1.4
Philippines	1997	17	90	0.2	0.8	3	40	5.7	2.3
Turkey	1997	75	71	1.7	2.5	5	25	15.0	2.8

Relationship Between Percentage of the Population over 60 Years Old and Public Pension Spending

Pension spending as percentage of GDP



Pension coverage around the world



Note: 'missing' countries indicate data unavailable.

Source: ILO, World Bank

Pension Systems Coverage

	Percent of labour force
OECD countries	83.3
East Asia	44
Latin America	32
Middle East/North Africa	34
South Asia	13

	Percent of population 15-65 yrs	Percent of labor force
China	17.2	20.5
Indonesia	11.3	15.5
Philippines	18.7	27.1
Thailand	18.0	22.5
Vietnam	10.8	13.2
India	5.7	9.1
Pakistan	4.0	6.4
Sri Lanka	22.2	35.6

Source: OECD (2009)

Population Ageing: A Global Phenomenon

	Growth rates of population 60 and over	
	2000-2005	2045-2050
More developed regions	1.9	0.4
Less developed regions	3.0	2.1
Least developed regions	2.9	3.5

	Developed countries		Developing countries	
	Present	In 2050	Present	In 2050
Population aged over 60	Over 20%	33%	8%	20%

	Median age	
	2009	2050
More developed regions	40	46
Less developed regions	26	37
Least developed regions	20	29

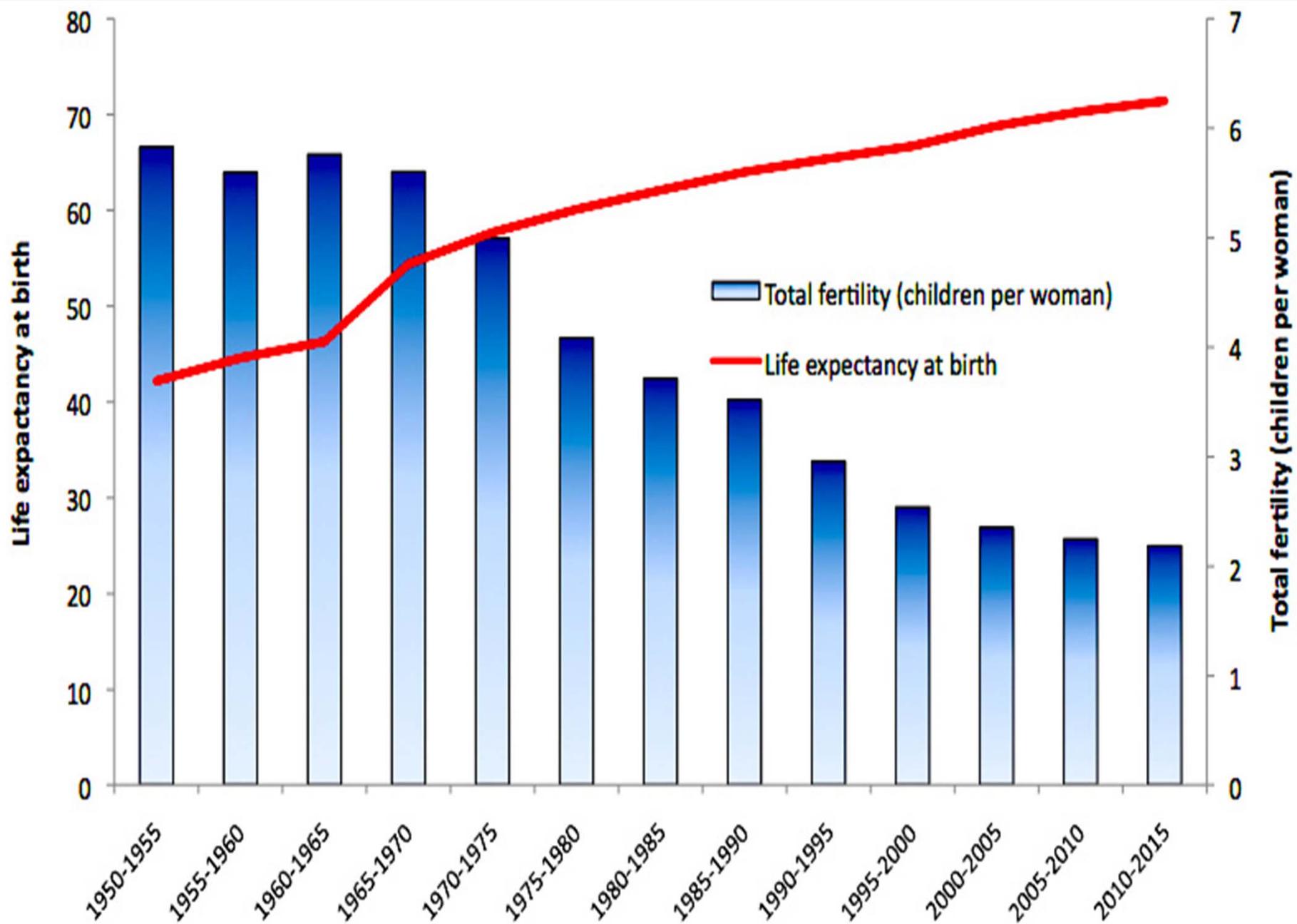
Source: World population ageing - UN forecasts

Potential Support Ratio

	Potential support ratio		
	1950	In 2007	2050
Number of workers per older persons	12	9	4

	2000	2025
South Asia		
Afghanistan	18.9	17.8
Bangladesh	18.6	12.9
Bhutan	12.5	12.4
India	12.4	8.2
Maldives	15.0	15.0
Nepal	14.8	13.6
Pakistan	14.8	12.7
Sri Lanka	10.8	5.5

Source: United Nations (2002), *World Population Ageing: 1950-2050*, New York (2002)



Source: United Nations, Department of Economic and Social Affairs, Population Division (2013). World Population Prospects: The 2012 Revision, CD-ROM Edition.

Objectives

- ▶ **Primary Objective: Ensuring Older People have a Decent Standard of Living**
 - ‘Adequacy’: ensuring Basic Standard of Living
 - ‘Insurance’: ensuring a Decent Replacement Rates
- ▶ **Secondary objectives**
 - Capital Markets – Institutional Development; encourage national savings
 - Labour markets – Retirement Decisions; restructuring
 - Public Finances – Providing funds for Socially / Economically Targeted Investments



Necessity to Develop Funded Pension and Insurance Products

- ▶ As Dependency Ratios Worsen, Fewer Workers to Support the Growing Number of the Elderly
- ▶ Traditional Family Support for the Elderly Weaken:
 - Increased Youth Mobility + Increased Migration + Rapid Industrialization and Urbanization
 - Increased Life Expectancy
- ▶ Public social security systems exist only in a few developing countries and are often **Inefficient**



Approach to Reforms

- ▶ A long-term, credible commitment by the government
 - Aligned with Political economy; Clear Political Mandate; Stable Political Conditions
- ▶ Local buy-in and leadership.
 - Credibility with Population
- ▶ Sufficient capacity-building and support for implementation arrangements
 - Reforms in Governance; Contribution Collections; Recordkeeping; Client Information; Asset Management; Distribution; Regulation & Supervision



Types of Reforms

- ▶ Systemic – Change in System itself (DB to DC)
- ▶ Parametric – Change terms of existing System e.g PAYGO
 - Reduction of public generosity / New benefit formula
 - Partial pre-funding of PAYG system (Ireland, New Zealand)
 - Enhanced reliance on tax-sponsored individual savings plans
- ▶ Transformational – PAYGO DB to DC
 - Repaying the implicit debt
 - Financial infrastructure and regulatory capacity
 - Financial market fluctuations and risk
- ▶ Privatization
- ▶ Pre-funding
- ▶ Diversification – Additional Pillars
 - Separating redistribution and income replacement
 - Risk diversification and reducing transition costs
 - Reform externalities on labor and financial market

Parametric Reforms

- ▶ Majority of Pension Reforms Involved DB
 - ▶ Countries frequently adjust Parameters:
 - 1995–2005, 18 Countries Increased the Retirement Age; 57 Increased Contribution Rates; 28 Modified Benefit Formulas; 10 Changed Vesting Periods; and 14 Changed the Contributory Base and/or Indexation Mechanisms.
 - MENA Region (2000–2005) All Countries Introduced some type of Adjustment – Not Always for the Best.
 - ▶ Adjustments, tend to be Ad-hoc or Discretionary:
 - ▶ Usually Fiscal Problem is the Motivation.
 - ▶ Policy Makers and Stakeholders Negotiate which Parameters can be Changed.
 - ▶ Linkages between the various parameters / choices are ignored.
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Common Themes in Reforms

- ▶ Linkages to Lifetime Contributions
- ▶ Higher Retirement Age and a Reduction in Special Categories
- ▶ Use of Payroll Deductions to Ease Cost on Points of Service
- ▶ Maintenance of CRA at Organizational Level v/s National Level
- ▶ Funding and Diversification of Assets
- ▶ Private v/s Public Management of Funds
- ▶ Switch over to a DC Plan
- ▶ Greater Individual Responsibility
- ▶ Risks with Convergence of Employers role
- ▶ Building up of IT Infrastructure and Upgrading of Regulatory Capacity of the Institutions

Design Principles

- ▶ **Adequacy**
 - Enough money to Save and Survive
- ▶ **Self-financing and Sustainable**
 - Benefits should be financed wholly from contribution revenues without support from the central budget
- ▶ **Safety, Security and Regulations**
 - Pensions Promises be Sustainable and Affordable
 - Pensions are protected against Inflation
- ▶ **Transparent and Predictable**
 - Know what U Expect in Retirement Income
- ▶ **Efficient, Portable and Motivational**
 - Administration is Effective and Costs are Low
 - Incentives to Work, Enroll and Save



Challenges Ahead

- ▶ Developing Efficient Payout Systems
- ▶ Reaching lower to middle income groups
- ▶ Allocation of risks between public and private
- ▶ Capacity of individuals to exercise responsibility
- ▶ Flexible Retirement Incentives
- ▶ Employment Transition & Preservation
- ▶ Addition of Asset Classes
 - (e.g. Real Estate, Private Equity, Derivatives)
- ▶ Portfolio Choice Within Plans
- ▶ Financial Literacy and Rational Behavior

Issues in Developing Nations

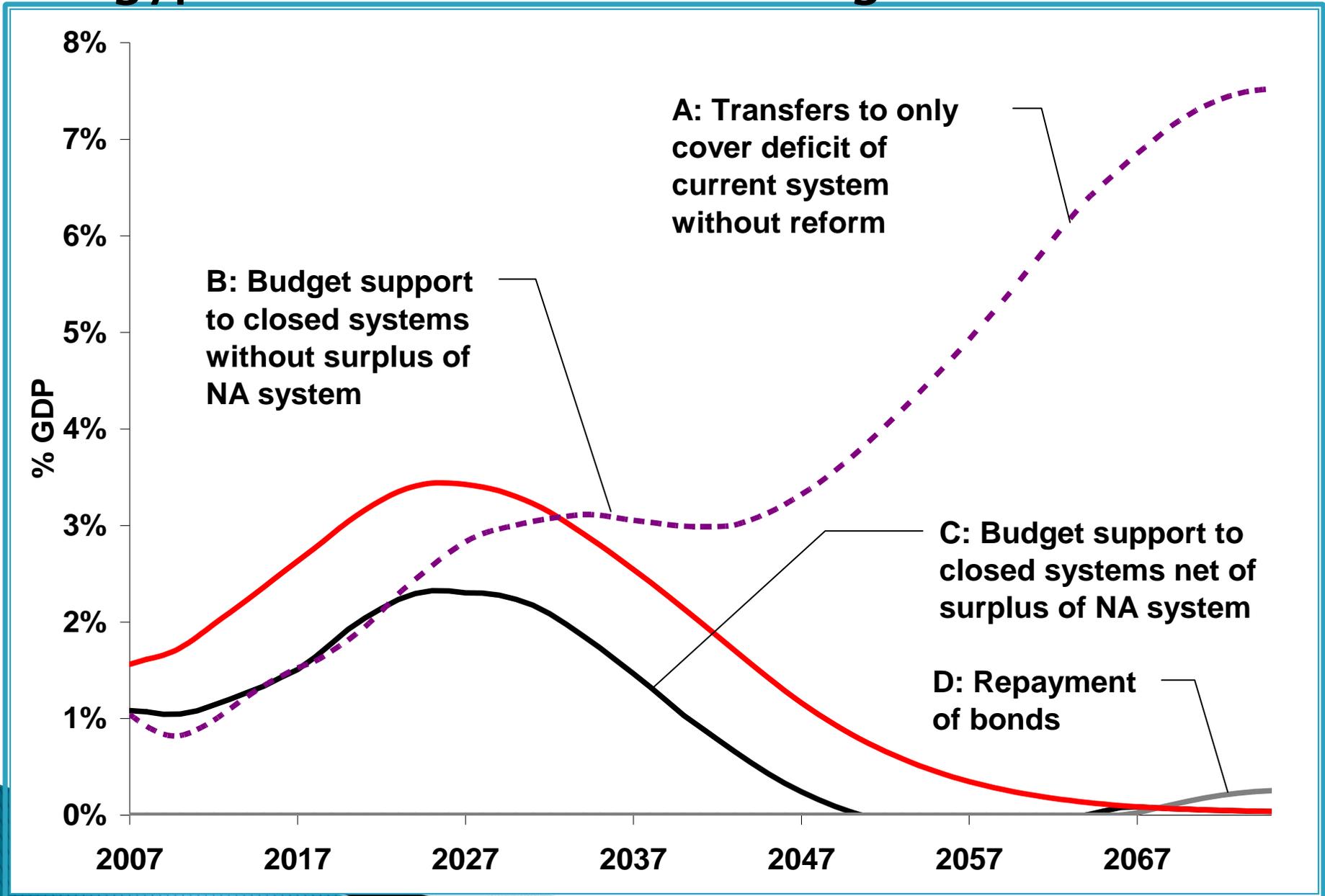
- ▶ Reaching low income and informal sectors
 - Delivery Infrastructure & Account Administration
 - High Cost of Collections and Individual Accounts
- ▶ Creating Domestic Investment Markets (chicken and egg problem)
- ▶ Diversified Domestic Portfolios
- ▶ International Diversification



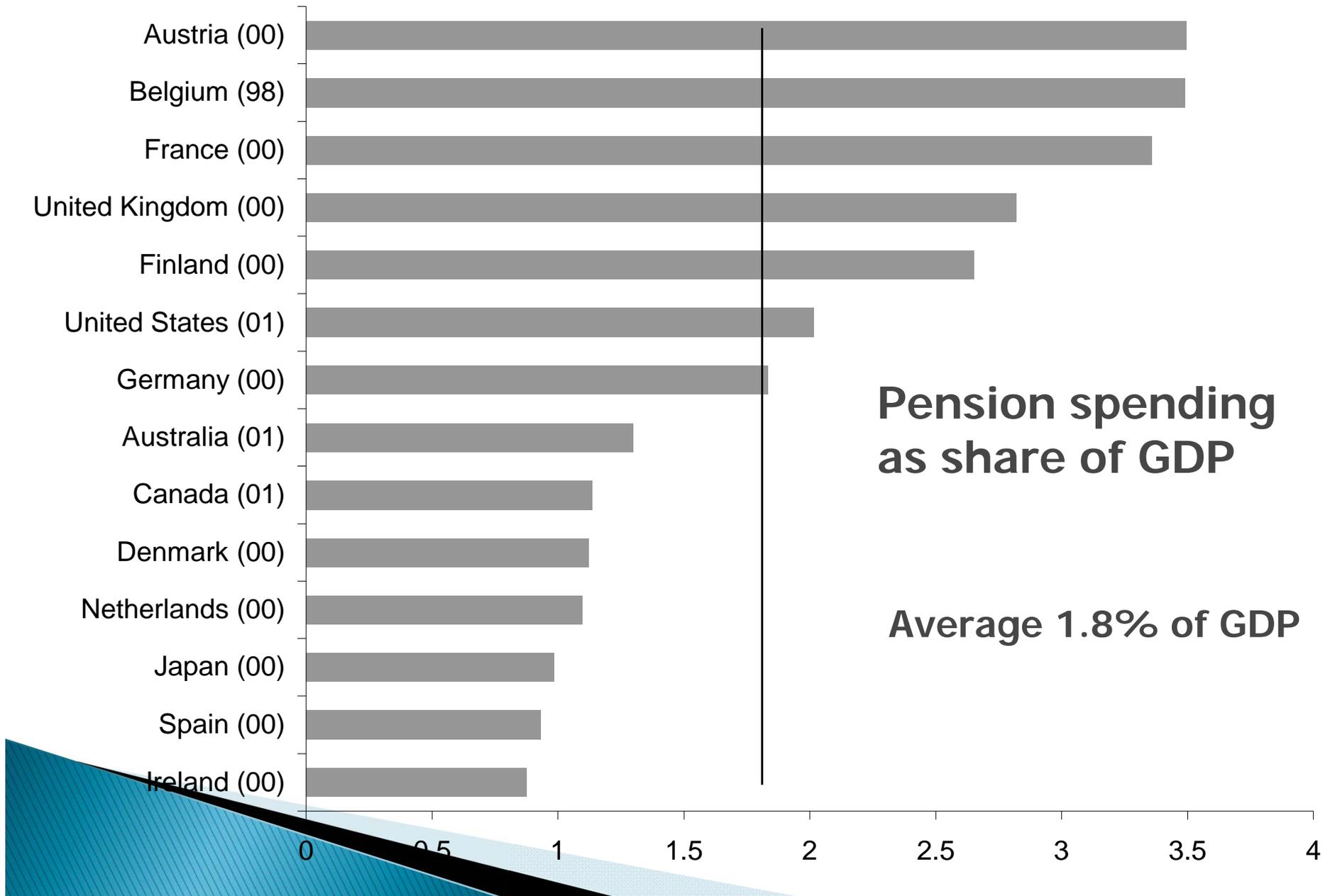
Issues in Developing Nations

- ▶ Reforming Civil Servants Schemes
 - Creating Realistic Expectations
 - Understanding the Need
 - Participatory Reforms
 - Employees Confidence
- ▶ Conversion of Severance Arrangements to Retirement Savings
 - Early Retirement
 - Job Mobility
- ▶ Efficient Investment of Existing Provident Funds

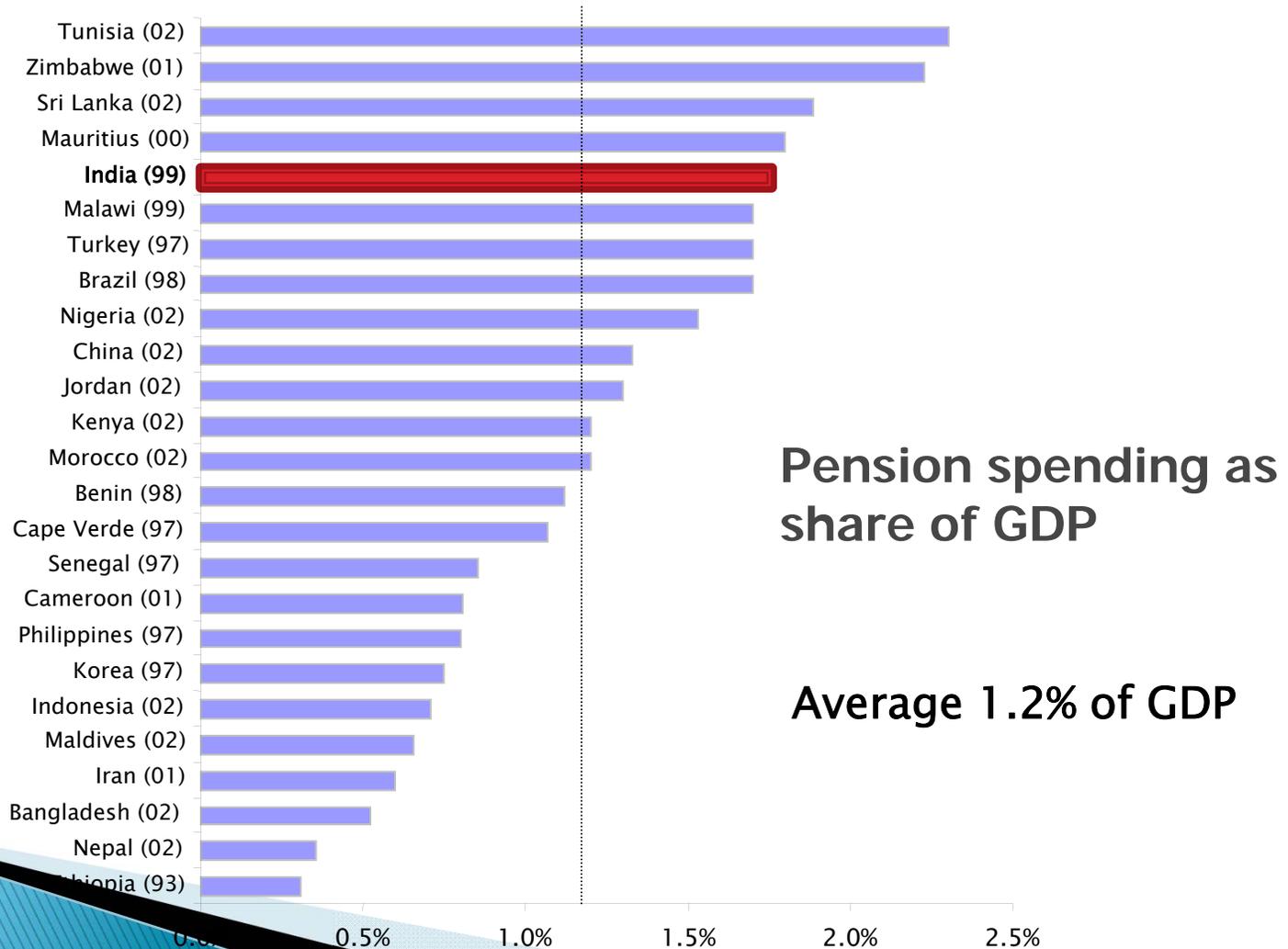
Egypt: Cash Flow Smoothing Curve

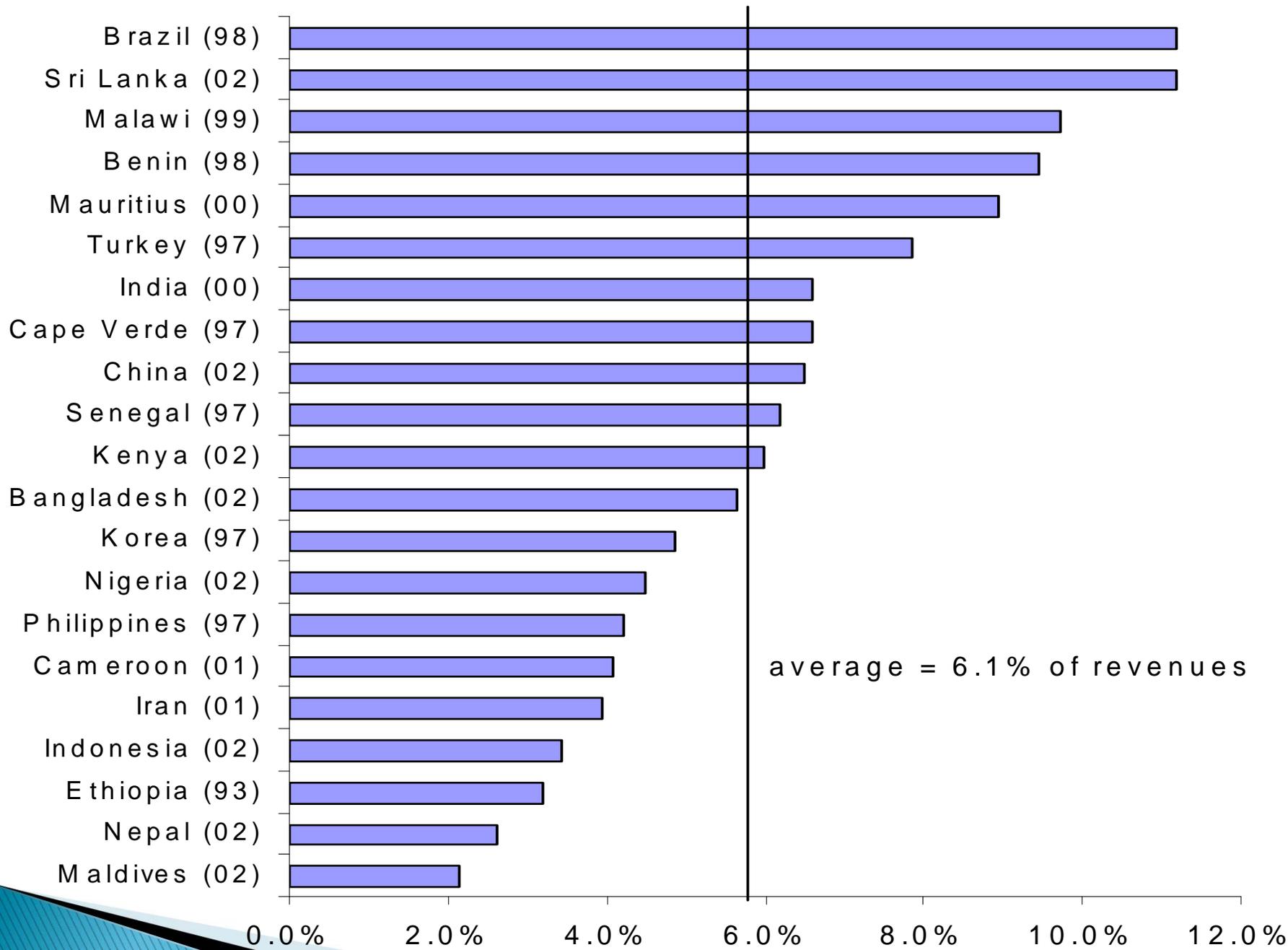


Fiscal Burden in OECD

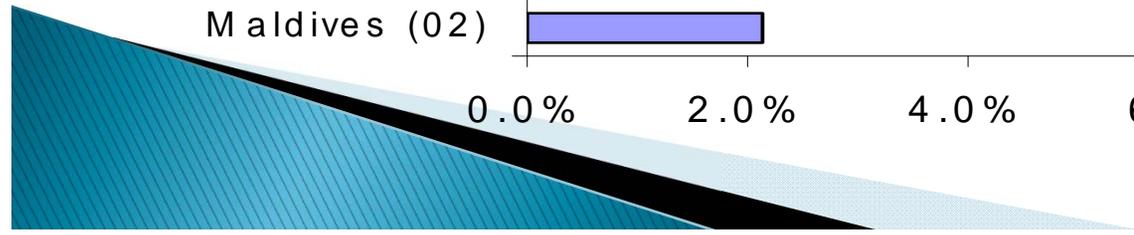


Fiscal Burden in Low & Middle Income Countries





average = 6.1% of revenues



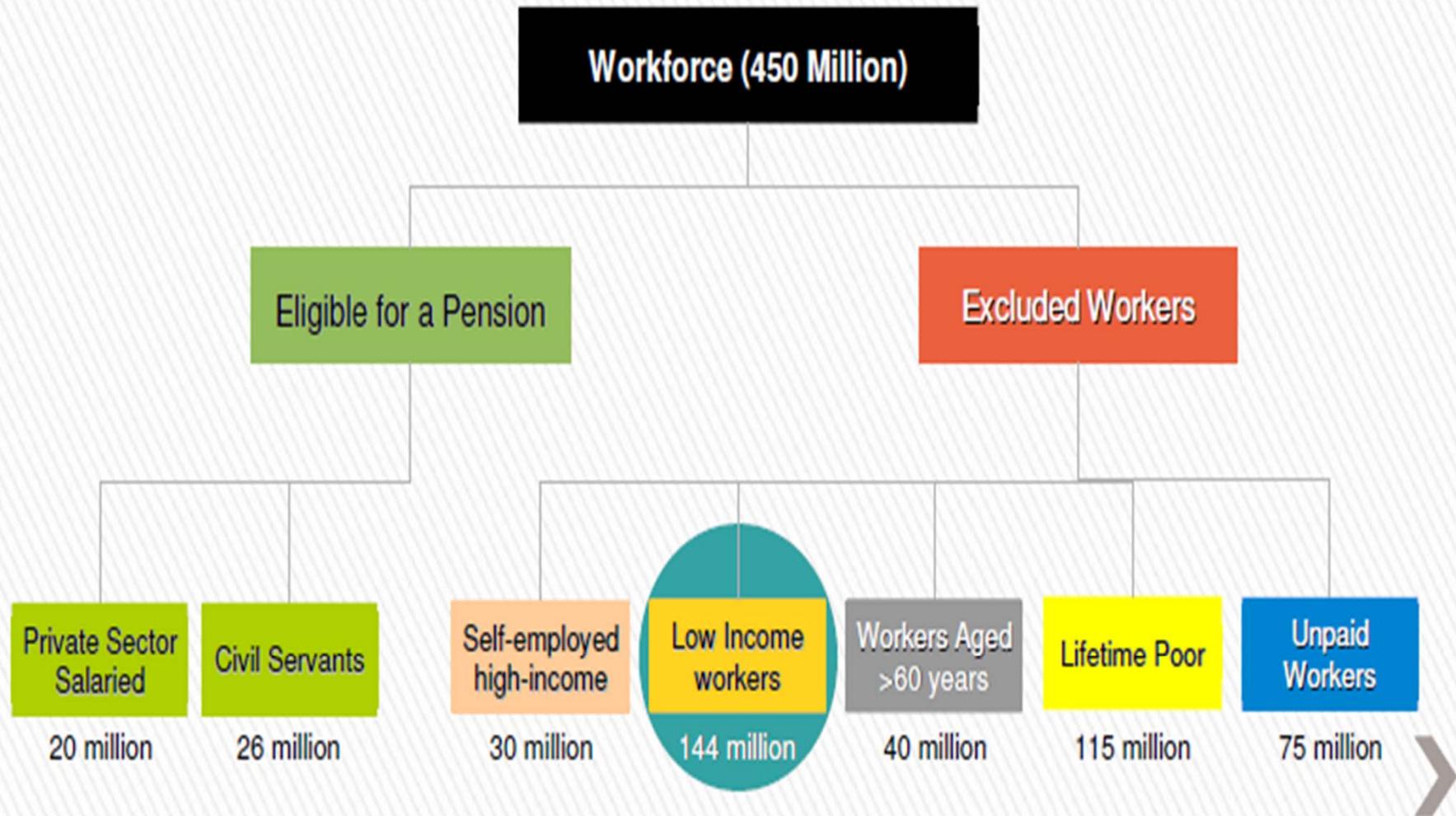
Approach for An Inclusive Pension Lessons from India

INDIA'S PENSION COVERAGE GAP



-  Excluded informal workers who can save for old age
-  Unpaid workers
-  Lifetime poor
-  Formal sector workers with pension benefits

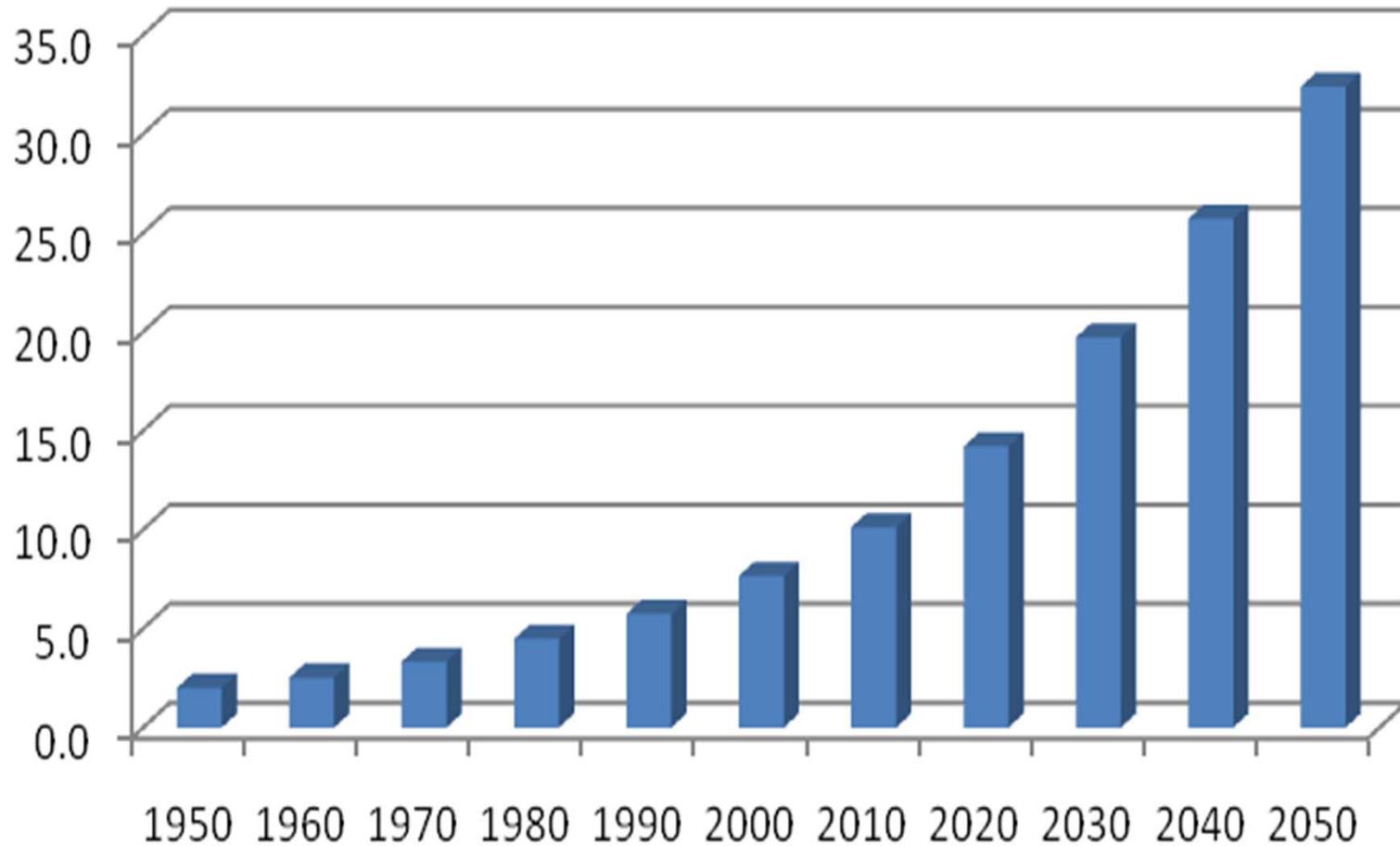
India's Pension Coverage Gap



Sources: *Indian Retirement, Earnings and Savings Survey*, Indian Ministry of Finance and *Invest India Incomes and Savings Survey, 2007*

Growing the Micro Pension Market | UTI-IIMPS 2011

Population of 60+ in Crores



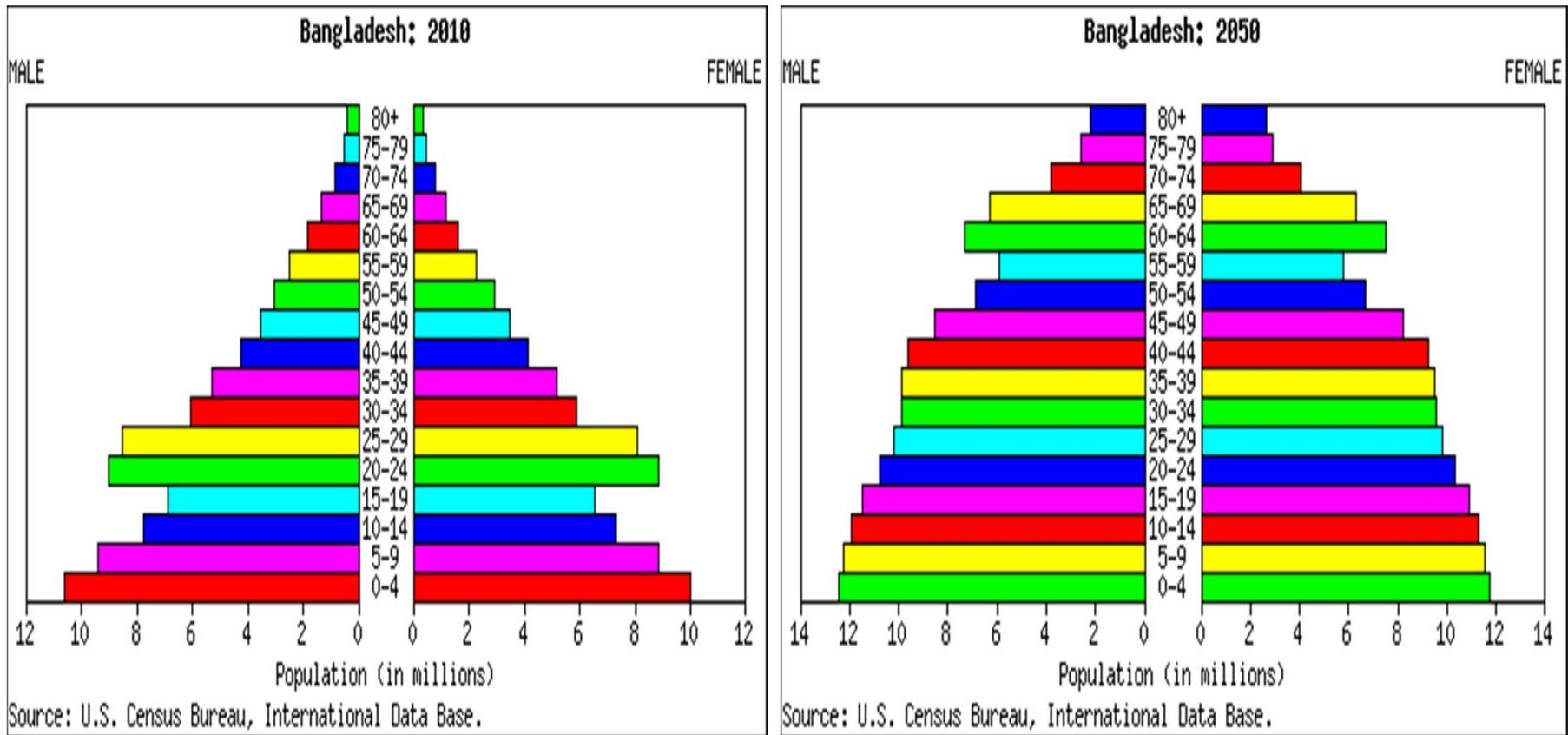
Compulsions for Bangladesh



Fiscal Cost of Social Pension
2010

Fiscal Cost of Social Pensio
2025

Bangladesh's Population Pyramids



The ADB estimates one in four women in Bangladesh will be widowed or divorced by the age of 50.

By 2025, 60+ population expected to be 9% at 18 million, from a current estimate of 6%, ie 9 million

Micro Pension Model Evolution Since 2006

- ▶ 2006: Sewa Bank Pilot with 25000 Women Saving a Dollar a Month Without Support from Government
 - Lobbying with State Governments and Civil Societies
 - ▶ 2008: First Co Contributory Pension Scheme for 20 Identified category of Informal Sector Workers by Government of Rajasthan
 - Lobbying with Ministry of Finance, Government of India
 - ▶ 2009: National Pension System Informal Sector
 - ▶ 2010: Pan India Announcement of 'Swawlamban'
 - NPS Lite for Informal Sector
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Initial Conditions

- ▶ Informal Sector Spread 3.3mn sq. kms.
 - ▶ Low intermittent incomes, potentially tiny contributions and modest balances highly sensitive to transaction costs
 - ▶ Frequent mobility across jobs and locations
 - ▶ Low literacy and low financial literacy
 - ▶ Limited formal finance usage and penetration
 - ▶ Rapidly improving life expectancy – almost at OECD levels
 - ▶ Breakdown of the joint family
 - ▶ Limited fiscal capacity to deliver meaningful, population-wide, tax-funded social assistance
 - ▶ Tax incentives will not produce voluntary coverage
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Micro-Pension[®] Model Components



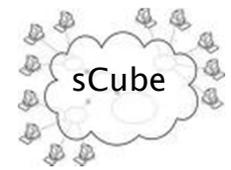
SDP

Customers

Open Bank A/c;
Deposit savings in
A/c

BC

Periodic SI
by IIMPS



Customer
HelpLine



Central
Data
Processin
g
Hub



Research &
Development



Audit

Pre-enrollment and ongoing education, enrollments, document processing, processing of NCTs, SI reminders and statements delivery

BCs provide banking access; Bank partners implement SI and transfer aggregated funds to UTI / PFMs

Implementation support, IEC, operations, reconciliation, IT, data & transaction processing, Helpline, Audits, and R&D



MPF Designed Card Based Collection Model



- Near Zero Capex
- Tangibility
- Real time transactions
- Automatic reconciliations
- Flexibility
- Convenience
- Secure



- Portable
- Affordable

Challenges and Issues In Designing and Implementing Micro Pensions



Pension Literacy

- ▶ **Latent Need into Demand for Micro Pension**
 - ▶ **Concept of Pension Conspicuously Missing**
 - Concept Seeding amongst Daily Wage Earners who live on Hand to Mouth
 - Lower Level of Literacy, Pension Literacy and Banking Habits
 - Behavioral Changes in Savings Pattern
 - Constant Motivation Towards Regular Contributions even after Co Contributions
 - ▶ **Reckoning the Challenges:**
 - Interactive Sessions with Potential Groups / Members
 - Direct Communication, Realization and Awareness Creation on Old Age Issues / Dependence / Longevity / Health Issues / Importance of Savings for Old Age
- 

- ▶ **Issues on KYC and Bank Accounts**
 - Dovetail with Financial Inclusion Drive of Government / Banks
- ▶ **Extensive Use of Information Education Communication (IEC) Tools and Techniques**
 - Well Researched IEC Tools / Flyers / FAQs / Calculators / Skits / Films etc.









Product Design

Suitable for Low Income Informal Sector Workers

- ▶ Simple to Understand, Fair and Transparent in Costing as well as Investment
- ▶ Regulated Product and Processes at the Backend
- ▶ Co Contributions
 - Tax Equity
 - Sense to prefunded with lower contributions
- ▶ Sustainable and Portable
- ▶ Pure Pension: Co Contributions for initial few years using CCTs But Locked till Retirement
- ▶ Provident Fund: Liquidity for Partial Withdrawals under certain Exit Loads



▶ **Product Related Challenges**

- Complexity of Product at Accumulation and Withdrawal Stage
- Lobbying with Governments on Co Contributions
- Risk and Returns in the Product itself
- Regulated Long Term (Locked) for Old Age and Medium Term (Liquidity) Combo Product
- Inflation Hedging by Increasing Contribution

▶ **Sustainability and Portability Challenges**

- Labor Market Movement / Migration
- Sustainability of Agencies / NGOs



Process Design

- ▶ Education and Enrollment Delivered through Workers at Grass-root Level
- ▶ Education led Banking Model using No Frill / Savings Bank Account for Transfer of Periodic Contributions
- ▶ Cashless fraud free environment
- ▶ Backend Central Processing Unit for Centralized Processing
- ▶ Transfer of Contributions to Respective Fund Managers
- ▶ Delivery of Welcome Kit, Statement of Accounts and Non Commercial Transactions



Way Forward on WPC Forum

- ▶ Research and Development
- ▶ Pension for Bottom Billions
 - <http://www.efinancialnews.com/story/2013-11-18/pensions-for-the-poorest-countries>
- ▶ Sensitization of Stakeholders
 - Donor Agencies / Funders / Governments / Ministries / Civil Societies / NGOs / Trade Unions
 - Capacity Building and Training
- ▶ Fund Management Issues
 - Create Common Pool of Resources under IMF / UNDP / WB / ADB Supervision
 - Allow 50% Investment Outside Country

Are you saving for your old age?

Thanks Q & A



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