Live Long and Prosper: ageing in East Asia and Pacific

Robert Palacios
World Bank
Key messages

- East Asia experiencing unprecedented ageing
- Policies to increase labor force participation are needed
- Ageing will cause fiscal pressure through higher spending on health, long term care and pensions
- Retirement protection solutions will differ across countries depending on two things:
  - past pension policy decisions due to ‘pension inertia’
  - Context of ageing including the role of the ‘fourth pillar’
- There are many positive steps that can be taken to minimize the potentially negative impact of ageing
Structure of presentation

1. Demographics and the labor force
2. Health and long term care
3. Pensions
Demographics and the labor force
East Asia, led by China, has more older people than any other region

Rising to ½ billion in 2040!

65+ in million in 2015

- East Asia
- Europe & Central Asia
- South Asia
- North America
- Latin America & Caribbean
- Sub-Saharan Africa
- Middle East & North Africa
- Other East Asia & Pacific

World Bank Group
More importantly, the pace of ageing is unprecedented

Time it takes to double share of population aged 65+ from 7-14%
A shrinking working age population in much of EAP is inevitable ...
While in the post-dividend period, countries must find ways to increase labor force participation rates to avoid an ‘ageing tax’

Retirement incentives, life long learning, healthier ageing, accommodating workplaces, subsidies, childcare, immigration
Health and long term care
Health: good and not-so-good news...

**The good news**

- EAP people are living longer
- They also have more years of healthy life expectancy
- In much of EAP, communicable diseases are no longer the primary case of death & morbidity

**The not-so-good news**

- Non-communicable diseases (NCD) are exploding: more middle aged people have them & older people often have multiple chronic conditions
- Many people with NCD go undiagnosed and/or untreated – leading to high-cost acute treatment later
- In much of EAP, unhealthy behaviors are high, including smoking, salt intake and alcohol consumption
- Ageing is leading to new health challenges such as dementia
Health spending rising – but only partly due to ageing

- ageing contributes to increasing health spending (<1/3), but non-demographic factors more important
- Health spending has outpaced income growth
- NCD-related costs generally on the rise due to changing behavior but will be exacerbated by ageing
- Health insurance coverage has grown but there are gaps in financial protection
- Study points to inefficient spending; eg., hospital-centric provision, lack of strategic purchasing
Long-term care: avoiding mistakes and planning ahead

- Public sector support for long-term care remains nascent in developing EAP with rapid growth in ‘oldest old’
- Important to avoid defaulting to expensive long term hospital stays
- With the strains on traditional networks, there is a need for proactive policy measures – but government cannot do it all, and needs markets, families & individuals to play a role
- ‘Ageing in place’ should be the guiding approach, with a strong reliance on home- and community-based care – both more affordable & giving higher quality of life
Timing of pension system introduction varies significantly
Pension system design also varies...

- **Group 1: Defined contribution based systems**
  - Hong Kong**
  - Malaysia**
  - Singapore**

- **Group 2: Pay-as-you-go DB schemes**
  - China (transitioning to hybrid DB/DC, but DC ‘empty’)
  - Indonesia (new DB began in 2015)
  - Korea**
  - Japan**
  - Mongolia*
  - Philippines*
  - Thailand*
  - Vietnam*

- **Group 3: No mandated national scheme**
  - Cambodia
  - Lao (but planning to introduce)
  - Myanmar (but planning to introduce)
  - Timor-Leste

** = high coverage
* = moderate coverage
Low coverage

Orange – immature schemes
...leading to different risks

<table>
<thead>
<tr>
<th>Country</th>
<th>Benefit Target</th>
<th>Degree of redistribution</th>
<th>Member risk</th>
<th>Risk to government</th>
</tr>
</thead>
<tbody>
<tr>
<td>China</td>
<td>High</td>
<td>Large</td>
<td>Low returns on DC component</td>
<td>Large unfunded liability</td>
</tr>
<tr>
<td>Hong Kong</td>
<td>Low</td>
<td>Small</td>
<td>Low returns on DC; longevity risk</td>
<td>None</td>
</tr>
<tr>
<td>Indonesia</td>
<td>Low</td>
<td>Small</td>
<td>Low returns on DC; longevity risk</td>
<td>None</td>
</tr>
<tr>
<td>Japan</td>
<td>Moderate</td>
<td>Moderate</td>
<td>Sponsor risk/default</td>
<td>Large unfunded liability</td>
</tr>
<tr>
<td>Korea</td>
<td>Moderate</td>
<td>Large</td>
<td>Sponsor risk/default</td>
<td>Moderate unfunded liability</td>
</tr>
<tr>
<td>Malaysia</td>
<td>Low</td>
<td>Small</td>
<td>Low returns on DC; longevity risk</td>
<td>None</td>
</tr>
<tr>
<td>Mongolia</td>
<td>Moderate</td>
<td>Large</td>
<td>Inflation risk; sponsor risk/default</td>
<td>Large unfunded liability</td>
</tr>
<tr>
<td>Philippines</td>
<td>High</td>
<td>Large</td>
<td>Inflation risk; sponsor risk/default</td>
<td>Large unfunded liability</td>
</tr>
<tr>
<td>Singapore</td>
<td>Low</td>
<td>None</td>
<td>Low returns on DC component</td>
<td>None</td>
</tr>
<tr>
<td>Thailand</td>
<td>Moderate</td>
<td>Moderate</td>
<td>Inflation risk; sponsor risk/default</td>
<td>Moderate unfunded liability</td>
</tr>
<tr>
<td>Vietnam</td>
<td>High</td>
<td>Small</td>
<td>Sponsor risk/default</td>
<td>Large unfunded liability</td>
</tr>
</tbody>
</table>
Public pension spending lower in EAP for its demographic stage
Yet many people in EAP countries want the state to provide financial support in old age...
Social pensions increasingly supplement the contributory schemes
Pensions: Balancing coverage, adequacy and sustainability

• Group 1: DC schemes face adequacy concerns that are creating pressure on governments to supplement benefits.

• Group 2: Mature pay-as-you-go DB schemes face large unfunded liabilities and most face pressure for increased coverage – e.g., China using both matching contributions and social pensions.

• Group 3: Pension liabilities still moderate (mostly civil servants) but pressure to expand coverage; has become clear that traditional contributory schemes won't get there fast enough.

• Regardless of starting point, low adequacy or coverage and large unfunded liabilities all imply higher future pension spending of one type or another.
Different countries need to address different weaknesses

<table>
<thead>
<tr>
<th>Country</th>
<th>Sustainability</th>
<th>Coverage</th>
<th>Adequacy</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cambodia</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>China</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Hong Kong</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Indonesia</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Japan</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Korea</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lao</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Malaysia</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mongolia</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Myanmar</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Philippines</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Singapore</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Thailand</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Timor-Leste</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Vietnam</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Concluding observations

- While the entire region is experiencing unprecedented ageing, it is staggered and the starting point is heterogeneous.
- Younger countries hope to emulate the East Asian miracle productivity story of their elder neighbors but are unlikely to get rich before getting old.
- Older countries must look for ways to increase labor force participation, especially for upper income workers covered by pension schemes.
- Fiscal pressures are inevitable; more efficient health and LTC spending can help but some increase is unavoidable.
- The largest ageing-driven expenditure in most countries is pensions; despite huge differences in pension systems, there will be fiscal pressure to supplement inadequate pensions and use general revenues to expand coverage – in some cases while paying off mature DB unfunded pension liabilities.
Concluding observations

• Pension reform paths will be different for each country because (i) pension policy is subject to inertia and (ii) the income support gaps depend on multiple contextual factors outside of pension policy.

• Most defined benefit countries need parametric reforms to achieve financial sustainability while defined contribution schemes must address adequacy concerns due to low return-wage differentials and low contribution densities.

• East Asia will likely continue the global expansion of the role of social pensions as part of the system – the challenge is to integrate them efficiently with the consumption smoothing pillars of the system.

• Defined contribution countries and those with partially funded DB schemes will have to invest effectively.

• The right reforms can alleviate the fiscal burden as well as offsetting the impact of ageing on the labor force while improving the welfare of the elderly so that they can ‘live long and prosper.’