



INDONESIA PENSION CONFERENCE

25 YEARS OF PENSION SAVINGS

"Way Forward for Next Quarter Century"

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Grand Hyatt Hotel, Jakarta



SESSION 3

Incentivizing pension savings

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INCENTIVIZING PENSION SAVINGS

- Why bother?
- People are going to live a lot longer – in poverty?
- Limited capacity of the Government to keep paying



INCENTIVIZING PENSION SAVINGS

- Voluntary pension savings low coverage rate...
-even with incentives
- Different types of tax incentive have same fiscal impact...
- ...but psychologically individuals prefer 'up front' incentives
- Not clear if tax incentives actually increase overall savings or just move them around
- Other types of fiscal incentives needed to get those outside the formal sector to save



ITS EASY- JUST TELL PEOPLE TO SAVE MORE

- Is awareness effective?
- One message for all groups
- Is there a place for the Grim Reaper?
- Are we selectively deaf?

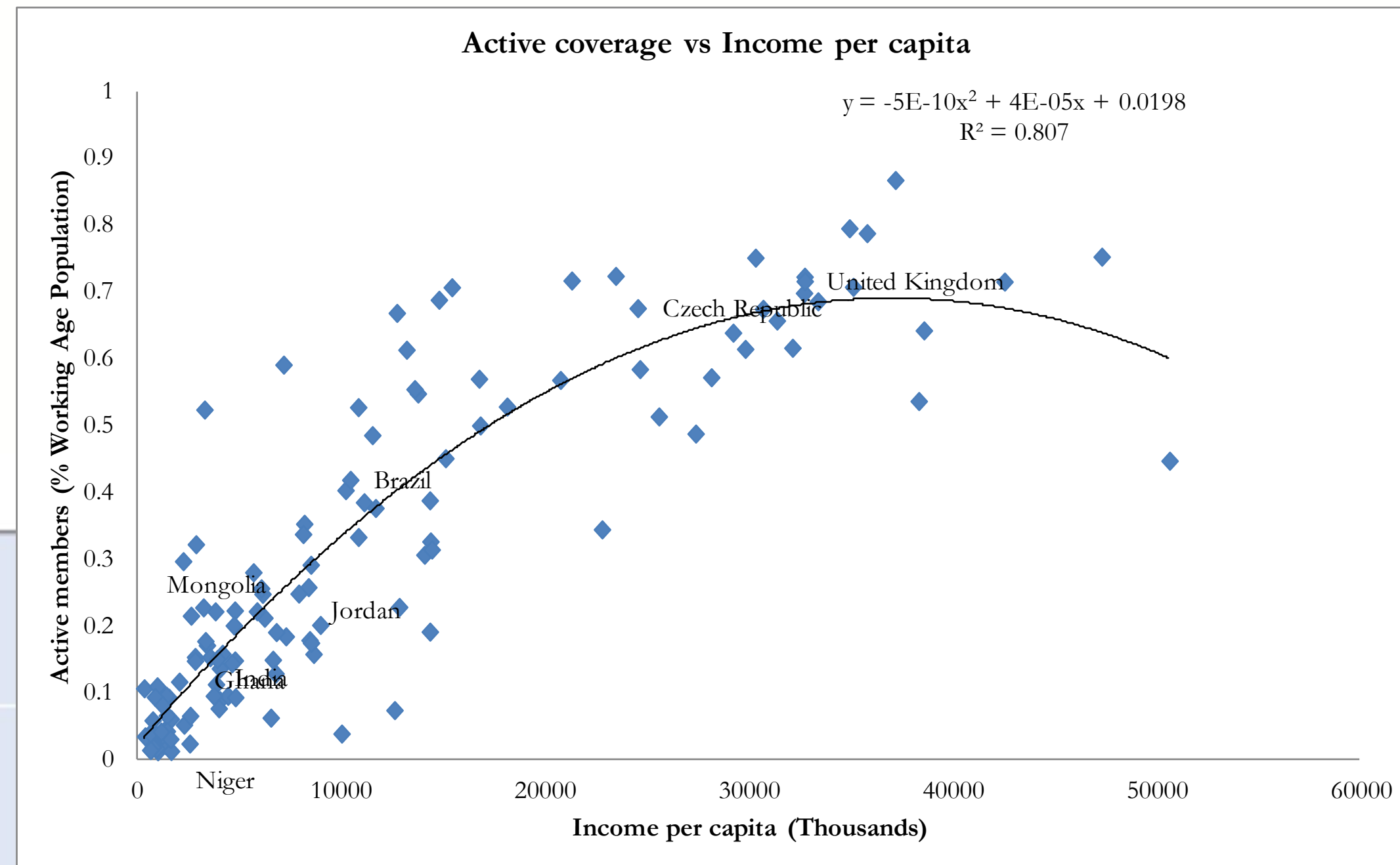
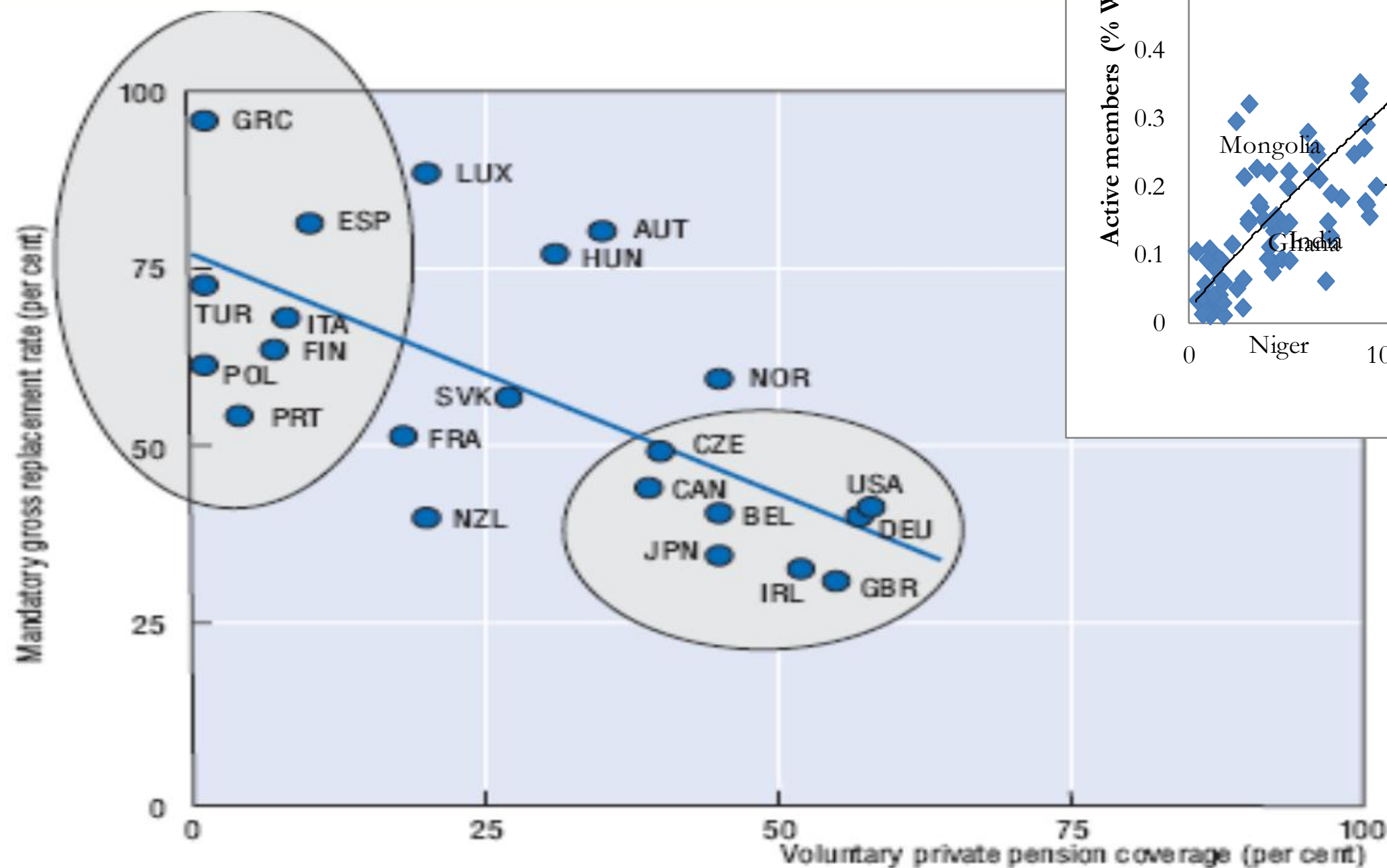


BUT WE ALREADY PROVIDE LOADS OF INFORMATION...

- Since the crisis – disclosure is king
- We provide loads of information more relevant to a finance professional than a pension contributor
- Do we attempt to answer the question – will I have enough if I keep going at this pace?



COVERAGE LINKED TO GDP PER CAPITA + LEVEL OF PUBLIC PENSION



TAX INCENTIVES CROWD OUT OR CROWD IN SAVINGS?

- **Studies of the 401(k) system in the US are contradictory**
 - Some find very high substitution through both decreased private savings and leverage suggesting tax arbitrage and substitution
 - Other find conclude net positive additions but at moderate levels – Some estimates (Engen and Gale 2000) estimate that at best 30% represent net additions to savings
- **Many other more complex issues arise from secondary effects (e.g. form of assets, how government finances tax subsidies)**
- **Preliminary analysis of developing countries and mandatory systems find some net additions**
- **Key factor may be level of development of financial markets – suggests higher potential for substitution in US and Europe**



TAX INCENTIVES

- Important empirical research concludes that tax incentives lead mainly to reallocation
 - Attanasio et al. (2004), Disney et al. (2007), Chung et al. (2006) for the UK.
 - Gale and Scholz (1994), Engle et al (1994, 1996), De Leire (2002), Attanasio et al. (2004) for the USA.
- Other research concludes that tax incentives create mainly new savings, raising national savings
 - Poterba et al. (1995, 1996a, 1996b), Hubbard and Skinner (1996), Engelhardt (2001) and Benjamin (2003) for the USA.
 - Ayuso et al. (2007) for Spain.
 - Fehr and Habermann (2006, 2007) for Germany.



IMPACT OF DIFFERENT TAX INCENTIVES

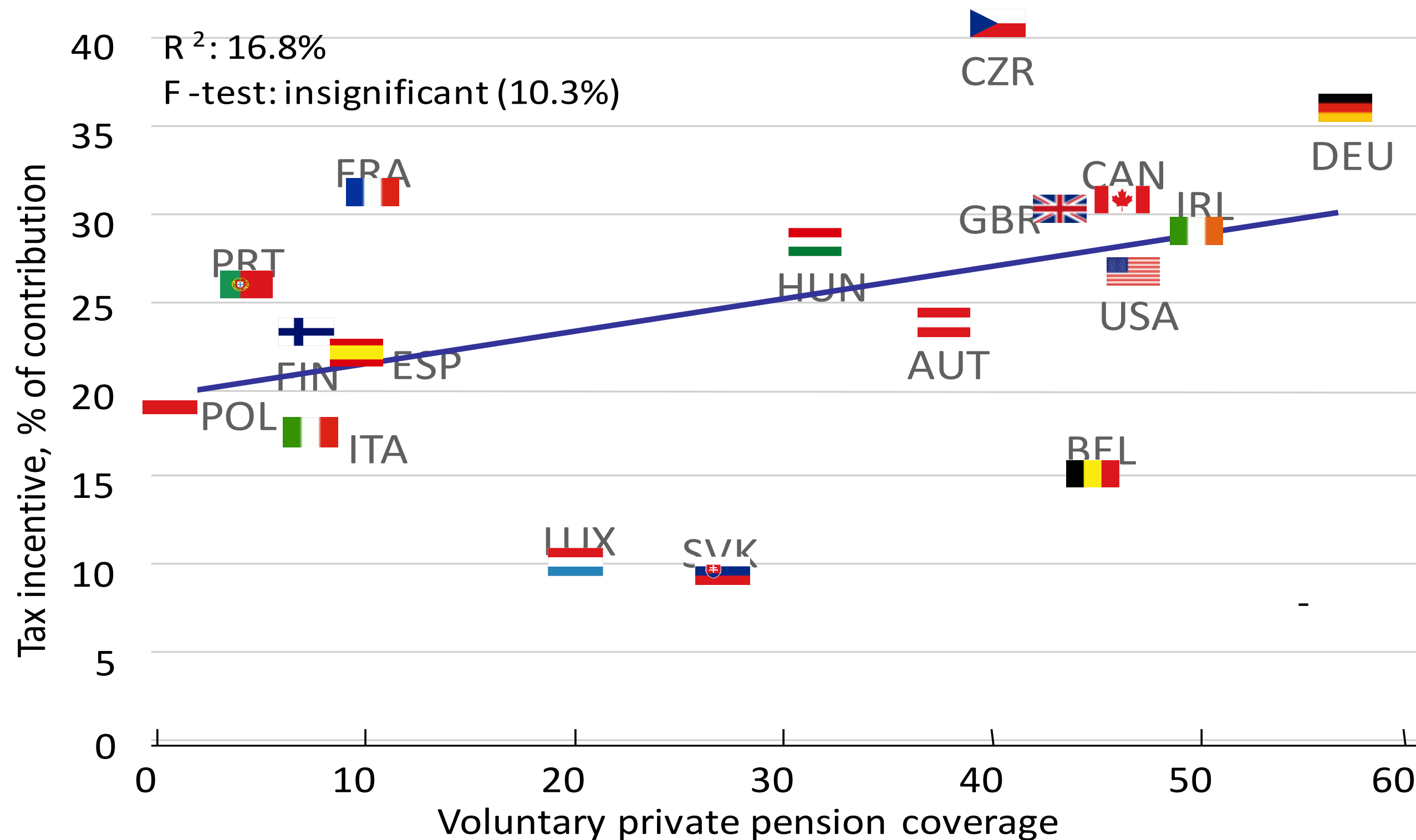
	EET	TEE	TTE	ETT
Contribution	100	100	100	100
Tax		-25	-25	
Fund	100	75	75	100
Net investment return	61	46	33	44
Fund at retirement	161	121	108	144
Tax on pension	-40			-36
Net pension	121	121	108	108

Note: assumes contribution made 5 years before retirement, with a tax rate of 25% and annual returns of 10%

	Contributions	Income	Benefits
Botswana	E	E	T
Namibia	E	E	T
Nigeria	E	T	E
South Africa	E	E	T
Chile	E	E	T
Colombia	E	E	E
Costa Rica	E (t)	E	E
Mexico	E (t)	E	T
Peru	T	E	E
Uruguay	E	E	T
Hungary	E	E	T
Poland	E	E	T
India	E	T	T
Indonesia	E	T	T
Korea	E	E	E
Philippines	T	T	E



VALUE OF TAX INCENTIVES DOES NOT PREDICT COVERAGE



DISTRIBUTION OF TAX INCENTIVES (USA IRA + DC PLAN TAX SUBSIDIES)

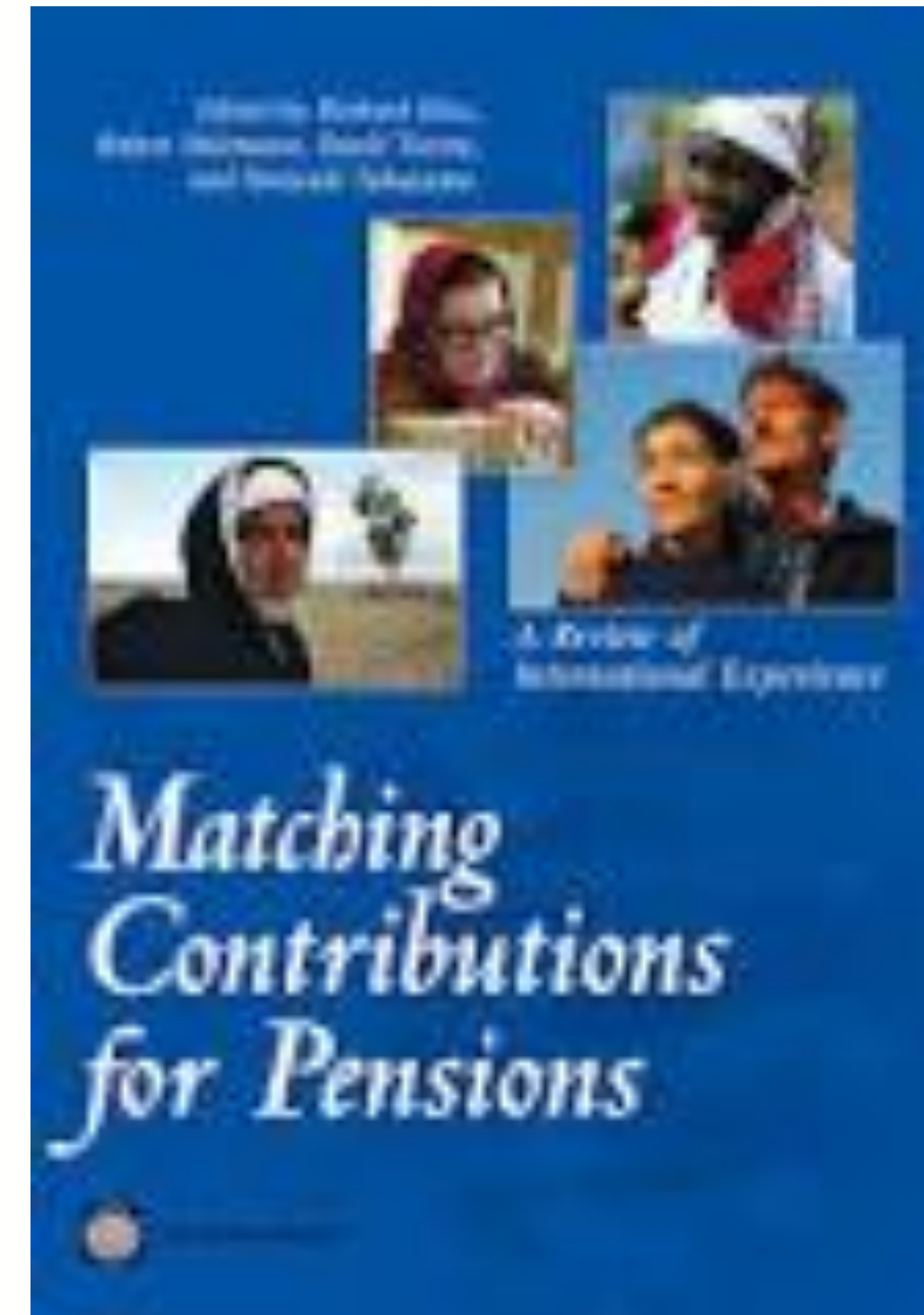
<i>Income Quintile</i>	<i>% or Units</i>	<i>Share of total</i>	<i>Average Value</i>
Lowest	2.0	0.2	\$6
Second	12.7	2.9	\$78
Middle	25.0	8.2	\$218
Fourth	43.0	19.3	\$513
Highest	61.0	69.3	\$1,838
Total	28.7	100.0	\$531

Source: Urban Institute-Brookings Tax Policy Center, 2004



MATCHING CONTRIBUTIONS EXPERIENCE

- **China:** rural pension system – which includes government match - successful increase in coverage but benefit levels low
- **India:** matching contribution for informal workers into New Pension System some success with on-going reforms
- **Korea:** match for fishermen and farmers increased participation from these groups into national pension system
- **New Zealand:** Kiwisaver started with cash incentive to remain in auto-enrolment account
- **Germany:** Reiser pensions cash incentives increased voluntary participation



FISCAL INCENTIVES CONCLUSIONS

- Some are necessary to increase voluntary pension savings
- Design important so increase overall savings from target groups
- Other mechanisms may be as successful at lower cost

