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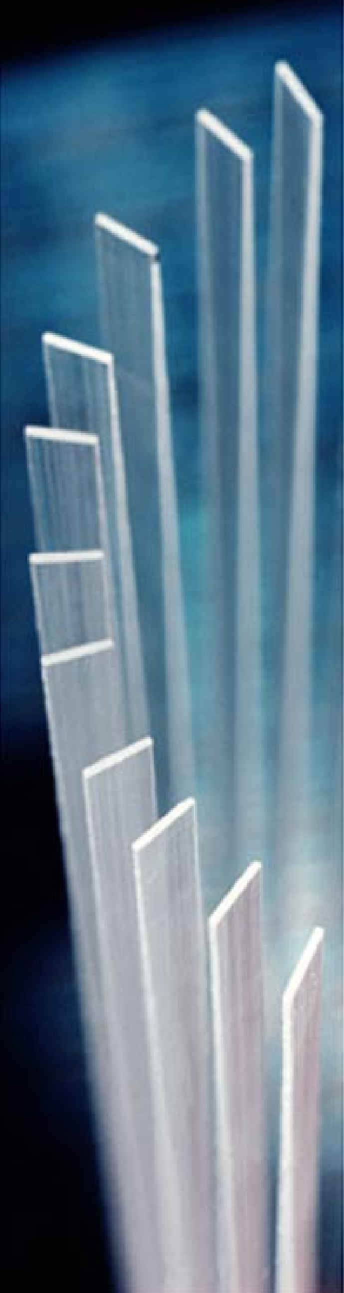
27th International Congress of Actuaries

- Social Security Committee



"Pension Reform in China"

BY

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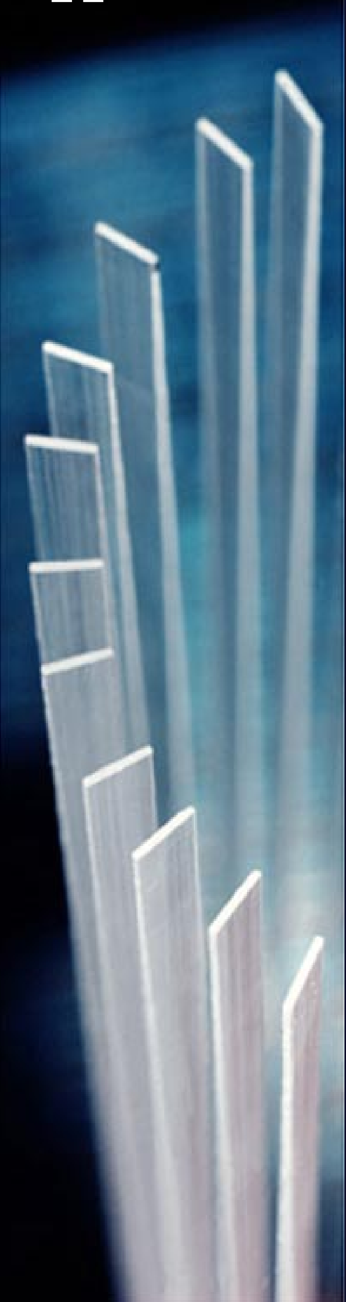

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Map of China

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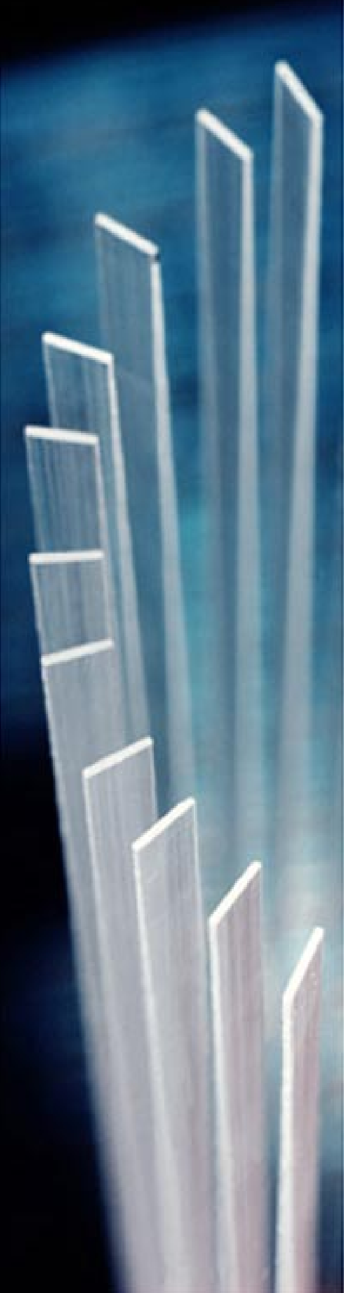


PRC Population

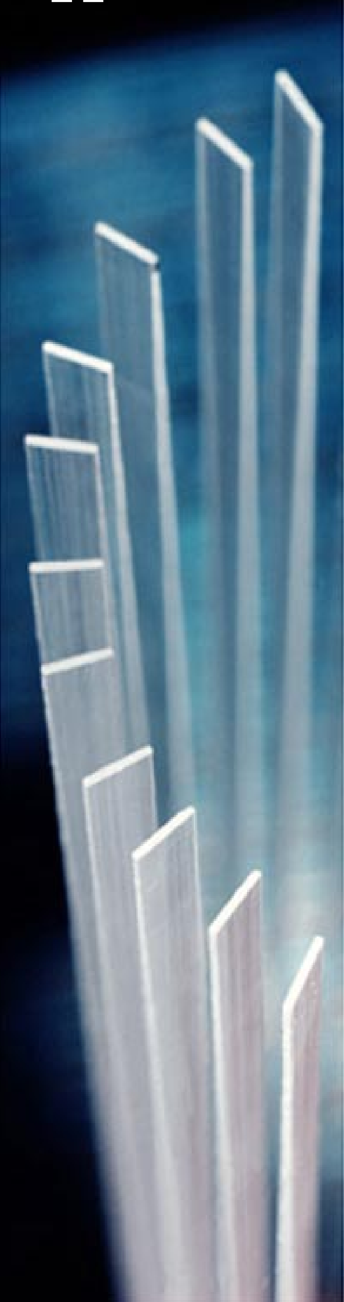
Total:	**Almost 1.3 billion**
Rural Population:	**900 million**
+	**+**
Urban Population	**400 million**

Ages:

0-14	**100 million**
15-64	**275 million**
65+	**25 million**

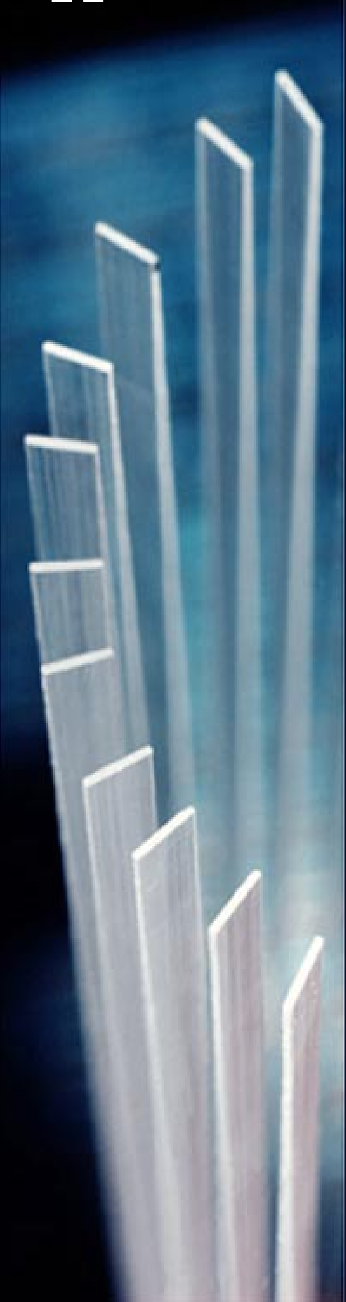
Consider:

- **One Child Policy**
- **Greatly improved life expectancy**
- **Dependency Ratio deteriorating rapidly**



Old System ('Iron Rice Bowl')

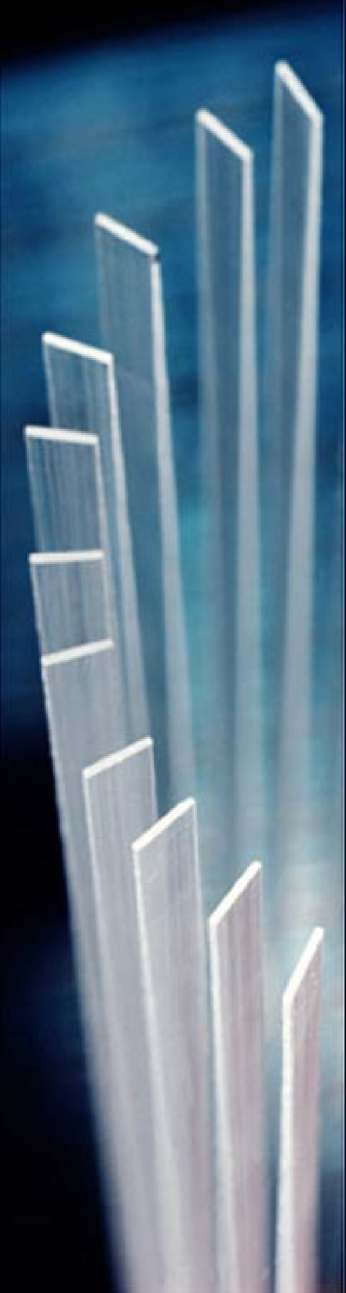
- **Workers employed for life by State Owned Enterprises (SOE)**
- **Low Wages but Total Security**
- **Pension at 60 (Males) or 55 (Females) = 80% of final salary**
- **Pensions paid by SOEs**
- **No Pre-funding or Reserves (i.e. pay-as-you-go), but what if SOEs unable to pay pensions?**
- **China is very concerned about social unrest resulting from unpaid pensions and the unemployed**



World Bank

- In early 1990s, World Bank studied how best to solve pension issues in China

- World Bank suggested a three pillar approach
  - Government run basic pension
  - Privately run individual accounts
  - Voluntary employer/individual savings



Pension Principles for Future

- Reduce pension expectations
- Cost burden to be shared by employer and employee
- Move towards pre-funding

Reasons?

- Population projections
- SOE restructuring
- Develop domestic capital markets

New System (‘Safety Net’)

- New Unified Pension System Reform (July 1997)
- Expand coverage to all urban employees
- Gradually raise retirement age (to 65 years for men & women)

Benefits

- Pillar I = Basic Pension of 20% of average provincial wages
- Pillar II = Individual account based on 11% contributions
- Pillar III = Voluntary Supplementary Benefits

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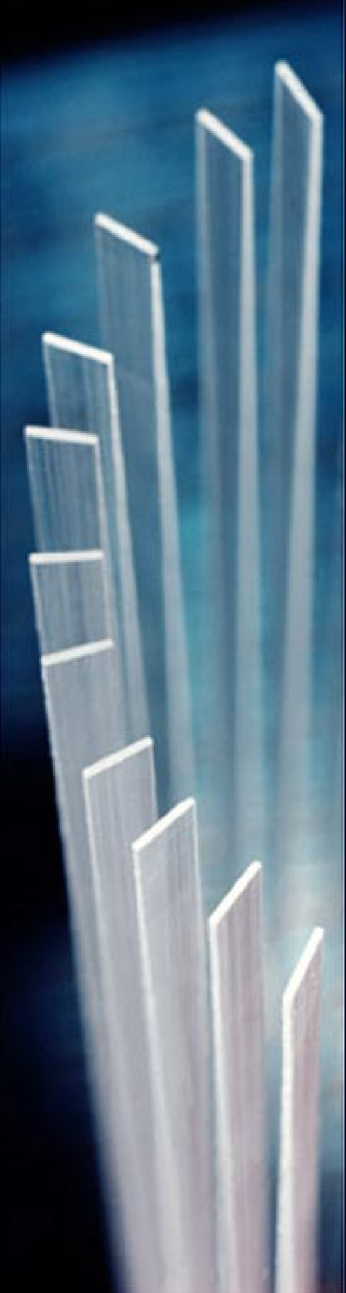

Financing

- **Employee** = 4% salary contribution

  increasing by 1% every 2 years up to 8%

- **Employer** = Approx 20% of salary contribution

  (Subject to salary maximum and local variation)

Pension Assets

- Pillar I and II pension assets approximately RMB 125bn, (US$15bn) in government bonds and deposits, managed by Social Security Bureaus; however not enough for future obligations

- Pillar III pension assets managed by insurance companies; fully funded schemes

- The government is considering several initiatives to meet the pensions shortfall

    - Special taxes
    - Lottery
    - Issue of recognition bonds
    - Sale of State owned assets
    - Launch of Chinese Tracker Fund

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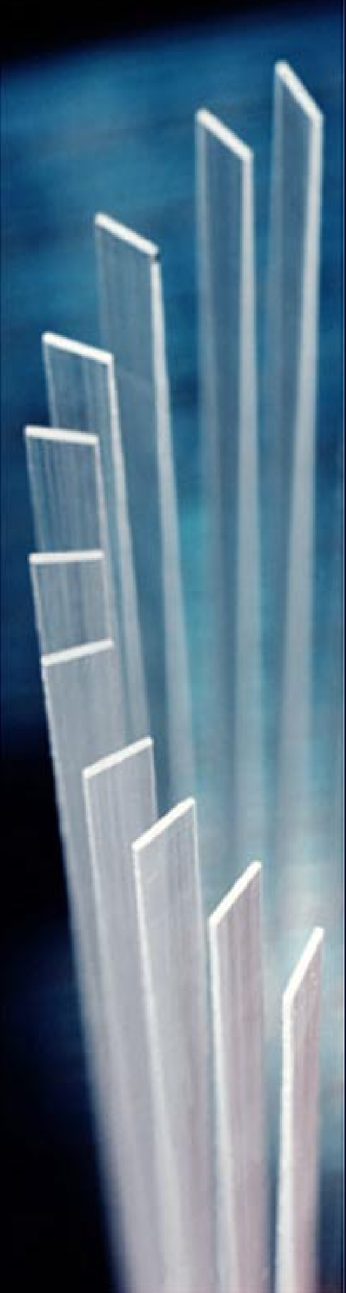
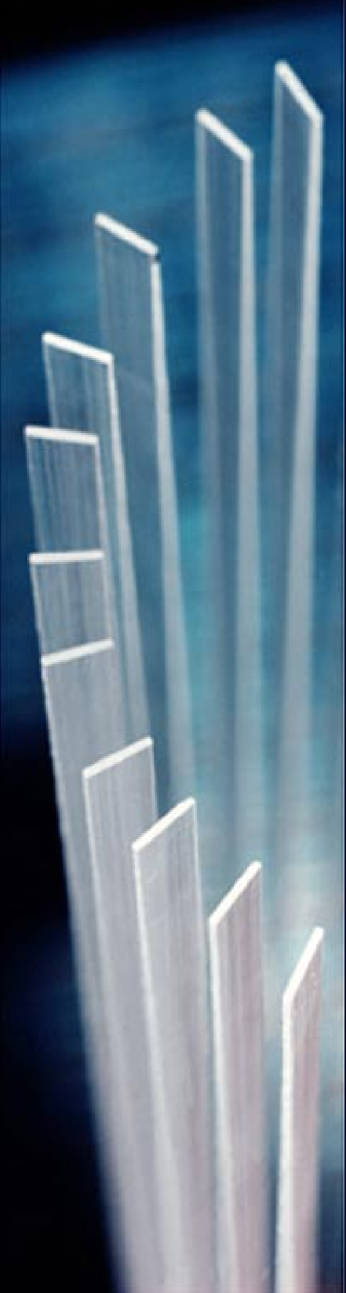


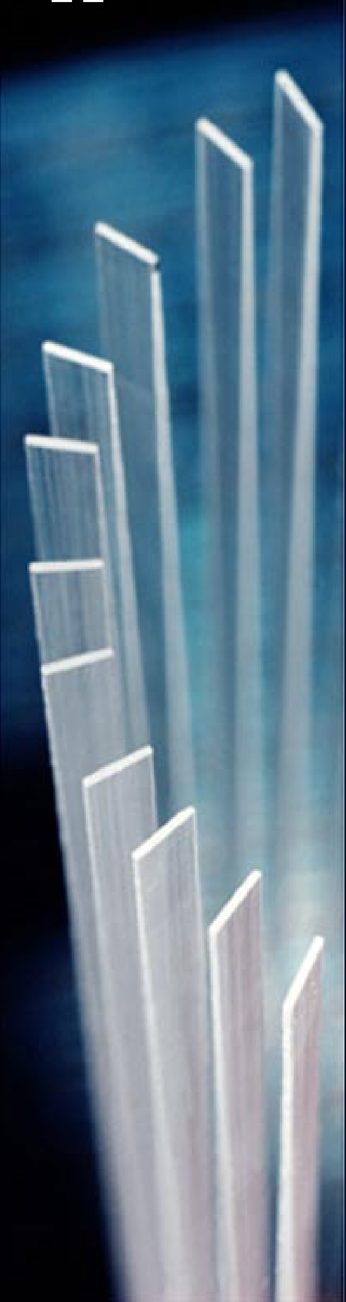
Develop Capital Markets

- SOEs to be restructured: 1,000 – 2,000
- Merge, close, downsize or corporatize
- List on Stock Market through A shares?
- How much capital is required in the next 5 years? 10 years?
- How to apply pension assets to capital markets and maximize returns (deposits + bonds + equities + mutual funds + real estate + infrastructure)
- World Bank estimates pension assets of US$1.8 trillion by 2030



Implementation Issues

- Compliance
- Administration
- Preservation
- Portability
- Transitional issues
- Education
- Taxation

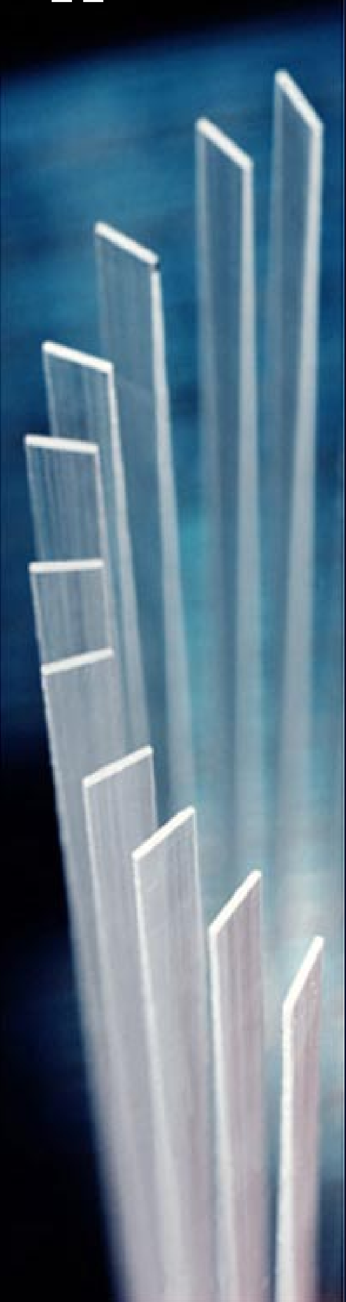


National Social Security Fund

- In the event that some provinces have insufficient funds for Pillars I & II, the State Council has established a “fund of last resort”
- National Council for Social Security Fund to act as Trustees
- Income: State Shares equal to 10% of IPO’s
- Investment Management: will appoint external managers
- Outgo: to be decided

Liaoning Experiment

- Liaoning – industrial province in north east
- Very serious funding problems
- Document 42 (July 2001)
- Basic pension – 30% of local average earnings
- Individual account
  - Employees' contributions only (8%)
  - Must be properly funded
- Major problem of back funding to be solved

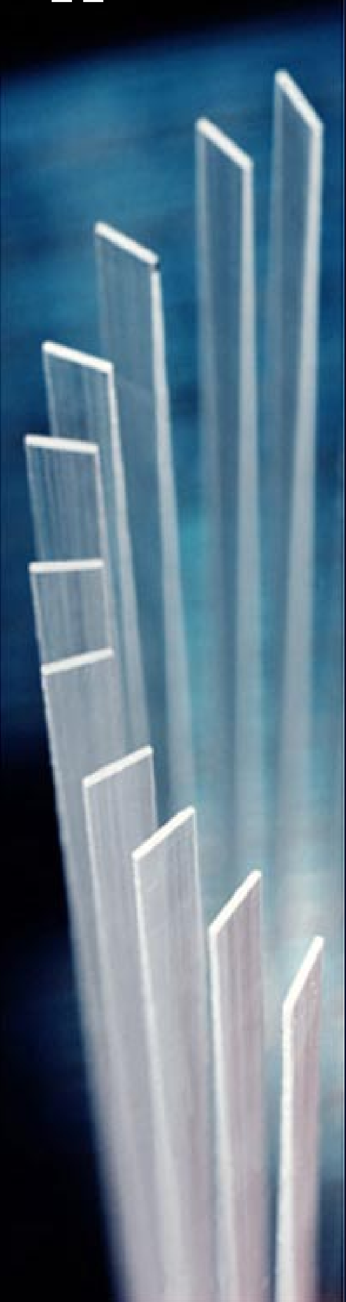


Supplementary Pension Plans

- Employer sponsored retirement schemes: Group pensions through domestic life companies
- "Enterprise annuity" proposals by MLSS
- SPPs to be offered by entities licensed by Ministry of Labour and Social Security
- Tax concessions likely to encourage SPPs
- By 2005 international insurers can write group business

Opportunities for Fund Managers

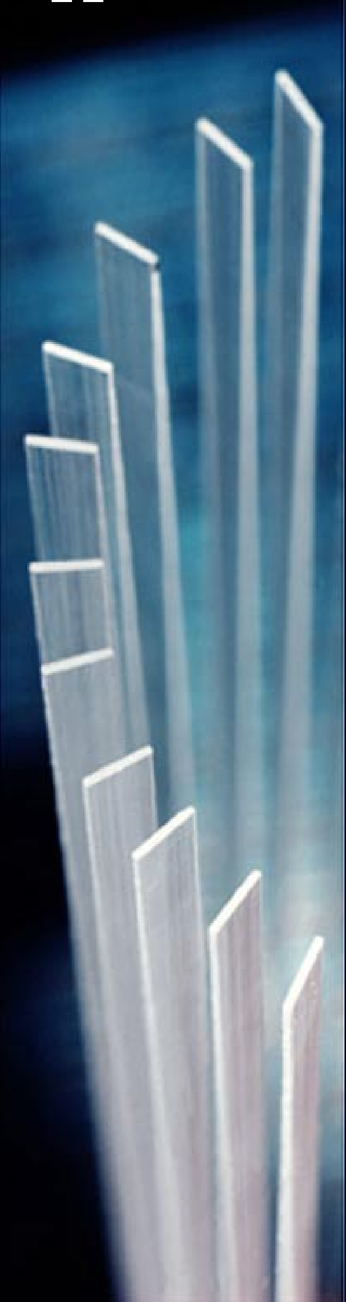
- Pillar I; No
- Pillar II;
  - Short term – No;
  - Medium Term – Outsourcing by Social Security Bureaus;
  - Long-term – 401(k) plans?
- Pillar III; Via Insurance Companies;
  - Later segregated funds?
- National Social Security Fund; Possible



Comparison of Hong Kong and PRC

- **2 aspects to every retirement system**
  - **Design**
  - **Funding**
- **How do HK and PRC measure up?**

	Hong Kong	PRC
Design	X	✓
Funding	✓	X



Possible Developments in China

- Open-ended Funds
- JV Investment Companies
- Chinese Tracker Fund
- Merging of Stock Markets
- Merging of A and B Shares
- Free Market for Foreign Insurance
- Liberalisation of Pension and Insurance Funds Investment
- Development of Unit-linked Insurance and 401(k) Pensions
- Privatisation of Second Pillar Pensions(Individual Accounts)
- Convertibility of Renminbi
- International Investment by Institutions