Singapore’s Multi-Pillar System of Social Security

KDI-World Bank Conference on “Multi-Pillar Model of Social Safety Net”
Held in Seoul, 6 December 2006
Introduction

- I will describe the different pillars of social security in Singapore
- I will argue that Singapore has
  - an elaborate social security system for the middle and upper classes, and
  - inadequate arrangement for the poor.
- The weak support system for the poor is due to the government’s aversion towards “welfarism”,
- But this has changed somewhat recently due to changed circumstances.
The notion of multi-pillar system popularized by the World Bank’s 1994 Report *(Averting the Old Age Crisis)*

- It proposed three pillars.

In 2005 a group of World Bank’s senior staff members published “a policy note” *(Old-Age Income Support in the 21st Century)*

- It proposes an expanded and more flexible social security system consisting of five complementary pillars.

I will use the 2005 document as a template for discussing Singapore’s social security system
## The Five Pillars of Old Age Income Security

<table>
<thead>
<tr>
<th>Objective</th>
<th>Financing</th>
<th>Program Features</th>
</tr>
</thead>
<tbody>
<tr>
<td>Poverty alleviation. Redistribution</td>
<td>Government’</td>
<td>• Mandatory • Publicly managed • Means tested • Minimum Benefits</td>
</tr>
<tr>
<td>Income replacement. Some redistribution</td>
<td>Contribution – PAYG or partially funded</td>
<td>• Mandatory • Publicly managed • Defined Benefits or Notional Defined Contributions • Earning-related benefit</td>
</tr>
<tr>
<td>Income smoothing, through savings</td>
<td>Tax-Preferred private savings or insurance. Fully funded.</td>
<td>• Mandatory • Privately managed • Defined Contributions • Benefits equal contribution plus returns on investment</td>
</tr>
<tr>
<td>Income smoothing, through enhanced savings</td>
<td>Tax-Preferred private saving. Fully funded.</td>
<td>• Voluntary • Privately managed • Fully Funded Defined Benefits or Defined Contribution • Benefits equal contribution plus returns on investment</td>
</tr>
<tr>
<td>Continuing protection where possible</td>
<td>Financial and other assets</td>
<td>• Voluntary • Privately and informally managed • Informal intra-family or inter-generational financial and non-financial help. Eg. Housing, healthcare</td>
</tr>
</tbody>
</table>
Zero and First Pillars

■ Zero Pillar
  ■ Meant to provide a minimal level of protection to all those without sufficient income.
  ■ Eligibility conditions are meant to be flexible so as to include all those who need support.
  ■ Government funded, as contribution requirement would may exclude some potential beneficiaries.

■ First Pillar is a new proposal
  ■ Targeted at the working poor, those who don’t or can’t save, and those who face unusually high longevity or market risks
  ■ Benefits tied to income – but scope for some redistribution to those who need additional support.
Second, Third and Fourth Pillars

- The Second Pillar is a compulsory savings arrangement
- The Third Pillar is a voluntary savings arrangement
- The Fourth Pillar is a new proposal.
  - Recognizes that informal mechanisms a vital source of income protection.
  - Prominent examples include Family and Home ownership
## The Pillars Old Age Income Security in Singapore

<table>
<thead>
<tr>
<th>Pillar</th>
<th>Program</th>
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<tbody>
<tr>
<td>0</td>
<td>• Public Assistance.&lt;br&gt;• Ad hoc financial relief.</td>
</tr>
<tr>
<td>1&lt;sup&gt;st&lt;/sup&gt;</td>
<td>• Nil</td>
</tr>
<tr>
<td>2&lt;sup&gt;nd&lt;/sup&gt;</td>
<td>• Central Provident Fund (CPF)</td>
</tr>
<tr>
<td>3&lt;sup&gt;rd&lt;/sup&gt;</td>
<td>• Supplementary Retirement Scheme (SRS)</td>
</tr>
<tr>
<td>4&lt;sup&gt;th&lt;/sup&gt;</td>
<td>• High level of Family support.&lt;br&gt;• High level of home ownership.</td>
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</tbody>
</table>
Zero Pillar in Singapore

- Consists of
  - Public Assistance
  - Welfare programs run by the Community Development Councils (CDCs) and the Ministry of Community Development, Youth and Sports (MCYS).
  - Ad hoc grants and fiscal reliefs
  - Tax incentives for encouraging private donations to charities by individuals and firms.
  - Encouragement for social services to be delivered by volunteers.

- The government calls these disparate measures ‘many helping hands’ approach to social welfare
Public Assistance (PA)

- PA is intended to benefit “... financially distressed Singaporeans who by reason of age, illness, disability or unfavourable family circumstances, are unable to work and have no means of subsistence as well as no one to depend upon.”
- PA is only for those who have a good reason for not working and have no other source of income or family support.
- PA monthly benefit amount is S$260 for an adult and S$825 for a family of four.
  - Equivalent to 8% of average GNI for single adults and 6% of per capita GNI for a family of 4.
  - Compared to OECD average of 29% of GNI.
Public Assistance

- PA recipients form 0.07% of the population.
- Approximately 85% of all PA recipients are “aged destitutes”.
  - Yet, only 0.8% of the elderly receive it.
- There are many other small schemes to help families with education, housing, and utility bills.
  - They usually require one or more family members to be working.
Ad Hoc Benefits

- Government frequently gives out *ad hoc* benefits
  - Just before 2006 elections, the Government distributed S$3.6 billion in Progress Packages and Workfare Bonuses
  - In recent years, billions of dollars have been given out through various assistance schemes, including New Singapore Shares, Economic Restructuring Shares and CPF Top-Ups.
- Significantly, these do not impose binding obligation on the government and are purely discretionary basis.
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<th>CPF</th>
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<td>■ Established in 1955.</td>
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<tr>
<td>■ Participation is compulsory for all employed persons, except for foreign workers and casual and part-time workers</td>
</tr>
<tr>
<td>■ Contribution rates have ranged 5 – 50% of wages.</td>
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<tr>
<td>■ Current combined contribution rate is 33% of wages.</td>
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<tr>
<td>■ Employee contributes 20% and the employer 13%.</td>
</tr>
<tr>
<td>■ Members’ accounts are divided into 3 sub-accounts, reflecting the different functions of CPF</td>
</tr>
<tr>
<td>■ Ordinary: holds 60-75% of funds</td>
</tr>
<tr>
<td>■ Special: holds 10-20%</td>
</tr>
<tr>
<td>■ Medisave: holds 15-20%</td>
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CPF

- Ordinary Account
  - Funds in this account may be withdrawn for a range of purposes, including housing and approved investment.
  - Withdrawal for housing and investment form >75% of all CPF withdrawals.

- Special Account
  - Fund in this account is for retirement and may only be withdrawn at the age of 55 years.
  - Members are required to leave a minimum sum in the CPF: US$ 46,728.
    - The amount is released in instalments from the age of 62 years until it is exhausted.
  - Withdrawal for retirement formed only 14% of all withdrawals in 2005.
CPF

- CPF is estimated to provide replacement income of 27-30% of the last pre-retirement income.
  - Compared to OECD average of 57% for 2nd Pillar programs
- Projected that 60-70% of the 50-55 years age group will not have sufficient funds in their CPF account to meet the minimum sum requirement.
- Low replacement is due to
  - Withdrawals for housing
  - Low returns -- 1.2% 1987 and 2004, the CPF provided average annual real returns of only%
  - Most importantly, absence of risk-pooling
Supplementary Retirement Scheme (SRS)

- It allows employees (but not employers) to make voluntary contributions up to S$11,475 (S$26,775 for foreign workers) a year into their personal accounts, which can be invested in a variety of financial instruments excluding property.
- Contributions and investment gains are exempt from taxes, but half of the withdrawal amount at retirement is subject to tax.
<table>
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<tr>
<th>Family support</th>
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<tbody>
<tr>
<td>Family is the main source of income for 80% of aged male and &gt; 50% of aged females.</td>
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<td>Children provide &gt; 75% of income for three-fifths of the elderly.</td>
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<td>Yet 79% of elderly had monthly income of below US$ 584, (approximately 1/3rd of per capita GDP).</td>
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<td>The income support the aged receive from their family members is reinforced by common living arrangements.</td>
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<td>93% of elderly live with at least one non-elderly person alone.</td>
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<td>The family support system is hard to maintain due to:</td>
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<td>- Declining family size</td>
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<td>- Growing share of aged</td>
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<tr>
<td>- Proportion of population 65+ years old will rise from 6 in 1990 to 15 in 2020</td>
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</table>
Housing

- Approved Housing Scheme allows members to use their CPF to buy public (1968) and private (1981) housing.
  - Buyers of public housing flats are eligible for loans up to 80% of the selling price for up to 30 years.
  - Interest rate is slightly above the rate offered by savings account – currently 2.5%.
- Most home owners in Singapore are able to service their mortgage loans entirely from their CPF contributions.
- Home ownership in Singapore is 90%, up from 30% in 1970.
- People may be over-investing in housing
  - A typical worker at the age of 50 years and above in Singapore has 73-77% of her/his financial assets in housing and only about 20% in CPF.
- Sluggish housing prices a concern – affects retirement income.
Conclusion

- Singapore has
  - robust Second Pillar – CPF
  - strong Fourth Pillar -- widespread home ownership and family support
  - reasonably strong Third pillar – SRS
- Its main shortcoming is the absence of a meaningful Zero and First pillars capable of adequately protecting those not covered by other arrangements.
- Government is increasingly aware of the problem and is looking for alternatives.
- Concerns triggered by:
  - Economic fluctuations
  - Stagnant and declining wages for the less skilled and older workers
  - Growing income inequality.
But efforts to establish a genuine Basic Pillar of income security hindered by the government’s antipathy towards Western welfare state and its commitment to tying welfare benefits to work.