Institute of Policy Studies

Report on IPS Forum on CPF and Retirement Adequacy
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OVERVIEW

On 22 July, the Institute of Policy Studies (IPS) organised a Forum on the Central Provident Fund (CPF) and Retirement Adequacy at the Shangri-La Hotel in Singapore.

The Forum was structured around two panel discussions. The first examined the desired outcomes of the CPF system based on current and projected retirement needs and taking into account Singapore's rapidly ageing population. The second focused on how those outcomes could be achieved in an effective and sustainable way. Speakers were invited to give their suggestions on reforming the CPF system and their views on alternatives to the CPF that could help people build their retirement funds.

The Forum also featured two dialogue sessions, one with Minister for Manpower, Tan Chuan-Jin at midday, and another with Deputy Prime Minister (DPM) and Minister for Finance, Tharman Shanmugaratnam.

The Forum was attended by 260 people — from academia and the private, public and people sectors — who were invited for their interest in the subject. It began with an introduction by IPS director Janadas Devan, followed by an overview of Singapore's old age security system by Chief Executive Officer of the CPF Board (CPFB), Yee Ping Yi.

The presentations and dialogue sessions helped clarify how the CPF system works and also provided specific suggestions that policymakers could consider. Also, a strong appeal was made to attend to the old age security needs of those who may not have worked or have insufficient CPF savings.

Many questions were asked about the history and the integrity of the system. DPM Tharman clarified that the way that CPF funds were invested had evolved since the time of its creation. Initially, CPF monies were invested by the CPF Board in Government securities issued by the government. Proceeds from the borrowings were managed by the Monetary Authority of Singapore prior to the establishment of GIC in 1981, and the proceeds could be used to finance infrastructural development in the country before 1992. In the system at the moment, DPM explained, CPF monies were invested by the CPF Board in Special Singapore Government Securities issued and its returns were guaranteed by the Singapore government. These monies were in turn invested by the Government of Singapore

Investment Corporation (GIC) along with other government funds. The Singapore Government shielded CPF members from the investment risk and bears the risk of investment returns of GIC (for the pooled government monies) not matching up with the guaranteed rate of return. It was able to do so because of its substantial asset buffer – built up through years of budget prudence and investments. GIC managed the assets as a whole, without regard to their specific source.

DPM Tharman also reminded participants that the CPF had initially been more of a savings plan for home ownership, allowing 90% of elderly Singaporeans to own their homes. This relieved them from having to pay rental fees for accommodation out of their retirement funds in their senior years.

Both ministers said that the CPF could be further strengthened to accommodate the needs and risk profiles of CPF members. It might be good to incentivise private firms to set up supplementary retirement schemes for their employees as well.

Specific issues were raised about how the CPF system functioned as follows.

For one, as the CPF system was targeted almost entirely at those in the workforce, those who are not employed — due to disability, caregiving responsibilities or other reasons — lacked the means to fully benefit from the system. At the moment, such people benefitted if family members transferred money to help them build accounts. Ministers and panellists agreed that such needs had to be addressed through social assistance schemes of the government, especially since there was no state-funded minimum pension scheme in Singapore.

The CPF was a single, albeit broad, pillar of retirement funding. While trying to combine the upside of a defined benefit scheme with that of a defined contribution scheme, one criticism was that it lacked the diversity and flexibility in the investment of funds that retirement funds in other countries enjoyed. Singaporeans overwhelmingly depended on the CPF for retirement funding and 72% of CPF Investment Scheme (CPFIS) assets were placed in low-risk deposits. Of those participating in the CPFIS, 85% failed to achieve returns above the 2.5% that they would have achieved by leaving their money in the CPF Ordinary Account.

Changing demography in Singapore also represented a challenge to the system. The gap between the retirement age and life expectancy was widening despite the raising of the retirement age. According to the Melbourne Mercer Global Pensions Index 2013, the gap was 19 years between the drawdown age (at 62 years old) in the CPF system and life expectancy (81 years old). This would stretch to 21 years in 2035, with drawdown age (65 years old) and life expectancy (86 years old) if nothing else changed.

Associate Professor (A/P) Kalyani Mehta also noted that increasing life expectancy did not necessarily decrease the years of associated disability, which would suggest that healthcare costs would rise. Reversing this, or “morbidity compression”, should be a desired outcome – where a long life would be a relatively healthy one without any attending significant increase in the cost of healthcare.

Along with this changing demography came the other factor of changing family structures. A/P Kalyani cited decreasing age support ratios of people of working age to retirees at 65 years old and above[1] from 13.5 in 1970 to 6.4 in 2013, as well as rises in the number of elderly living alone especially because of the increase in singlehood and rates of divorce and separation. Thus, the paradigm of “Family as the first line of defence (for retirement)” had to be reviewed; it could not be taken for granted that there would be family to address the needs of Singaporean seniors.

There were also significant differences within the elderly age group, with younger generations of seniors able to take advantage of better economic circumstances, a longer working life and a higher propensity for retirement planning, as well as closer ties to their children. This was different for the older seniors of today.

The CPF’s focus on aiding Singaporeans to own their homes had its own set of implications. A/P Lum Sau Kim said that many Singaporeans placed most of their CPF funds from their Ordinary Account in housing for a number of reasons: they lacked avenues of investment that would protect their monies from inflation with the assumption that they would receive high returns from investment in property. This led to constrained retirement adequacy with low cash balances; poorly diversified retirement fund portfolios that were exposed to housing sector shocks and wider systematic risks. It had to be recognised also that housing was a highly illiquid investment asset.

A/P Lum added that while there were several ways of monetising the housing asset, they were unpopular. Housing as a nest egg for retirement depended on future housing prices, rents and interest rates, not to mention the fact that that a HDB lease was a depreciating financial asset. It was necessary too, said A/P Lum, to manage price expectations to prevent clustering or cohort effects when Singapore hit demographic bumps or other tipping points that might lead to a simultaneous rebalancing of housing portfolios.

It was also important to consider the CPF system with a behavioural lens. Donald Low explained that Singaporeans, as anyone would, faced cognitive limitations in perceiving the advantages of the CPF system and would find saving for the future challenging because of the effect of present-biased preferences. It was also generally a difficult thing, psychologically, for people to imagine themselves as seniors. Finally, there was a tendency for people to be overly optimistic about their ability to manage their own money. The CPF system has helped to overcome these limitations.

There was a legacy issue that the government had to deal with as well - lower-wage level workers had, since the 1980s, experienced three cuts in the employer’s contribution for their CPF. That left certain cohorts of workers in the lurch as it had taken a long time for employers’ contribution rates to be restored. This has left large numbers of lower-wage workers unable to meet the Minimum Sum requirement, and has negatively affected their ability to retire.

There were suggestions on improving the returns to CPF funds.

Alfred Chia advised that CPF members make use of the technique of dollar cost averaging through a regular savings plan, which meant that one would buy a set value of shares at

[1] Number of working-age persons per retiree.

regular intervals. This would remove the propensity for investors to make decisions based on emotional and short-term considerations. While the CPFIS was an important scheme, the lack of financial education amongst CPF members or under-qualified financial advisors meant that members were not able to make good use of it.

Professor Joseph Cherian introduced his idea for setting up "CPF SoShoik LIFE". In this scheme, CPF LIFE would provide a base inflation-adjusted income for life paid through the current annuity scheme and the Minimum Sum. Beyond that base, it should be possible for CPF members to have options commensurate with their own risk profiles to improve returns.

Donald Low suggested that the adjustments to life expectancy, withdrawal age and retirement or drawdown age and the monetary requirements of the CPF system could be made more transparent, predictable and even automatic, as was the case in countries such as Sweden. He said it would be good to establish an independent unit to make projections of the adequacy of the CPF system for different income groups and household types. The government should ensure that members got relevant information about the system and that changes were adequately explained. This would ensure that there was a healthy level of trust in what was a good system, as it helped people overcome behavioural biases with regard to retirement savings.

A participant suggested that when the government established the level of increase in the Minimum Sum each year and for each cohort reaching 55 years of age, it should use an inflation index that excluded imputed rent. This way the Minimum Sum would not be over-stated.

Associate Professor Hui Weng Tat said that for middle-income earners, the returns on CPF savings were far from the acceptable or expected income replacement rates (IRR). This group would nevertheless have to depend on CPF returns for security in their retirement. He said that the employee contribution income ceiling could be raised for this segment of the population to allow them to accumulate more funds, raise payouts and meet expected IRR of this particular group.

FULL REPORT

Introduction

IPS Director Janadas Devan opened the Forum with a review of the historical and political development of social security systems across the world. He described how in Germany and England, it was the private sector and conservative government, respectively, that paved the way for such systems — contrary to the popular assumption that liberal and left-leaning socialist parties were the advocates. He also explained how the Forum was organised — Panel Discussion 1 would examine the demand side of the equation in retirement adequacy, i.e., what Singaporeans want or need for retirement; and Panel Discussion 2 would look at the supply side of how the CPF system and alternatives to it could sustain adequate funding for Singaporeans' retirement.

Overview of the CPF System

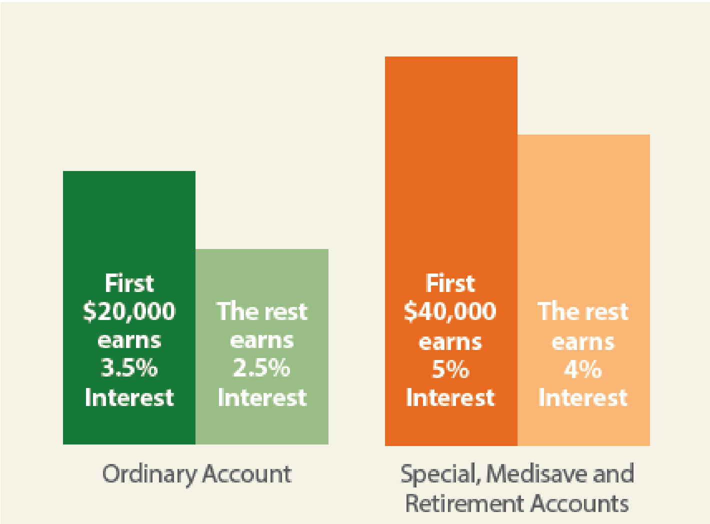
Mr Yee Ping Yi, Chief Executive Officer of the CPF Board, provided an overview of the national old age social security system and how the CPF system fit into that. The CPF, he explained, was a mandatory savings scheme funded by contributions from employers and employees, aimed at promoting retirement adequacy. To provide a picture of the retirement adequacy of CPF members, the median cash balance of active members aged 55 in 2013 stood at approximately $126,000 before factoring in savings withdrawn for the accumulation of housing assets. In 2013, 50% of active CPF members met the CPF Minimum Sum, including the 15% who pledged their property towards the Minimum Sum.

The CPF system has been one pillar of Singapore's social security landscape, alongside other investments in education, homeownership, and targeted assistance schemes to help the needy. These were the state's contribution to a citizen's journey right through life and ultimately to building-up resources for old age security. Funds in the CPF system are channelled to homeownership, healthcare needs, and retirement.

The CPF system differed from conventional defined contribution systems around the world in that CPF members were protected from investment and longevity risks. CPF members earned between 2.5% to 5% in interest rates in their CPF accounts and were shielded from the risk of low market interest rates (See Figure 1). CPF members will also enjoyed protection from longevity risk with the introduction of the national annuity scheme, CPF LIFE. CPF and CPF LIFE monies were similarly invested in Special Singapore Government Securities (issued and guaranteed by the Singapore government) which helped to secure such returns for members.

Nonetheless, the CPF system, Mr Yee said, faced the challenge of remaining financially sustainable with an ageing population, and in an unstable, low-yield investment environment – both factors that retirement systems faced all over the world today.

Figure 1: Interest earned on CPF contributions



Source: *Presentation on Old Age Social Security in Singapore* by Yee Ping Yi, Chief Executive Officer, Central Provident Fund Board

Panel Discussion 1: Meeting Current and Future Needs of Singaporeans — Desired Outcomes of the CPF System

The Future Retirement Landscape: Key Influencing Health and Social Trends

Associate Professor (A/P) Kalyani Mehta, Head of the Gerontology Programme of the School of Human Development and Social Sciences at the Singapore Institute of Management argued that it was important to take a holistic perspective to retirement funding and adequacy. She said that retirement should not be seen as just a financial event, but a social one where health and psychological dimensions should be considered as part of the experience. The proportion of elderly people as well as Singapore's median age and dependency ratios have been on the increase. Even as life expectancy rose in Singapore, the actual years of disability after retirement seemed to be the same as before. Singapore had not yet seen what was known as "morbidity compression" which would mean reduced years of disability which translate to a tempering of healthcare costs normally associated with an ageing society. Health trends in Singapore also pointed to need for more caregivers – there were more who were semi- or non-ambulant, or even suffer from dementia as they aged and would not be able to enjoy independent living.

Economic trends that had to be considered were inflation, increases to the Minimum Sum and whether more CPF members would be able to meet the requirement. Citing government statistics, A/P Mehta pointed to decreasing age support ratios (from 13.5 persons per senior person in 1970 to 6.4 persons per senior person in 2013); more elderly living alone especially because of the rise in singlehood (from 30% in 2002 to 32% in 2012, of the total population); and increasing rates of divorce and separation (from 2.2% in 2002 to 3.4% in 2012, of the total population). Therefore, the old paradigm - family as a first line of defence - needed to be reviewed, with the community and state stepping in to provide help when needed. These were some of the ways in which a holistic approach would be needed in considering what Singaporeans needed when they reached their senior years.

Future Needs and Wants of Seniors: Extrapolating From a 2011 Survey

A/P Tan Ern Ser of the Department of Sociology, Faculty of Arts and Social Sciences, National University of Singapore presented data on the financial adequacy of seniors and the role of the CPF from the 2011 National Survey of Senior Citizens.

Some information of note were: In comparing the financial situation of seniors aged 55–64 years ("young-old"), 65-74 years ("old") and those aged 75 and older ("old-old") across age groups and gender, the "old-old" and women did not fare as well as the rest. Around 21% of the "old-old" in his sample had an income below $500, compared to 6% of the "young-old".

A/P Tan, who is also Head of the Social Lab at IPS, said that 22% of "old-old" females earned below $500, compared with 7% of "young-old" females in his sample. The "old-old" (80%) and women (75%) tended to rely on income transfers from their children. While the "old-old" (55%) tended to depend more on their personal savings, males (48%) and the "young-old" (52%) were more reliant on paid work as their main source of income.

The larger question was the extent to which CPF funds mattered to the financial adequacy of seniors. More of "old-old" seniors and women tended to be in low-paying jobs. Overall, 23% of the the sample were cleaners. This proportion increased with age, and was disproportionately represented in the "females" category. Clearly these forms of employment did not and would not supplement retirement savings by very much.

CPF did not matter when seniors had little or no CPF money to begin with. A critical variable that seemed to be related to whether respondents felt financially secure was the strength of the ties they had with their children. In the sample, seniors who had a "very close" relationship with their children tended to say they were financially adequate (84%), while those who were "not close at all" to family said they did not have enough to retire on (33%). What was unclear however was whether perceived financial adequacy resulted in a strong relationship with their children, or if it happened the other way around.

Overall, A/P Tan suggested that the future looked better for retirement adequacy since the "young-old" tended to have higher incomes, more savings, a longer working life, as well as a higher propensity for retirement planning and better quality of relationship with their children.

CPF and Housing

A/P Lum Sau Kim, Director of Graduate Programmes of the Department of Real Estate at School of Design and Environment, National University of Singapore discussed the impact of housing financing and its implications on retirement adequacy within the CPF framework.

Housing has taken up a dominant proportion of total net withdrawals from CPF since 1968, when the government allowed CPF funding to be used for the purchase of Housing and Development Board (HDB) flats. Due to factors like the government's strong push for citizens to become homeowners, the reality was that many Singaporeans exhausted their funds in the Ordinary Account through the servicing of their housing debt or down-payment. With the lack of viable avenues of investment that would protect assets from inflationary pressures, and the general perception of high returns from investing in property in Singapore, many Singaporeans placed most of their CPF funds in housing. This resulted in a situation of constrained retirement adequacy with low cash balances.

With cooling measures such as the imposition of Valuation Limits (that has restricted the amount of CPF funds that can be used to finance housing purchases) and the Total Servicing Debt Ratio framework (that has placed a cap on the proportion of debt-to-income across various types of loans), more Singaporeans should be able to meet the Minimum Sum in future.

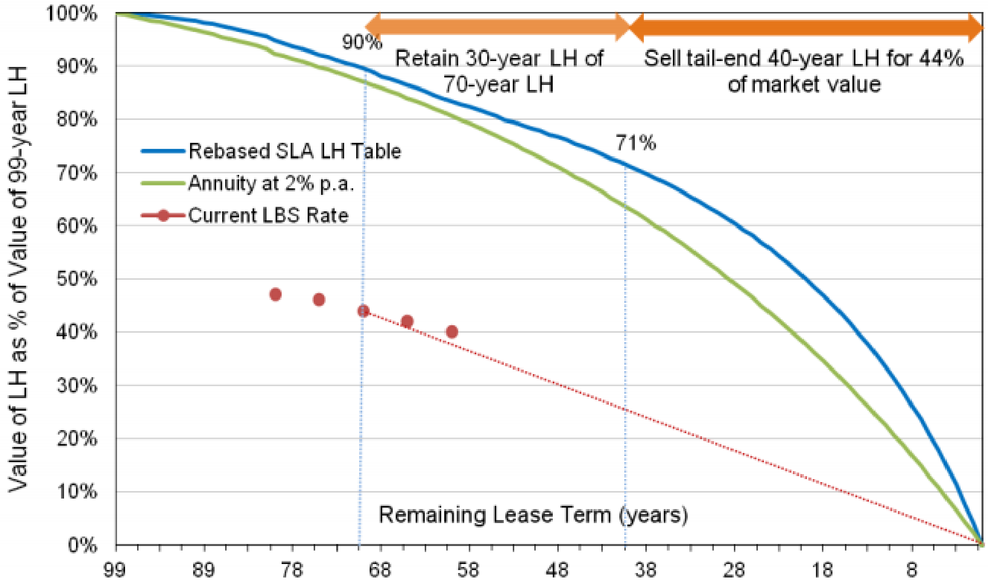
As for the multiple avenues of monetising one's housing assets, most have been unpopular with Singaporeans. A/P Lum cited statistics that she gathered from an Our Singapore Conversation session on housing monetisation held last year. She said that about 30% of non-rental HDB flats were owned by elderly citizens aged 55 and above, and 220,000 of these were fully paid for. Monetisation options included the subletting of whole flats or spare rooms, which has had a 10% take-up rate; the downsizing to studio apartments (SA), with 1,938 elderly households doing so in 2012; or the sale of the tail-end lease back to HDB for owners of three-room or smaller HDB flats through the Lease Buyback Scheme (LBS), with

471 elderly households doing so from 2009–2012. She shared that 240 elderly households had tapped the enhanced Lease Buy-back scheme in 2013, which included the Silver Housing Bonus. These options had low take-up rates for reasons that included the potential loss of privacy and security concerns when subletting rooms; the longevity risk of outliving the period of lease with the SA or LBS options; the concern that proceeds from monetisation may be treated as income and lead to the loss of medical benefits in means-testing subsidy systems; low economic literacy amongst elders; and the desire to bequeath property.

For the LBS in particular, the homeowner faced a straight-line decay in housing value for the tail-end of the lease sold on entry to the scheme (See Figure 2, where average LBS proceeds for 40-year leasehold apartments were only 44% of market value). In addition, any homeowner who exercised this option could only sell the 30-year lease option to HDB, where the decay of housing equity similarly followed a straight-line depreciation.

Another method of drawing on the value of housing assets was to use reverse mortgages, which would let owner-occupiers extract housing equity through a loan. NTUC Income first launched the scheme in January 1997, which was then extended to HDB owners in March 2006. This has not been popular for the key reason that banks required owners to make up the difference between collateral values and outstanding loan debts should housing prices fall. Other concerns with reverse mortgage included the fact it was not well understood by the elderly, and was susceptible to adverse selection and moral hazard. It was also important to note, said A/P Lum, that the sustainability of monetisation options faced the "wicked" problem of managing housing prices, i.e., monetisation required high prices and rents, but this in turn lowered the level of affordability for aspiring homeowners.

Figure 2: Pricing HDB leaseholds



Remaining Lease		Sold tail-end Lease		LBS proceeds	Implied discount
Years left	% of 99-yr	Years sold	% of 99-yr	% of market value	% p.a.
99	100%	69	89%	50%*	1.94%
90	97%	60	83%	49%*	1.77%
80	95%	50	78%	47%	1.70%
75	92%	45	75%	46%	1.64%
70	90%	40	71%	44%	1.61%
65	86%	35	67%	42%	1.57%
60	83%	30	63%	40%	1.53%
40	71%	10	31%	20%	1.50%*

Source: *Presentation on CPF and Housing*, by A/P Lum Sau Kim

The sustainability of housing as a nest egg hinged on the future path of housing prices, rents and interest rates, and how leasehold value decay was addressed given that the HDB lease was a depreciating financial asset. A/P Lum said it was also critical to manage price expectations to prevent clustering or cohort effects when Singapore hits demographic bumps or tipping points, where the simultaneous rebalancing of housing portfolios could induce shocks to the system.

Although the CPF system aimed at taking care of Singaporeans' housing, retirement and healthcare needs, portfolios were heavily skewed towards housing which, A/P Lum warned, increased the risk of shocks to retirement adequacy and the housing market as more households entered their deccumulation phase and monetised their substantial housing equity at the same time.

Behavioural Perspectives on the CPF System

Donald Low, Associate Dean (Research and Executive Education) and Senior Fellow at the Lee Kuan Yew School of Public Policy, provided the behavioural perspective on assessing the CPF system.

Even as the CPF system had its inherent strengths, Mr Low felt that there were several weaknesses that should be addressed so that the government could have the political support and will to undertake unpopular but necessary reforms when required. The strengths of the CPF system were found in its fiscal sustainability, and how it, together with housing, formed a unique Singaporean “welfare system where government help was dispensed within a framework of fostering self-reliance and reinforced the work ethic.

The drawback of such an approach was where narratives meant to encourage work and individual responsibility as well as to get citizens to think of the CPF monies as their “own monies” encourage an “each-man-for-himself” mentality. This made it difficult for the government to act for the greater good. Also, Mr Low argued that it was important that changes to any part of the CPF were made in a more predictable, transparent and even automatic manner. The failure to do so, combined with the lack of public education on how the CPF monies were invested, risked undermining public trust and support for the CPF as an institution.

When viewed through the behavioural lens, Mr Low explained that citizens faced cognitive limits in perceiving the advantages of the CPF system. There was the tendency to focus on present-, rather than future-biased preferences. For instance, it was difficult for most people to imagine themselves as seniors living in the future. This steered individuals towards current consumption and away from thinking of the future. In addition, stating a withdrawal age of 55 had created the effect of “anchoring” and resulted in unrealistic expectations of when members hit that milestone. Finally, there was a tendency for people to be overly optimistic about their own capabilities, including managing their own money.

Even as some degree of paternalism was therefore necessary given these cognitive limitations, such an approach would be inherently limited in what it would be able to achieve. Paternalism eroded individual ownership and could lead to hearsay and misguided information in the absence of accurate and timely information, amongst other issues. Possible corrections to the current CPF system could include giving CPF members some choice on the levels of risk they wished to take with their investments; for the government to provide information on how the CPF monies were managed or invested in a more timely and accessible manner; for an independent unit to make projections of the adequacy of the CPF system for different income groups and household types; and to explain CPF and CPF policy changes through a wider range of non-government communication channels.

Discussion

Responding to a question from the audience, Mr Low suggested that adjustments to the pension system could be made automatic and directly tied to life expectancy, as Sweden had done from the mid-1990s. This would insulate unpopular but necessary policy changes from populist sentiments, and allow the system to adjust according to known factors like a probable increase in life expectancy.

While addressing a point from a participant, some panellists agreed that the CPF system was not universal in that it only catered to those who had been employed. A/P Mehta said that women indeed tended to be disadvantaged in this regard because they often stopped working to play caregiving roles. Older generations of women were also kept out of the workforce due to conservative cultural values. Mr Low said that there was indeed the need for another system to address old age security for such people.

The discussion also extended to the redistribution of monies obtained from citizens. One participant suggested that there was a need to look beyond savings and towards avenues like the redistribution of taxes for the financing of retirement. Another participant asked if more profits could be channelled back to CPF owners from GIC's investment of monies, which included the CPF funds.

In response to a query from a participant on the weighted average interest on all CPF balances, Mr Don Yeo, Deputy Chief Executive Officer of the CPF Board, reminded participants that CPF members earned 2.5% on monies in their Ordinary Account with an additional 1% on the first $20,000, and 4% on monies in their Special, Medisave and Retirement Accounts with an additional 1% interest on the first $60,000 of balances. The weighted average rate of return across all CPF account balances was approximately 4%.

Other points raised included comments on the biological and physical aspects of ageing, as well as the issue of managing rising healthcare costs. One participant said there was a need to pay attention to those in their 40s, as early health screening could reduce healthcare costs later quite significantly. Another participant said that the import of cheaper immigrant labour would be a way to keep healthcare costs down. A look at the Manpower Ministry's foreign labour quotas showed that the service sector was at the bottom in terms of resource allocation.

Dialogue Session with Minister for Manpower Tan Chuan-Jin

Introduction

The dialogue session with Minster for Manpower, Tan Chuan-Jin was chaired by IPS Academic Panel Member, Hsieh Tsun-Yan.

Minister (Min) Tan began by discussing the key operating parameters of the CPF system and highlighting how the tweaking of different parameters will change the size of the "nest egg" at the accumulation phase when CPF members build up their individual accounts and the size of the payouts at the deccumulation phase.

The minister emphasised that when the CPF was introduced in 1955, the retirement age of Singaporean workers was 55 and life expectancy was between 60 to 62 years. Since then, life expectancy of Singaporeans had changed — of those turning 65 today, one in two would live beyond 85, and one in three would be likely to live beyond 90. This variable of increasing longevity was the single most important factor that shaped the parameters of any pension system in the developed world, including the CPF. In the light of that, Min Tan asked participants to consider several questions:

- What is the impact on retirement adequacy when we live longer?
- What happens to us when we stop working full-time or outlive our retirement funds?
- How do we ensure that the CPF system is sustainable?
- Considering the possibility of present-biased preferences and people not planning for the future, to what extent should provisions for retirement be left to the individual, or should the state be involved?
- How far do we wish to burden future generations as we consider more provision for retirement?

Many pension systems in the world now faced the difficulty of sustaining payouts that were promised previously without increasing taxation on working citizens.

The parameters affecting the accumulation phase included frequency of work, quantum of wages, contribution rates, interest payments on the money accumulated, and withdrawals for other uses. The parameters that affected the deccumulation phase were the age at which CPF members retired from work; when the payouts began; and how long the system had to support them. A change in one parameter would affect the others. For example, increased flexibility with regard to withdrawals for other uses in the accumulation phase would decrease the amount available to individuals in retirement. A higher payout quantum would deplete savings more quickly, while a later retirement age would conversely increase the amount in the accumulation side of the equation due to additional contributions from work. The goal of government, Min Tan explained, was to work within the above parameters to help Singaporeans accumulate a large enough nest egg to see them through their retirement years. CPF LIFE, an annuities scheme, provided payouts for an entire lifetime, he reminded the audience.

To sum up, the CPF system provided a basic level of assurance of retirement funding but it did not provide fully for everyone's needs. It facilitated home ownership and afforded help in covering the cost of healthcare. It was important to ensure that the system was sustainable and not a burden to future generations.

Discussion

Several threads of discussion emerged. One participant questioned the viability of raising the retirement age for people in certain professions — citing the examples of surgeons and truck drivers — due to physical constraints and ageing. Min Tan agreed, saying that re-skilling people through continuing education and training (CET) to help them stay in the workforce, even if it was to be in a different job from what they were used to would be important, provided that was what they wanted in the first place. It was clearly a personal choice but it was also a route to active and fulfilling life as a senior. For those who were not able to work, CPF was not the only system they could turn to as there were other forms of social assistance available.

The same participant also asked if MediShield Life would place an additional burden upon the younger generation, given that a significant proportion of Medisave payments were now being made by children on behalf of their parents. Min Tan replied that with MediShield Life and Medifund, there were now schemes available to help people. Those who wanted to pay for their parents would themselves continue to work and re-build their own CPF accounts.

A participant from a financial advisory firm said that while the Minimum Sum had been raised to keep up with inflation, wages on the other hand remained stagnant relative to rising costs of living in recent years. He asked what the Ministry of Manpower (MOM) was doing to raise salaries. Min Tan answered that many countries were grappling with this problem, and that Singapore had at least seen real wage growth of 2% to 3% in the past few years. He stressed the importance of remaining competitive and equipping individuals with the capacity to exploit employment and business opportunities. Programmes such as Workfare target those who struggled, and such measures had worked. The government, Min Tan said, was also looking at other ways to strengthen social safety nets in the long term.

A participant from a local non-government organisation asked if was possible for CPF statistics to be disaggregated by age and gender to better understand which groups of people had benefitted from the system. The participant went on to add her concern that women were not benefitting fully from the risk-pooling promised by CPF Life, as they were likely to have dropped out of the workforce earlier and they also tended to live longer than men, which meant that the payouts to such these women could be lower because they had not met the Minimum Sum. She also noted that CPF might inadvertently favour those who are wealthier as they benefited from tax deductions when they made additional voluntary CPF contributions, effectively placing an implicit tax on the poor.

On the former point, Min Tan agreed that women did live longer, but the broader question was who the vulnerable in Singaporean society were and whether they were provided for in some way. He explained that CPF, while important, was part of a larger social security system and some needs could be better met through other forms of social assistance. On the latter point, Min Tan replied that Singapore's tax and transfers system in Singapore was designed to be progressive and redistributive when taken as a whole.. Additionally, tax revenues funded other schemes such as education and housing subsidies, which benefitted poor families most.

Another participant asked about the viability of the Minimum Sum and the number of people who were able to meet the Minimum Sum from cash contributions to CPF alone, rather than cash contributions combined with property value. Min Tan acknowledged that many older Singaporeans went through the early phase when wages were relatively low, and did face a challenge of meeting the Minimum Sum. He also pointed out, however, that the Minimum Sum was merely intended to be a guideline to meet retirement needs comfortably, and was pegged to costs of living for that reason. The CPF was intended to provide a basic level of insurance that people can draw upon when in need. He was also confident that younger Singaporeans would be able to meet the Minimum Sum as they earn good wages.

On this issue, Min Tan also touched on discouraging over-investment in housing, with people depleting their CPF savings by spending more than they should on purchasing properties. This was ultimately a value judgment made by individuals: they had a range of choices — from low to high leverage — and some consciously chose the latter. The HDB had measures to help people "right-size" their choice of housing and manage their expenditure, but people were still free to make their choices. This then raised the question of the degree to which the system should allow people such flexibility.

A participant from a local university raised concerns regarding the lack of sustainability of growing wages in a tight labour market, asking if it was possible to guarantee that the Singapore economy would remain vibrant and that there would be good jobs in future, given that current figures showed that productivity seemed to have stagnated. He also asked if the introduction of a progressive wage model to certain industries would hurt competitiveness. Min Tan replied that certain sectors had proven that they could innovate and raise productivity under the current constraints. He agreed that wage growth without productivity growth would be detrimental in the long run, but pointed out that upstream, changes were put in place and results were starting to be seen. Min Tan also defended the progressive wage model, explaining that it provided incentives for companies to change and offer more commensurate wages to low-waged, low-skilled workers who were willing to upgrade themselves.

Lastly, a participant asked why payouts by CPF had not been pegged to inflation, citing the example of inflation-protected bonds provided by certain governments. He also noted that pegging the Minimum Sum to the Consumer Price Index (CPI) could over-state the inflation rate as the CPI used included imputed rent[2], which may not be applicable because the large majority of Singaporeans are homeowners. He estimated that removing this could lower the Minimum Sum by as much as $10,000. Min Tan said that the issue of including imputed rent into the calculation of inflation and how the Minimum Sum was calculated was indeed being reviewed. He also assured the audience that the government was looking at additional ways to strengthen the system and ensure long-term sustainability of returns as well as improve payouts of the system.

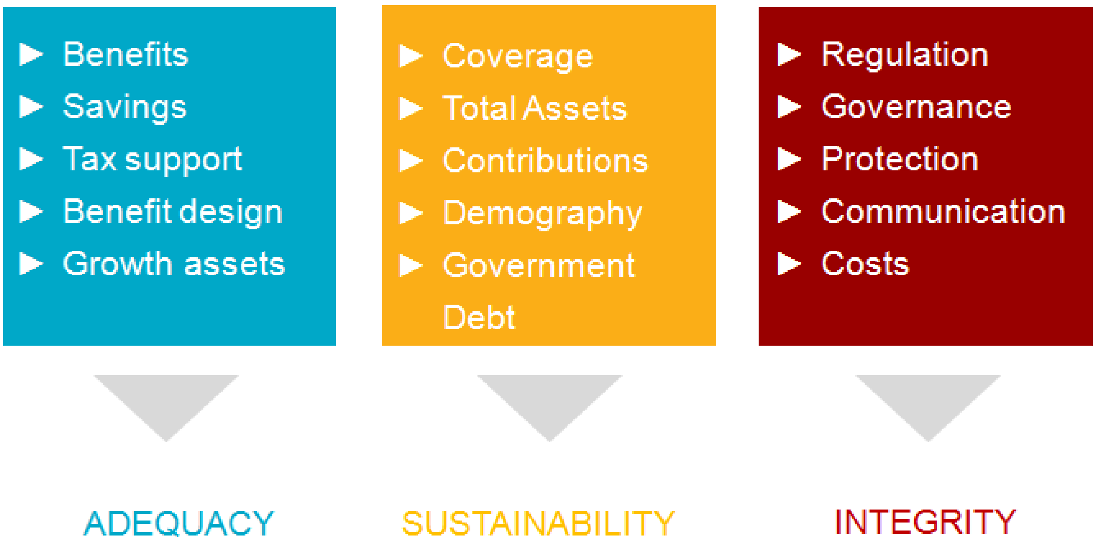
[2] Imputed rent refers to the amount of money that homeowners would pay if they were renting their homes instead.

Panel Discussion 2: Achieving the Desired Outcomes of Our CPF System in a Sustainable Way

International Retirement Income Systems: Challenges for the Future

Wong Su-Yen, Singapore Chairman of Marsh and McLennan Companies, began the second panel session by comparing the CPF system with pensions system around the world. Referring to the Melbourne Mercer Global Pensions Index, she discussed the criteria used in assessing those pension systems: adequacy, sustainability and integrity (see Figure 3). She focused mainly on the first two areas of concern because Singapore had fared quite well as compared to other countries in terms of integrity.

Figure 3: Three main areas of concern for retirement funds



Source: Melbourne Mercer Global Pension Index 2013

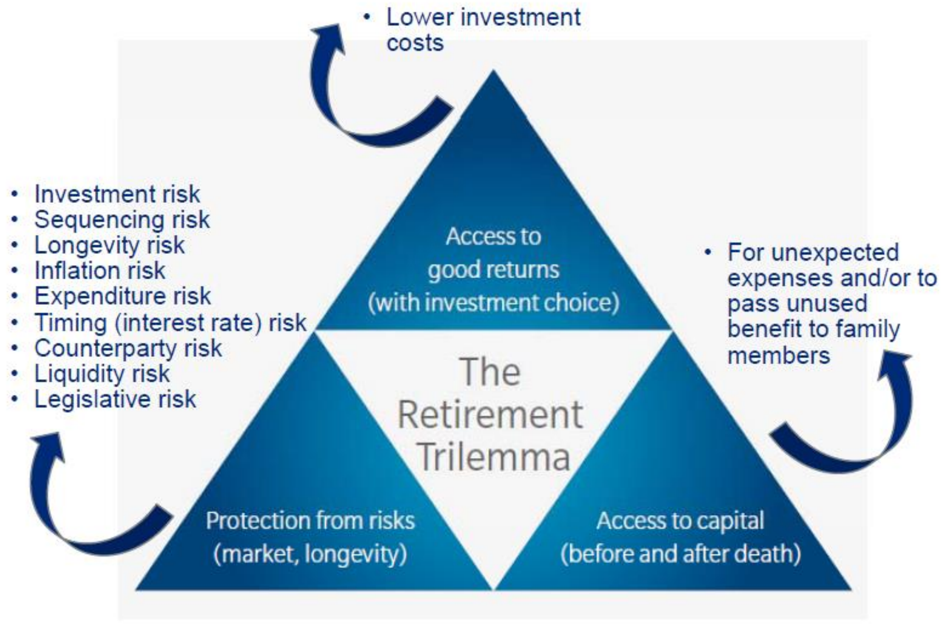
Singapore scored a "B" grade when marked against 20 pension systems around the world for two key reasons. The first reason was Singapore's lack of a formal minimum pension amount that all senior citizens can expect to receive. This was because retirement funding here primarily depended on the CPF system designed to cover people who accumulated funds by participating in the labour market. By looking at how much money the most needy people in Singapore accessed through government-funded public assistance schemes (she gave examples such as the Goods and Services Tax vouchers, and utility bills offsets), Ms Wong said what might effectively be a minimum pension for this segment would be the equivalent of 10% of Singapore's "national average wage". Although there was no international consensus on what a minimum pension amount should be for everyone, the Organisation for Economic Co-operation and Development suggested that a figure closer to 30% of the national average wage would be needed to meet poverty alleviation goals.

The second reason was the lack of diversity in how Singaporeans provide for their retirement funding. Singaporeans were almost entirely dependent on the CPF when it came to investing for their retirement. Also, within the CPF's investment schemes, almost 72% of members were invested in low-risk deposits, whereas people in other countries seemed to avoid them entirely, preferring higher-risk bonds and equities. Ms Wong suggested that it might be beneficial to reduce barriers to establishing private supplemental plans and to encourage monetisation of housing assets to help Singaporeans optimise their retirement funding.

As retirees had many needs, they had three imperatives with regard to funding their senior years: maximising their funds, managing risk and having adequate access to capital if and when the need arises.

The reality was that it was unlikely that there would be one particular product that could meet all three imperatives. People needed to take the portfolio approach and develop various plans to address each of those imperatives adequately. That "retirement trilemma" she described is illustrated in Figure 4 below.

Figure 4: The retirement trilemma



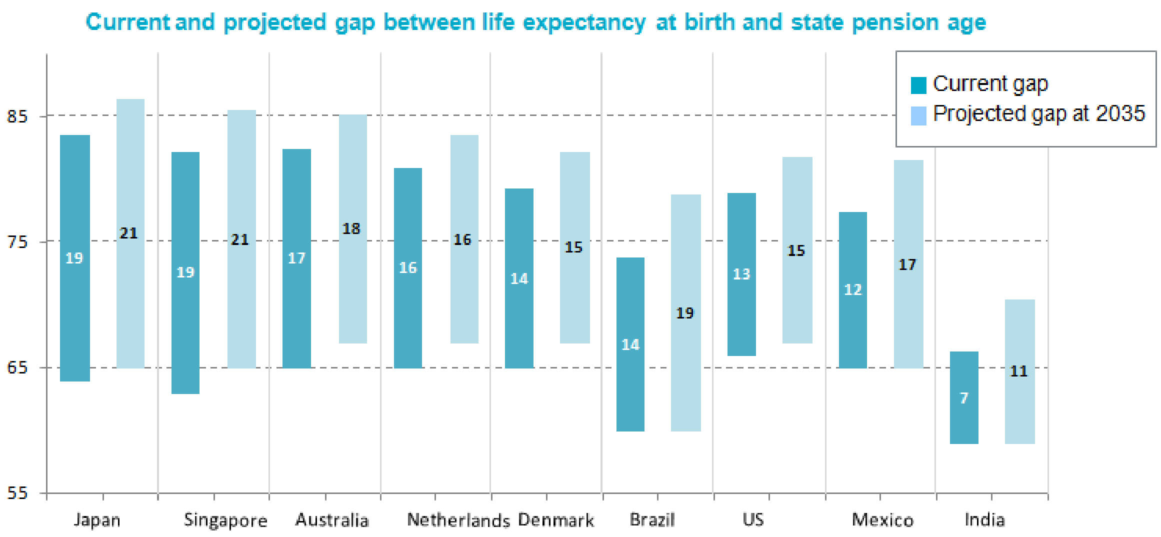
Source: Melbourne Mercer Global Pension Index 2013

As for the issue of sustainability, Ms Wong noted that the retirement age was established at a time when life expectancy was 60 years (for men). It now stood closer to 80 years.[3] While Singapore had raised the drawdown age to 65 years, the number of years citizens expected to live after 65 years of age continued to increase, placing further strain on the system. That

[3] A note on life expectancy: Many times during the panel, life expectancy was brought up. Usually, what is meant is life expectancy from birth, but as people age their life expectancy changes. For example, Ms Wong said that life expectancy for men is 80 years, but for men at the age of 65, the CPF Board and Singapore government believe that the life expectancy is 85, with about a third of that cohort living until the age of 90.

gap would have to be shortened, presumably by extending the retirement and drawdown ages. However, while in the past, working lives took a very linear path — people would study, then work and finally retire, Ms Wong said that in recent times that linearity had broken down. Workers were now interspersing their careers more variedly with periods of non-work or leisure. This would lead to a different way of approaching retirement where one might not exit the labour market entirely at any point in time. To illustrate where a government's and individual's interests met on this, she referred to the work done by the International Monetary Fund that indicated that the pension reform that was most likely to bring about long-term economic benefits was that of extending the working lives of people.

Figure 5: The life expectancy and retirement age gap



Source: Melbourne Mercer Global Pension Index 2013

Observations on a Worry-Free and Sustainable CPF System

Professor Joseph Cherian of the NUS Business School spoke on the myths and facts about the CPF system. In his opinion, the interest rate payments given by the CPF Board represented a tax-free, risk-free 3% real yield, a sum unmatched by any other government.[4] Thus, the 36% mandatory savings represented a good investment. He believed that the CPF and its component parts, such as CPF LIFE and the Minimum Sum requirement, represented a good system, but there were still opportunities to improve it.

Professor Cherian said that every retiree had three fundamental concerns: receiving a reasonable monthly payout; having that payout last through one's final days; and making sure that the payout would be indexed to his or her cost of living.

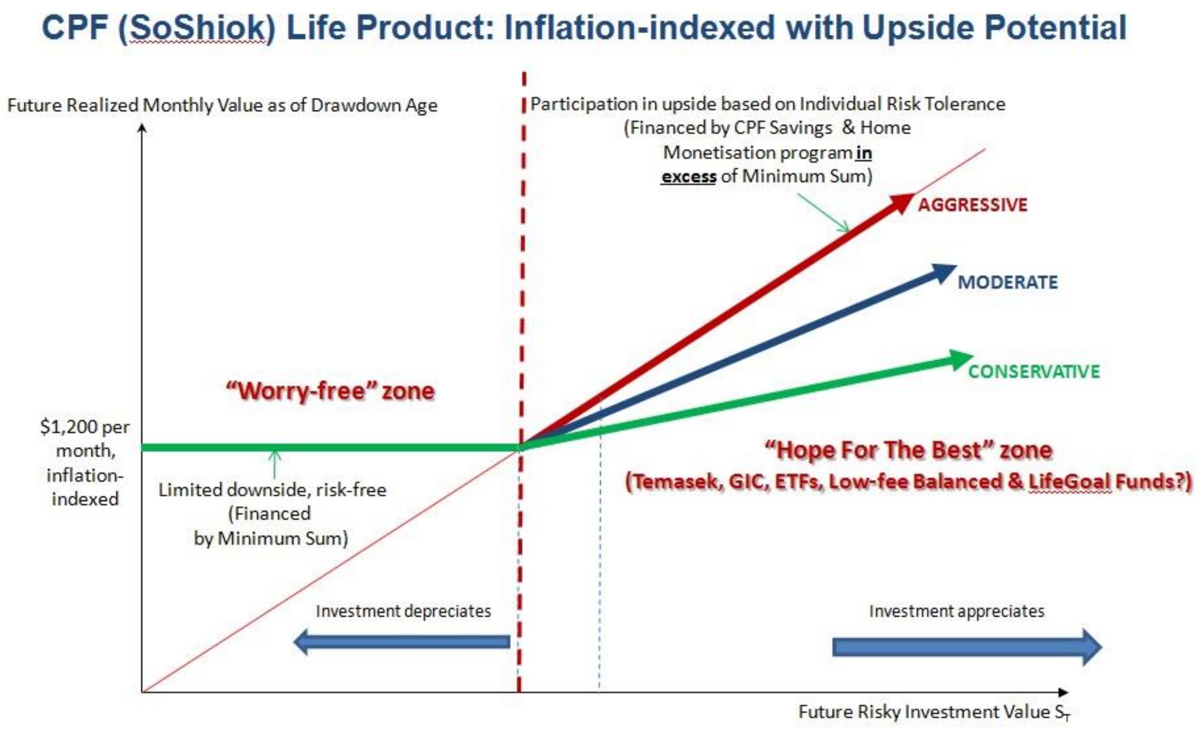
To that end, Professor Cherian suggested an alternative scheme termed "CPF SoShiok LIFE", which was a similarly annuitized scheme as CPF LIFE, but was inflation-protected and offered opportunities to further invest at a risk and returns rate commensurate with the

[4] This 3% rate was derived by assuming a 2% rate of inflation and subtracting it from the 5% interest rate given to the first $60,000 of CPF member's SMRAs (Special, Medisave and Retirement Accounts).

member's risk profile. He also hoped that as the government considered improving schemes to help Singaporeans monetise their housing assets for retirement, such as through the Lease Buyback Scheme, it would ensure that the lease would last till a person's final day rather than the 30 years as it stood now. That assurance should be put in writing.

One other suggestion he made was to design a scheme that allowed homemakers to also take part in the CPF on equal terms.

Figure 6: CPF SoShiok Life



Source: Centre for Asset Management Research & Investment (CAMRI)

Analysing the CPF Investment Scheme and its Alternatives

The presentation by Alfred Chia, CEO of SingCapital Pte Ltd, centred on the CPF Investment Scheme and the need for more education for both members of the CPF and the financial advisors meant to help them make investment decisions.

Mr Chia said that nearly 85% of CPF members who took part in the CPFIS did not make the 2.5% returns they would have received by leaving their money in the system. Mr Chia explored some of the reasons why this was so, and suggested that the primary cause was a lack of financial know-how on the part of the majority of Singaporean investors.

One of the solutions that he used to advise his own clients was the principle of Dollar Cost Averaging through a regular savings plan, which was to buy a set value of shares at regular intervals regardless of price in the belief that over time the total cost per share would even out and reflect less risk than buying the shares all at once.

The CPFIS was important to help Singaporeans get more from their CPF, he said, but could be further altered to bring out the best of the system. It was his opinion that the CPFIS SA schemes — investment schemes that allowed special account monies to be used — either be allowed to access higher-risk schemes of around 10% potential returns, or be terminated, as the likely investment returns now rarely beat the 5% that was guaranteed.

Concluding, Mr Chia reiterated his call for a deeper level of financial literacy to be taught to all Singaporeans, starting as soon as possible, to ensure that all Singaporeans were able to use investments as a means to save for their retirement.

Improving the CPF System

Associate Professor Hui Weng Tat from the Lee Kuan Yew School of Public Policy rounded off the presentations by saying that the CPF was a good system that could be made better. In his opinion, much of the unhappiness with the Minimum Sum Scheme stemmed from the gap between the official and effective withdrawal age.[5] In addition, there was a perception that the government had been inconsistent in tweaking CPF policy over the years. A/P Hui suggested that a way to address this was to be clear and transparent, and to recognise that life expectancy was growing by three to four years a decade. The government should decide on instituting an automatic and progressive rise in the withdrawal age from 55 years old now for succeeding cohorts of CPF policyholders to catch up with rises in life expectancy. This should also be coupled with demonstrating the benefits of a longer working life and life expectancy.

He also spoke about his belief that there was a need to address the looming issue of retirement adequacy for middle-income residents. This issue stemmed from the Ministry of Manpower underestimating both income growth and housing aspirations of the middle-income group. This middle income group would have to cut-back substantially on their standard of living. According to A/P Hui's estimations, regarding the income replacement rate (IRR), or the percentage of a person's average income over his working life that he could expect to receive in retirement, the CPF provided from 70% to 110% for income brackets between $1,200 to $1,900, but was only between 40% to 53% for those in the $3,000 income bracket. A/P Hui worked out those figures on the basis of two possible growth paths, one constant and one that was more optimistic.

A/P Hui's solution to this would be to raise the income ceiling for employee's contribution for those in the higher income brackets. It was not feasible to do this for the employer's contribution because it would affect Singapore's business cost, but he felt that workers would understand the change as long as it was made clear that the increases were tied to wage growth or inflation and that this would help middle income workers to save more for their retirement and raise their IRRs.

Discussion

Mr Manu Bhaskaran, IPS Adjunct Senior Research Fellow and Partner and Member of the Board at Centennial Group, chaired the discussion. Several themes that emerged included

[5] The official withdrawal age is 55 years. However, the drawdown age for CPF LIFE and the Minimum Sum Scheme is between age 62 to 65, depending on the year of birth.

the expectations that CPF members had with regard to their CPF funds, the adequacy of their funds, and how the disadvantaged could also benefit from a social pension system outside of the CPF system.

A number of questions focused on the how CPF members should view their CPF savings and its adequacy in providing for their retirement. Would CPF members tolerate the volatility that came with pegging the CPF rate of return to market rates? Also, was it practical to expect to maintain one's standard of living once one entered retirement, and to have the very notion of the age of withdrawal being placed at 55 years? One participant described the retirement age of 55 years as a "colonial hangover", saying it was not a realistic notion even when it was first implemented and certainly not appropriate in today's context when people were living much longer.

The panel replied that as the demographics of the population changed, so did the expectations of one's working life as well as retirement. For example, many young graduates today expected the lines between their day-to-day working life to blur and blend, and it might be realistic to expect that they may look at their retirement in the same light. In that case, it would not make sense for these younger generations to have a clear line as to when someone retired.

The panel also said that within the current structure, the best way to maximise gains from the CPF system was by better educating citizens and their advisors in financial matters. One of the panellists felt that from the date it was first implemented, some CPFIS schemes were clearly capable of making money for their investors, but Singaporeans were generally not able to find those schemes. They looked for immediate returns rather than to build steady long-term portfolios with better returns.

There was also some focus in the questions on how the CPF system was not effective for everyone, such as those who did not work or had dropped out of the workforce for various reasons, such as retrenchment or disability. The panel noted that the CPF was not a social safety net, and it could not be turned into one. The government would have to utilise other means to help these groups of Singaporeans.

That line of questioning also raised the case of lower-wage level workers who had, along with the rest workforce, experienced three cuts in the employer's contribution rate to their CPF accounts since the 1980s. At that time, Singapore had attempted to use the employer's contribution as a tool of macroeconomic policy. The cuts lowered business costs and helped to keep companies in Singapore afloat. That left certain cohorts of workers in the lurch as it had taken a long time for employers' contribution rates to be restored; as of now, contribution rates had yet to return to the original 20%. This, the participant suggested, left large numbers of lower-wage workers unable to meet the Minimum Sum requirement, and negatively affected their ability to retire.

The chairperson Mr Bhaskaran said that it was clear that the government no longer used cuts in CPF contributions as a tool for macroeconomic stabilisation. The panel added that it would be best to either have tried to offset the pain from that decision or make it up to those affected at a later time. It was then noted that while the Singapore government and the CPF Board erred on the side of caution in fear of spending too much money in the form of payouts and returns, it was important that they would not then make a different mistake of “spending too little”. While it was not wise to spend fecklessly, at some point, future generations would have to take care of themselves, and present generations would have to spend today’s money to take care of today’s disadvantaged.

In conclusion, Mr Bhaskaran reiterated that while the CPF system was generally good, it was not yet at the top of the class, citing the Mercer study presented by Ms Wong Su-Yen that had given it a “B” grade. Retirement adequacy was the primary worry, along with needing better financial education for both investors and advisors, and better inflation protection.

Dialogue with Tharman Shanmugaratnam, Deputy Prime Minister and Minister for Finance

The dialogue session with Deputy Prime Minister and Minster for Finance, Tharman Shanmugaratnam was chaired by Patrick Daniel, Editor-in-chief of English Publications at Singapore Press Holdings, and a former member of the board of governors at IPS.

DPM Tharman started the session by providing a historical account of the development of the retirement savings policy to highlight how it had evolved, and added that it would continue to do so to meet the basic needs of most Singaporeans.

The CPF system began by working more as a simple savings plan for homeownership. Many were poor as Singapore was still in the early stages of development; savings were fully withdrawn at 55 years of age with no restrictions. Much of the money spent was used on housing, and there was only one basic account. The merit of that was that today, 90% of Singaporeans owned their homes, ensuring that the elderly did not need to pay rents from their retirement funds. However, the government also understood that there was a proportion of the elderly who were asset-rich and cash-poor, and was studying ways to help this group.

In the second phase during the mid- to late 1990s, the system was re-balanced to boost cash savings for retirement. Thus, limits on how much policyholders could withdraw for property were introduced, along with the Medisave system and the Special Account. Interest payments were now made on monies held in the CPF.

On top of savings and interest payments, today, the government funded top-ups to CPF accounts of low-wage workers out of its budget. This meant that they received the equivalent of 6% annual returns on their savings when amortised over their full working life. There were also other subsidies that worked through the healthcare system, such as the top-up for premiums to the new MediShield Life insurance policy. DPM Tharman noted that while the CPF system was by no means perfect, it remained well regarded around the world by serious professionals and assured the audience that it would continue to evolve to meet the changing needs of people.

The government, he said, was committed to improving retirement security for all Singaporeans, with special help for those with low income, in a way that addressed the effect of inflation through the interest payments on CPF savings; and also by helping people unlock the value of their housing asset, particularly the elderly. It must also recognise that not all could take high risks for high returns. In 2007, the government was prepared to review the scheme but felt that the balances in policyholders' accounts were too low to be allowed to portion part for their savings into private pension plans.

Generally, such plans were not a "walk in the park", DPM Tharman said. He compared the returns on CPF with the Mandatory Provident Fund scheme in Hong Kong, noting that the returns on that scheme averaged 4% annually in nominal Hong Kong dollars since its inception in 2000. The CPF Special Account returns compared favourably with this figure. Expectations of higher returns would only mean that members had to be prepared to take a higher risk with their monies; one may go through many years without seeing any improvement in returns. Furthermore, the current investment environment had changed with low yields in money markets — global funds were now estimated to be able to earn 4% annually for the next 10 years. This low-yield environment would not last forever but it would be the case for the foreseeable future.

Discussion

A number of participants said that many wished for a bigger payout when they reached 55 years of age, rather than the $5,000 payout that has not changed over the past 10 years. Others noted that only 50% met the Minimum Sum anyway, and asked if there should be a way in which some other social pension scheme could be devised for the disadvantaged and groups that have such difficulties.

DPM Tharman reminded participants that there was a tension between the desire for flexibility to withdraw monies and the quantum of payout upon retirement, while also ensuring that payout accounts for the effect of inflation. If it were possible to withdraw larger sums, one would not just lose that sum, but also the compound interest that the money would have otherwise earned. He explained that these questions reflected the issues that were facing the CPF system. It was not possible to provide all three overarching requests — flexibility, adequate income throughout life, and adjustments based on cost of living — together, and a balance had to be struck among those requests.

On the other hand, another participant asked if the government could do more to incentivise companies to set up supplementary retirement schemes and Section 5 programmes that would allow for tax-exempt contributions from employers to retirement funding programmes for employees. DPM Tharman said that the government would also consider doing that — especially with regard to supplementary retirement schemes — but it would not affect the majority of CPF members.

DPM Tharman noted that while the CPF system had often been thought of as a single-pillar retirement scheme, it was a very broad pillar that had strong support from government. It was a hybrid system that incorporated good aspects of defined contribution and defined benefit retirement policies and provided a stable system while it guaranteed a rate of return. It was also boosted by government subsidies with targeted support for low-income members as well.

Questions were asked on how CPF monies were invested, whether Temasek Holdings ever received or managed these monies, whether GIC knew that it took charge of investing CPF monies, and finally whether there were excess returns on investment that could be paid out in the form of higher interest payments to policyholders.

Mr Tharman clarified that Temasek Holdings never received or invested CPF monies. CPF monies are invested in Government securities. Before 1992 the Government could use the proceeds obtained to finance infrastructure, such as road, economic and social infrastructure. This changed in 1992 with the passing of the Government Securities Act, requiring that all the proceeds had to be invested. In the current system, DPM explained, CPF monies were invested by the CPF Board in Special Singapore Government Securities (SSGS) that were issued and guaranteed by the Singapore government. Prior to the establishment of GIC in

1981, proceeds from the borrowings were managed very conservatively by the Monetary Authority of Singapore (MAS), but GIC now had the mandate to invest them in long-term assets and seek better returns.

DPM explained that GIC managed all government monies taken as a whole with no regard or concern to the source of that money. Its mandate was to invest for the long-term, take the appropriate level of risk and get returns significantly above the global rate of inflation. If GIC were to invest only CPF monies with the goal of providing returns for account holders, the management of funds would be quite different. The government had taken on the risk of the guarantee on the capital sum and interest payments on CPF monies which was possible because state assets were larger than its liabilities thanks to prudent fiscal planning over the past five decades.

Figures on returns were publicly available and published by GIC. However, these were not the returns gained from CPF monies alone, but rather returns gained from the investment of all government assets, including unencumbered assets.

Mr Daniel asked DPM if there was a specific segment of Singaporeans that the CPF system was designed around. DPM clarified that the scheme was to provide for basic retirement needs. That was why the withdrawal sum at 55 years was set at $5,000 and the income ceiling for maximum CPF contributions at $5,000 — the 80th percentile of the population by income. It was pegged at providing a basic stream of income of $1,200 through CPF Life. As a national scheme, it would not meet the needs of those who are better off and have higher expectations about the quality of life when they retire. Many Singaporeans also had their housing asset, which was important, but in government surveys about what people relied on for retirement, there was evidence that those who were better off did have significant financial assets as well.

DPM Tharman listed a few key priorities going forward: to make sure that housing prices moderated and rose in a manner that did not spiral beyond the increase in incomes, and to reduce the ratio of median income to the cost of the mode of housing that a citizen at that income level would buy. Another would be to rely more on social risk-pooling as Singapore's life expectancy rose. Certainly the system has moved from one based on individualised accounts to a hybrid form with risk-pooling elements. Overall, when one added the government budget-financed enhancements and the reforms introduced over the past seven years — whether through the Workfare system, housing grants, healthcare subsidies and how these feed into the CPF system — it was clear that social compact had changed and an improved social support system was in place. To illustrate, a low-wage couple today would receive the equivalent of $160,000 in subsidies and assistance by the time they reach 65 years of age.

Mr Tharman assured participants that he would consider the suggestions shared at the Forum so that the CPF system served some of the groups of people who seemed to have been left out, i.e., the self-employed, homemakers and the disabled. More generally, the CPF system would be strengthened as a basic pillar of retirement funding for all Singaporeans.

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