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Review of the Pension System in Thailand

Overview

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Review of the Pension System in Thailand

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This note is still a draft to be revised when the main pension report is concluded.

Key Messages

This note provides an overview of the coverage, adequacy, financial sustainability and policy consistency of the Thai pension system. It is a summary of a longer report which aims to provide analysis and recommendations that contribute to ongoing national policy discussion on pension policy, and input into an overarching Social Protection Diagnostic Review (SPDR) that the UN is jointly carrying out with the Thai Government. The report will be followed by an Actuarial Valuation which will provide updated projections of the Social Security Office (SSO) fund.

While the Thai pension system is assessed to have made substantial strides in terms of coverage, it confronts significant issues in terms of adequacy, financial sustainability and policy consistency. A key underlying issue is the architecture of the pension system and the fragmentation of pension schemes across different categories of workers. This architecture does not reflect or accommodate the mobility and dynamism of the Thai labour market, and the high levels of non-standard work and self-employment. If these issues are not addressed, they threaten to undermine the effectiveness and financial sustainability of the pension system in the context of rapid population ageing.

The report makes the following recommendations, divided into two strands:

1. **Immediate reforms to improve pension system effectiveness**

   These should focus on boosting pension adequacy, building faith in the pension system and supporting households through the economic recovery from COVID-19. Key strands are:

   - **Increase the value of the Old Age Allowance** (OAA) to provide a more meaningful pension guarantee, and an economic stimulus to support households recover from the crisis.
   - **Make parametric adjustments to SSO pensions** to increase pension adequacy, including (a) increasing the wage ceiling of the scheme and (b) providing for periodic payments for workers with shorter contribution histories than the current 15 year requirement
   - **Postpone the roll out of the proposed National Pension Fund** (NPF) so that it forms part of a more systematic pension reform.

2. **Develop a national strategy for pension system reform**

   This national strategy can provide a vision to guide ongoing adjustments to the pension system in a way that ensures policy consistency. The vision would articulate the function, financing and interaction of pension schemes in Thailand to build towards a coherent multi-tier system providing adequate and sustainable benefits. This paper sets out options for a system of complementary tiers that can support Thai workers as they move through their careers. The main shape of this system would be as follows:

   - **Tier 0: The Pension Floor** (OAA, complemented by the State Welfare Card and disability allowance). As part of this, integration of OAA and SSO benefit payments has potential to support better pension adequacy, system sustainability and payment delivery as well as making the system more transparent, fairer and creating positive labour market incentives.

- **Tier 1: Guaranteed earnings-related benefits** (SSO). This requires making further parametric changes to strengthen the adequacy and sustainability of SSO. The report also outlines options to extend guaranteed and periodic earnings-related pension benefits to non-wage workers currently in the informal economy.
- **Tier 2: Harmonised complementary savings.** This involves ensuring that the array of saving options available (National Savings Fund, proposed NPF, Government Pension Fund (GPF) and provident funds) provide a coherent and effective landscape for savers.

Additional issues to be considered would be the greater integration of civil servant pensions into the national pension system and strengthening the enabling environment for pension reform (including other social protection benefits, and labour market policies).

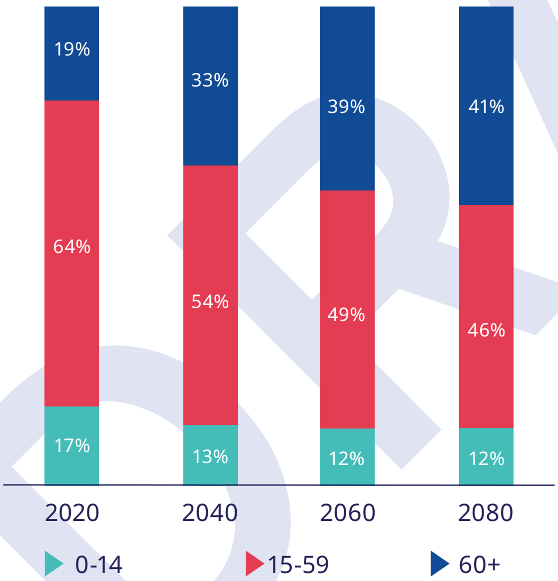
Report Overview

The context for the Thai pension system

Demographic and societal changes taking place in Thailand mean there is growing need to enhance the effectiveness and sustainability of the country's pension system. Thailand is one of the most rapidly ageing countries in the world (Figure 1). While this reflects the fruits of economic and social development, old age is associated with increasing challenges of ill health and disability which reduce the capacity to earn an income (Figure 2). Future generations of older people will be less able to rely on their children than previous generations, and the expectation that government should play a role is growing.

Thailand's population will rapidly age in the coming decades

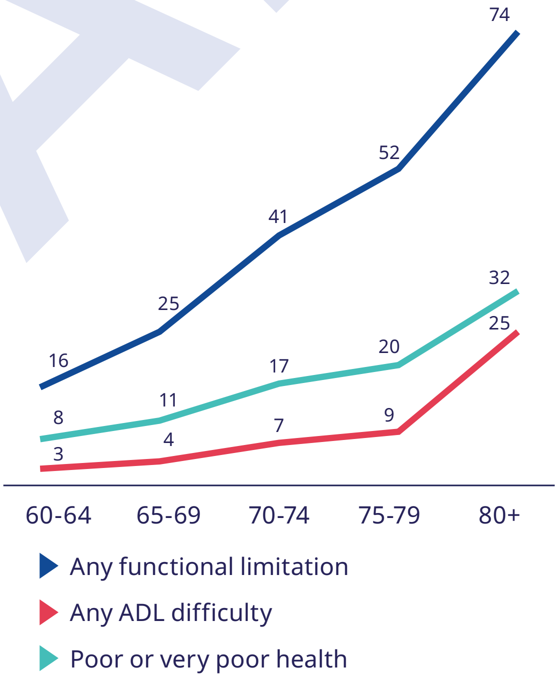
Figure 1: Population by age group, 2020-2080



Source: UN Population Division (2019)

Disability and ill health create barriers to earning an income in old age

Figure 2: Proportion of older people with functional limitations and difficulties with activities of daily living, by five-year age group



Source: Teerawichitchainan et al. (2019)

Pension policy can make a positive contribution to the recovery from the COVID-19 crisis, towards a more robust and sustainable economic trajectory. Recent years have seen a slowing of Thailand's economic growth and – for the first time in many decades – increases in poverty. COVID-19 has provided a further economic setback for Thailand, nevertheless, it has also highlighted the important role that social protection plays in protecting people from risks and shocks, and enabling robust and sustainable economic development. Pensions – as part of a comprehensive social protection system – will play a key role in many of the broader tasks facing Thailand, including boosting productivity, formalising the labour market, and reducing poverty and inequality.

An effective pension system needs to be adapted to the structure and dynamism of the Thai labour market. Half of the Thai labour force is found in vulnerable employment, and slightly over half in the informal economy. Yet the picture is not static. Many workers frequently move between different forms of employment throughout their working lives. The pension system needs to be designed in a way that accommodates workers in this variety of changing work arrangements, while also contributing to formalisation of the labour market.

Assessment of the current Thai pension system

The current array of pension schemes in place in Thailand has many strengths, but also important weaknesses. This report assesses the Thai pension system along the lines of three outcomes of coverage, adequacy and sustainability, as well as the question of policy consistency. It also makes reference to the pension tiers (or pillars) described by the ILO multi-pillar pension framework.

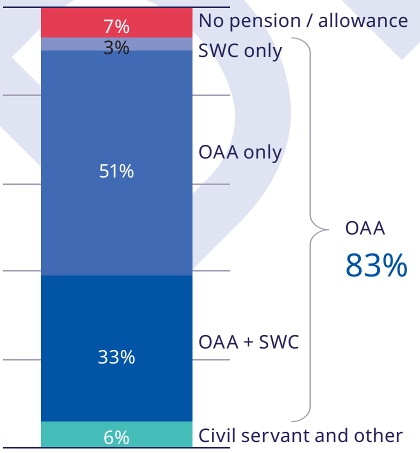
Coverage

Thailand has made considerable progress in recent years to build a near-universal pension system (Figure 3). This success rests heavily on the rapid expansion of the tax-financed Old Age Allowance scheme (OAA) since 2008 which covers around four in five older people. The gap consists of retirees from the civil service (who are not eligible) and a small portion of older people who receive no allowance at all. Over a third of older people also have their income supplemented by the newly introduced State Welfare Card, while a small portion also receive the non-contributory disability allowance.

Coverage of contributory schemes is much lower (Figure 4). The short history of pensions under the Social Security Office (SSO) – initiated in 2000 – means that up to now very few older people receive contributory pensions. An estimated 44 per cent of the employed population is actively contributing to SSO retirement scheme, which promises higher levels of contributory coverage for future generations of older people. There has also been some increase in coverage in the last decade, including via schemes directly targeted at informal workers (the National Saving Fund, and Section 40 of the SSO). However, around half of Thai workers are not regularly contributing to a pension scheme.

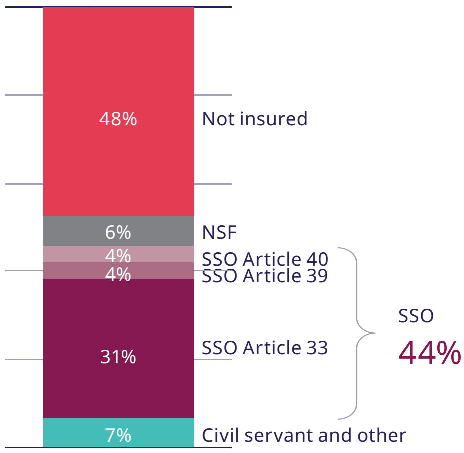
Over 90% of older people in Thailand receive a pension or allowance…

Figure 3: Percentage of older persons (60+) receiving a pension/allowance, by type, 2019



… but only around half are insured by a contributory retirement scheme

Figure 4: Percentage of the employed population insured by old age retirement schemes, by scheme, 2019



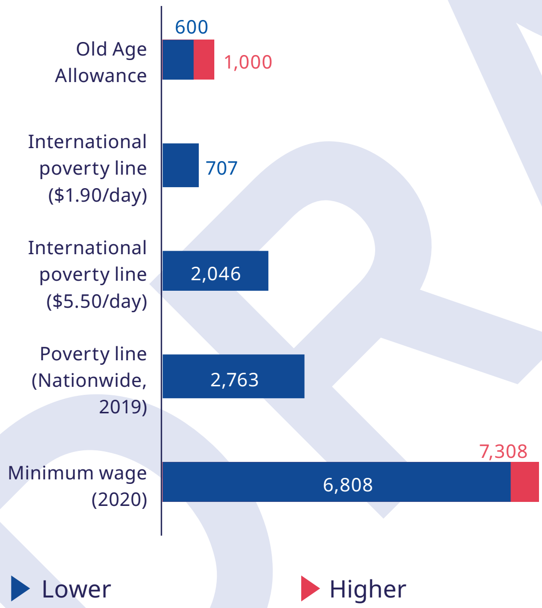
Note: NSF includes all members (not limited to actively contributing members). Under "Civil servant and other", other pensions include private teachers fund and pensions provided to workers in government enterprises.

Adequacy

Despite its high coverage, the benefit level of the Old Age Allowance is low by both national and international standards, and far from providing a minimum pension floor (Tier 0). While the scheme has had an important impact on reducing poverty, it is far from sufficient for an older person to rely on without significant additional income from work and family support. The benefit (of between 600 and 1,000 baht/month) falls well below national and international poverty lines, and is one of the lowest social pension benefits in the region and the world when compared to average income (at 3 per cent of GDP per capita) (Figure 5 and Figure 6). The lack of indexation also means the benefit has lost about a fifth of its real value since the last increase in 2011. The State Welfare Card provides a welcome supplement, however, the low benefit does little to reduce this issue of adequacy and the scheme does not accurately target the poorest older persons.

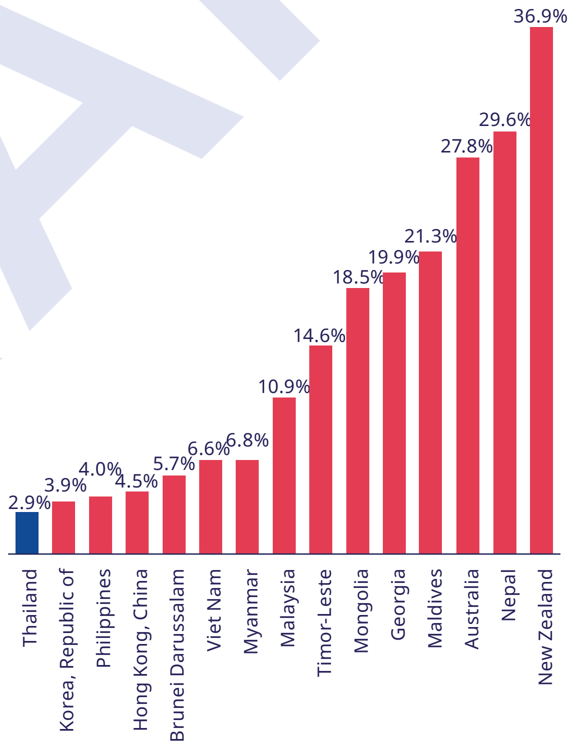
The Old Age Allowance benefit level is low relative to national benchmarks...

Figure 5: Old Age Allowance benefit relative to relevant benchmarks (2019-2020)



...and one of the lowest social pension benefits in the world.

Figure 6: Benefit levels of social pensions for selected countries, % of GDP per capita, latest year

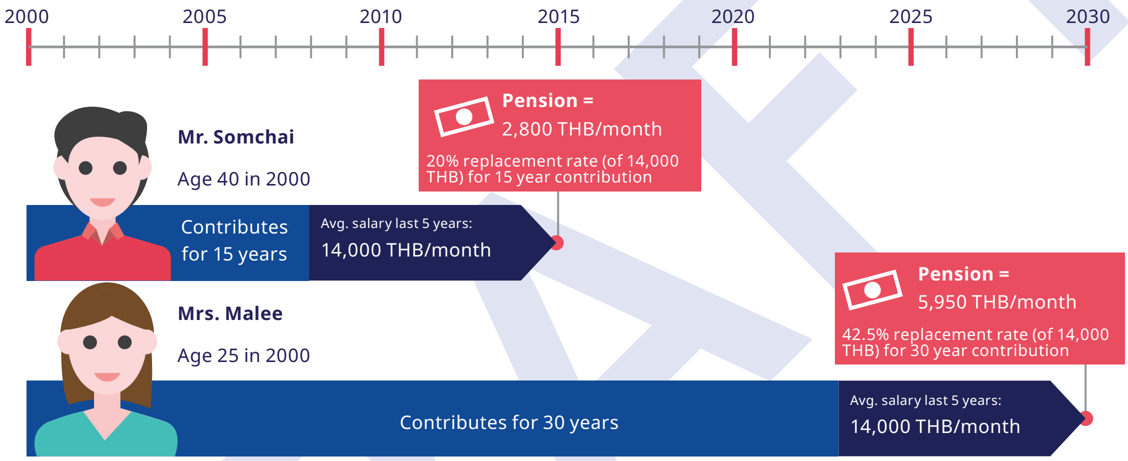


Source: HelpAge International (2018)

In principle, the SSO scheme has potential to provide adequate earnings-related benefits (Tier 1). The SSO pension (Article 33) promises to provide a pension of 42.5 per cent of a worker's previous salary after 30 years of contribution , which can comply with the ILO's Social Security (Minimum Standards) Convention 102. Currently, the short history of the scheme means that benefits for those who have retired are much lower, but this can change over time (Figure 7).

Workers retiring in the future will receive significantly higher benefits than those retiring in recent years

Figure 7: Pension benefit for workers with differing lengths of contribution, but identical wage profiles during the last 5 years of contributions



Nevertheless, some important factors will depress levels of adequacy in future if no action is taken. The most pressing is the salary cap for the scheme (15,000 baht/month) which has never been increased, and is no longer in line with the earning profile of contributors. Other important issues contributing to lower adequacy include low retirement ages, the nature of the pension formula and the fact pension benefits are not indexed to inflation or wages once a member retires.

Saving schemes targeted at informal sector workers are likely to provide low benefits in most cases. The lump sum benefit provided under Article 40 of the SSO will in most cases be small (due to low contributions) and not provide a predictable level of income security during old age. While the NSF provides a periodic benefit for up to 20 years, it is likely that this will be no more than 600 baht/month for most members (and often not lasting the full 20 years), given the low level of contributions made to the fund. Another important issue relates to pensions provided under Section 39 of the SSO, which means that workers who move from formal enterprises to self-employment during their final working years will receive much decreased benefits.

Lump sum benefits exist across the pension system which threaten scheme objectives and create disincentives to members. Lump sum payments are made to workers with short contribution histories under the SSO (Article 33) and civil service pensions, and as the standard pay-out under the Government Pension Fund and Article 40 scheme (SSO). For those receiving lump sum benefits, the money received is often depleted during the early years of retirement, which creates and issue for adequacy of old age retirement income. This, in turn, contributes to issues of financial sustainability issue, as this depletion of savings puts further pressure on other forms of support (such as the OAA and other non-contributory programmes).

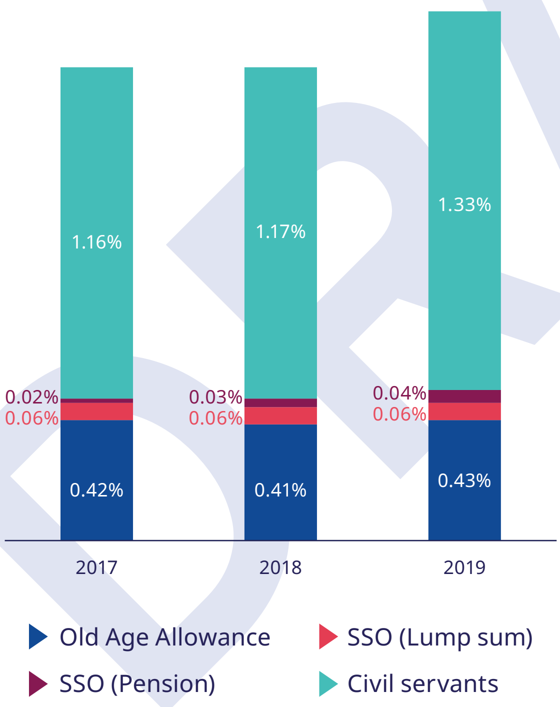
1 Calculated on the basis of the average salary for the last five years

Sustainability

Overall, pension spending in Thailand is relatively low compared to other countries facing similar demographic transitions. Total expenditure on old age pensions and other old age income security programmes currently amounts to 1.8 per cent of GDP (Figure 8), which is below countries such as China, Mongolia, Republic of Korea and Viet Nam. Currently, more than two thirds of this expenditure (1.3 per cent of GDP) is in the form of civil servant pensions, with remaining expenditure dominated by the OAA (0.4 per cent of GDP). The IMF project that by 2060 the cost of the tax-financed civil service scheme would reach 2.4 per cent of GDP, which is significant for a scheme covering a small share of older persons. Despite the universal coverage of the Old Age Allowance, the level of expenditure is modest by international standards (Figure 9). SSO pension expenditure remains small given the scheme only recently began paying pension benefits, but will increase in the coming decades.

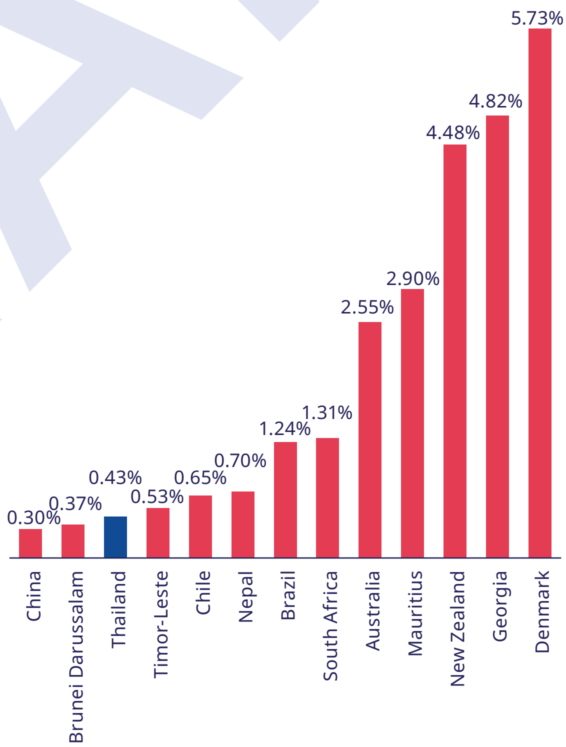
Pension expenditure in Thailand is dominated by civil servant pensions

Figure 8: Total expenditure on old age social protection schemes in Thailand, 2017-2019



Expenditure on the Old Age Allowance is low compared to other countries

Figure 9: Expenditure on high coverage social pension schemes, per cent of GDP, latest year



Source: HelpAge International (2018)

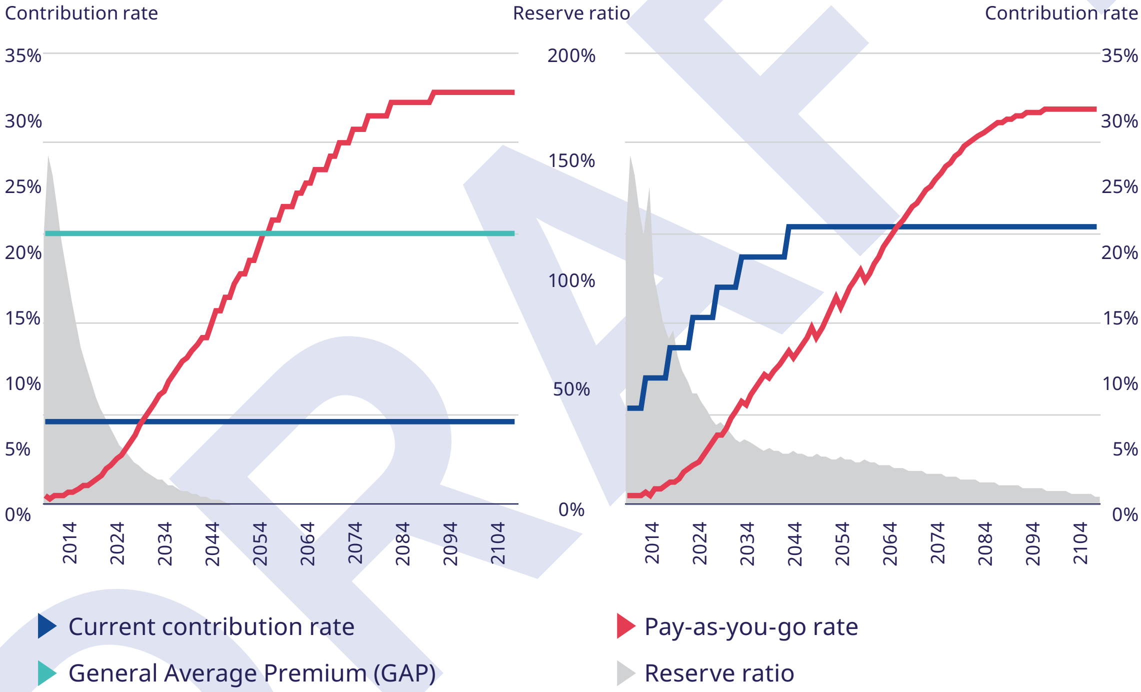
Without action, the financial position of SSO pensions will deteriorate over the coming decades (Figure 10), however, pragmatic gradual adjustments can put the scheme on a strong financial footing. The most recent Actuarial Valuation conducted by the ILO found that gradual increases to the contribution rate and the retirement age would put the scheme on a solid footing beyond the year 2100 (Figure 11). These necessary adjustments are in line with reforms of schemes in other middle and high-income countries.

Without reform, the SSO pension fund reserves will be depleted by 2054...

...but parametric reforms can put it on a sounds financial footing

Figure 10: Key aspects of the financial projection of SSO pensions

Figure 11: Reform scenario with increases to retirement age and contribution rates



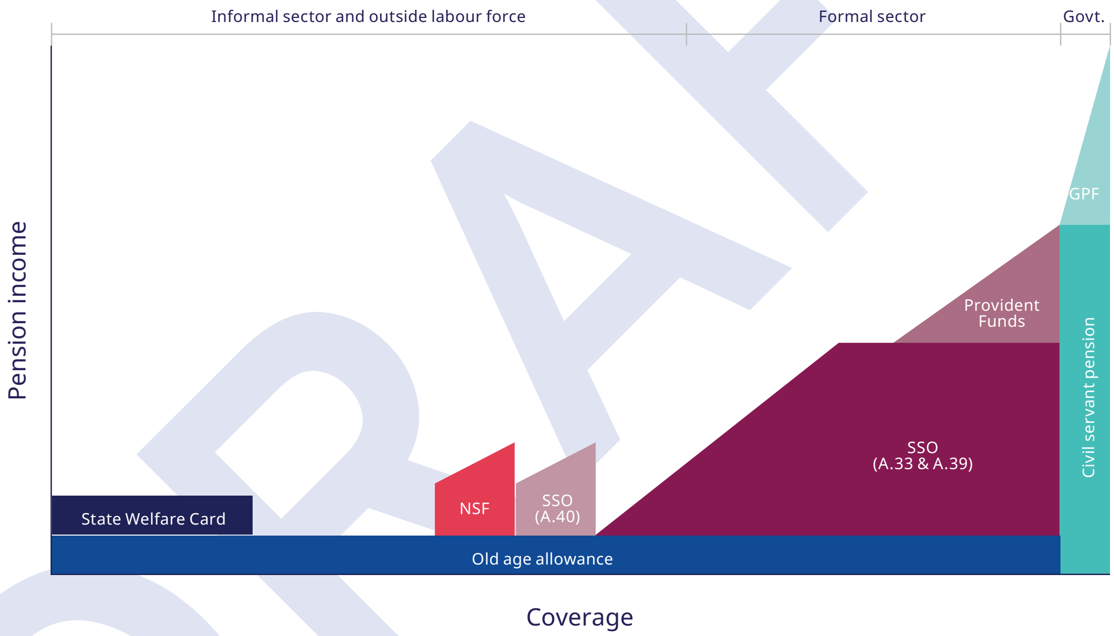
Source: ILO (2016)

Policy consistency and harmonisation

The compartmentalisation of the pension system around different forms of employment is not well adapted to the fluid nature of the Thai labour market (Figure 12). Pension schemes are generally organised according to workers' employment status, which does not recognise the way in which workers move between different forms of employment during their working lives. There is also tendency for fragmentation within the same group of workers. Examples include the SSO Article 40 and the NSF offering similar schemes for informal workers, and the proposed National Pension Fund (NPF) set to exist in parallel to SSO. The decision to make SSO benefits supplementary to the OAA was a positive step, but the two schemes remain administratively separate.

The Thai pension system is compartmentalised around different forms of employment

Figure 12: Illustration of the current Thai pension system



Fragmentation has negative consequences for adequacy, incentives and financial sustainability. Lack of portability between schemes results in situations where workers with long careers and significant contributions to social security may end up with inadequate benefits. Fragmentation also has a financial cost: first, inadequate benefits from fragmented contributory schemes put greater pressure on tax-financed schemes and, second, fragmented decision making can contribute to inefficiencies in the system. An example is the potential for a rapid and significant expansion of the proposed NPF to crowd out the space to put SSO pensions on a sound financial footing (Box 1). It is also a lost opportunity to provide a coherent set of incentives to workers, that can support processes of formalisation.

Box 1: The proposed national pension fund

The Government of Thailand is currently considering the introduction of the National Pension Fund (NPF): a mandatory defined contribution scheme. Once fully implemented, the scheme would mandate all employees in enterprises of at least one or more employees to be members of the scheme.[2] Employers and employees would each make a contribution of 10 per cent of the employee's salary (20 per cent in total), with the option to increase the contribution up to 15 per cent. Contributions would be invested by financial institutions. At reaching the age of 60, members would be able to receive their total savings (plus interest) as a lump sum, or as a pension for a period of 20 years. It is proposed that scheme would be gradually phased in.

While the introduction of a mandatory defined contribution scheme could form a positive element within the pension system the current proposal raises important concerns. These include:

- The impact of the NPF contribution rate on SSO financial sustainability. The proposed contribution rate for the NPF (20 per cent) is not compatible with the SSO contribution rate (around 18 per cent) necessary to ensure the fund's sustainability. The combined contribution rate is unlikely to be politically, socially or economically feasible. There is a risk that the expansion of the NPF undermines efforts to put the SSO fund on a solid financial footing.
- Limitations of lump sum benefits, in terms of adequacy and predictability.
- Fund investment: The success of the NPF will depend heavily on high investment returns, however, the draft NPF Act lacks specificity on these issues.
- Fragmentation: There are important questions as to how the scheme would interact with other defined contribution schemes (GPF and NSF) and the SSO which targets the same membership.

Given these issues and the current economic context, there is a strong case for temporarily delaying the launch of the NPF scheme.

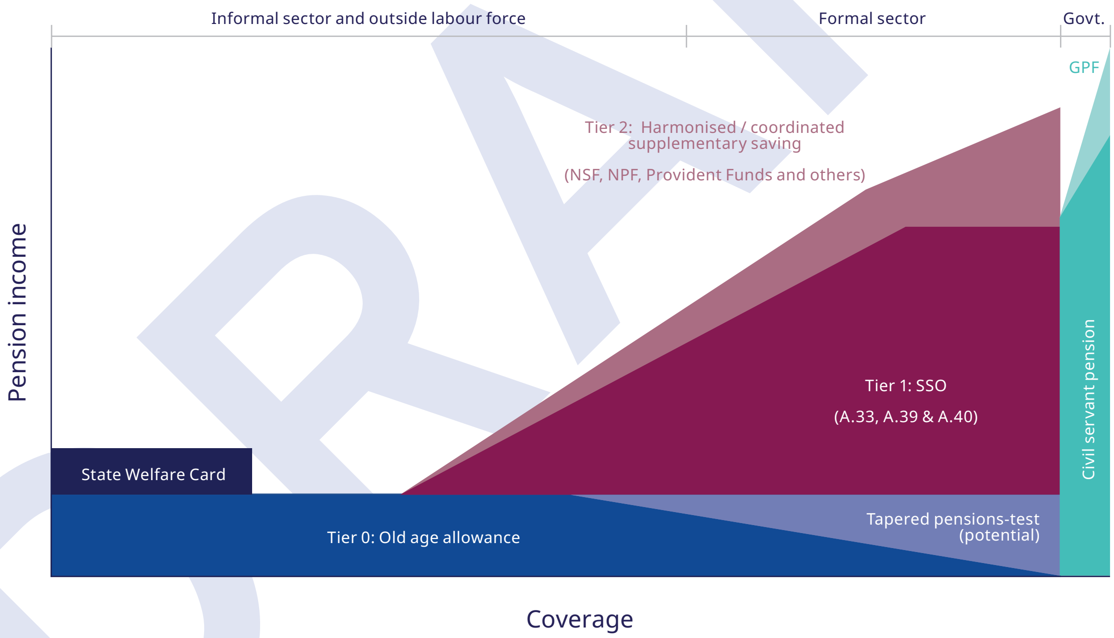
2 Exceptions apply to (1) Government officials and permanent employees of the central government, provincial government, and local government, (2) Director, teachers and educational personnel under the legislation on private schools, and (3) Other fund members or persons in other pension systems as prescribed by ministerial regulation.

The way forward

Based on the analysis of the current system, the report outlines a broad vision for a more effective and harmonised multi-tier pension system. Improving effectiveness would build on the strong coverage of the existing system but seek to build a system that provides adequate pensions in the context of the high levels of informal employment and labour mobility in Thailand. This would involve moving from a system that compartmentalises workers into different categories, to a multi-layered arrangement that can follow workers on a range of diverse career paths (Figure 13). Such an approach would seek to create a more coherent set of incentives for workers and employers, supporting the expansion of contributory schemes and, in tandem, catalysing the transition to the formal economy. An integrated multi-tier system would also create a more efficient pension landscape, enabling a system that provides truly adequate income protection in a way that is financially sustainable.

A multi-tiered pension system can provide a more efficient, effective and coherent landscape for workers in a diverse range of circumstances

Figure 13: Illustration of an outline future scenario for the Thai pension system



While not prescribing a precise set of actions, the report outlines a set of broad elements for a way forward. A range of specific options are set out, although many will require more detailed analysis and dialogue. The key elements of this vision are as follows:

1. **Increase adequacy of the Pension Floor (Tier 0), primarily via the OAA.** This will be critical for the current generation of older people and those soon arriving at their old age who cannot wait for the time needed for the maturation of contributory schemes. There are various scenarios for the design of this floor and the OAA over time, including: the potential for a tapered pensions test (reducing benefits for those with other pension income), the complementary role of the State Welfare Card and disability allowances, and adjustments to the age of eligibility for the scheme.

2. **Reinforce SSO pensions as the core earnings-related scheme (Tier 1) providing adequate earnings-related benefits in a financially sustainable fashion.** This would require adjustments of parameters to strengthen adequacy and sustainability, including: contribution rates; the wage ceiling; the way benefits are calculated; and the retirement age. Previous Actuarial Valuations provide a solid basis for understanding the scope and scale of reforms necessary, and upcoming Actuarial Valuation of the SSO will provide updated guidance.

3. **Modify existing schemes within SSO to extend guaranteed earnings-related benefits (Tier 1) to the non-waged workers.** Such an approach would seek to provide guaranteed contributory earnings-related benefits to workers including those in self-employment and small and medium enterprises. If designed well this could support efforts to formalise the Thai labour market, and provide portability for those moving between different forms of employment. Care would be needed in providing strong incentives.

4. **Build a harmonised set of arrangements for complementary savings (Tier 2). This would rest upon a more robust Tier 1 described above.** The aim would be to locate existing complementary savings schemes (NSF, GPF, the proposed NPF and private Provident Funds) as part of a coherent package. This would seek to be to provide a clearer landscape for savers, greater portability, and better returns on investment. This could involve greater coordination between schemes, or merging of some schemes (or functions within them).

5. **Closer integration of the OAA and SSO.** This would allow the two benefits to be paid as a single pension payment, which could support two key reforms: (a) the introduction of a tapered pensions-test, which could support financial sustainability of the scheme in the long-term and (b) replacing lump sum payments for short contribution histories with pension benefits paid together with OAA benefits. The full report provides a menu of options for greater integration.

6. **Consider greater integration of civil servants into the national pension system.** Options would include creating greater portability between the schemes, aligning scheme parameters, and/or bringing gradually more government employees under the SSO scheme.

7. **An enabling environment for pension reform.** Various initiatives outside the realm of pension policy have an important interaction with the pension system, and can be considered enablers of successful reforms. These fall into two categories:

   - **Policies to accompany increases in pension ages**. These include: (a) labour market policies that support longer working lives for those who can and wish to and (b) strengthening the system of disability benefits (contributory and non-contributory) to support those facing disability before pension ages.

   - **Services and other initiatives to reduced costs for older persons.** These include solutions for long-term care, access to affordable health care and other relevant subsidies such as for transportation.

To guide this process, the report proposes a concrete step forward would be to develop a national strategy on pension system reform to articulate a clear vision for the pension system in Thailand. Such an approach would involve moving beyond scheme-level discussion to consider the shape of the pension system as a whole. This would involve bringing together all actors involved in the pension system, and exploring specific reform proposals in more detail.

Nevertheless, the report also proposes immediate adjustments to the pension system to increase its effectiveness straight away. This would contribute to three outcomes (1) increasing the immediate income security of older people, (2) increasing the faith in the pension system by increasing levels of adequacy and (3) providing a boost to household income that can contribute to the wider recovery from COVID-19.

What could reforms mean for individuals?

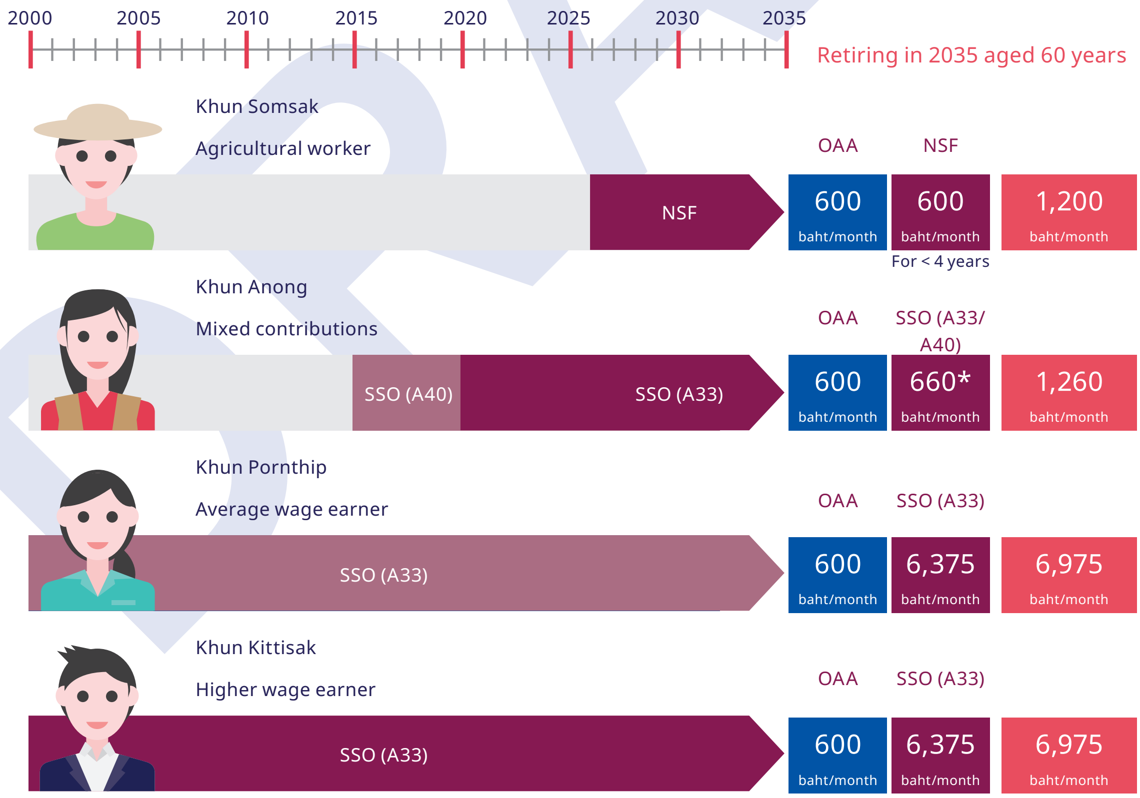
In order to illustrate the potential impact of pension system reforms, this final section considers how some of the proposed reforms would affect individuals with different profiles. All individuals are assumed to retire from the labour force at age 60, in January 2035. The figures below show the situation with and without a set of reform options which include:

- **Increasing the OAA** to 2,000 baht/month for older persons aged 60 and over (and indexed to inflation)
- **Pension benefits** are offered to SSO recipients with short contribution histories (using the accrual rate of 1.33% per annum).
- **An increase in the SSO contribution ceiling** to 20,000 in 2021, and indexed to average wages thereafter.
- **A tapered pensions test.** The OAA benefit is reduced by 1 baht for every 3 baht of SSO pension above 4,000 baht/month.

These options should be considered illustrative, and specific options required further analysis and dialogue.

Pension reform results in significantly higher benefits for workers in a range of circumstances

Figure 14: No reform



* Value of monthly amount for Khun Anong is the total value of lump sum benefits (207,858 baht) divided by female life expectancy for 2035-40 (26.2 years)

Figure 15: With reform

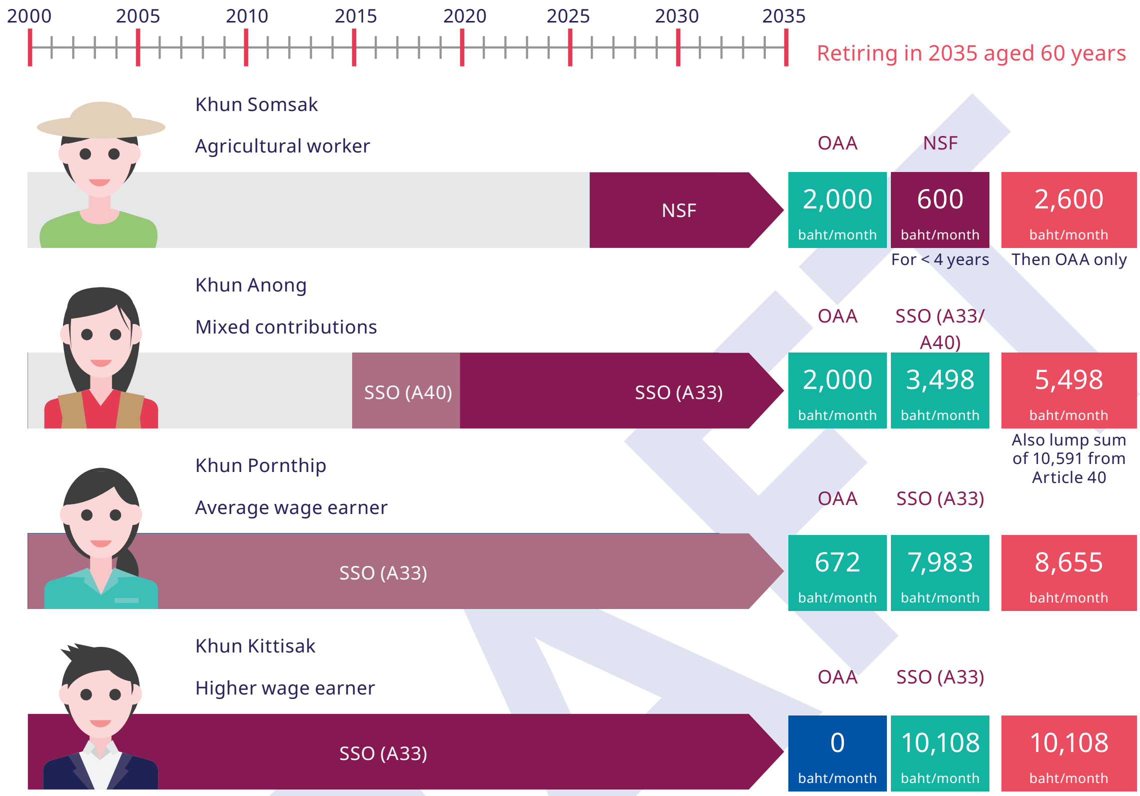


Table 1 describes the individual scenarios and why the benefits they receive are higher. A more detailed explanation is provided in the full report.

Table 1: Individual profiles and benefits received with and without reforms

Profile		Impact of the reform
	Khun Somsak is an agricultural worker who spends most of his life outside the social protection system. At age 51, in 2026, he decides to join NSF, contributing 100 baht per month (with a 100% match from government) every month up to his 60th birthday.	An increased OAA benefit brings Khun Somsak's pension benefit much closer to the poverty line. However, he still only receives the NSF benefit of 600 baht/month for around 3.5 years. This low benefit level is due to the small contributions made over a short period.
	Khun Anong starts work as a self-employed street vendor at age 41 after many years out of the labour force caring for her young children. She contributes to Article 40 for 5 years before gaining formal wage employment at age 46, earning the average wage*. She then contributes to SSO Article 33 for 14 years before retirement.	Without any reform, Khun Anong is unable to claim a periodic pension from SSO due to not meeting the 15 years minimum contribution. She therefore receives two lump sum benefits (from both Article 33 and Article 40), with low adequacy across the years of retirement. By extending pension benefits to those with shorter contribution histories, the reform significantly increases her SSO pension. The increase in the OAA also gives a substantial boost. Her situation could be further improved by integration of Articles 33 and 40.

Profile		Impact of the reform
	Khun Pornthip has a formal sector job earning the average wage* and contributes consistently to SSO Article 33 from 2005 to the end of 2034.	While Khun Porthip's wage is below the contribution ceiling in 2020, by 2034 it is significantly higher (19,610 baht/month). Increasing the contribution ceiling increases the SSO benefit significantly. The higher SSO benefit means she is affected by the tapered pensions-test for the OAA included in the reform. However, the 672 baht/month OAA benefit she receives is still higher than the benefit without reform.
	Khun Kittisak also has a formal sector job, but earns 5,000 baht/month above the average wage*.	Despite the higher wage, Khun Kittisak's pension benefit from SSO is the same as Khun Pornthip as – for both – it is calculated relative to the contribution ceiling. The increase in the contribution ceiling significantly improves his SSO pension. The higher SSO benefit and the tapered pensions-test for the OAA means that he receives no OAA.

* The average wage in 2020 was 14,460 (LFS 2019). For future benefit calculations it is assumed that average wages will grow by 2.2% per annum in real terms. The average wage in 2034 is assumed to be 19,610 (in 2020 prices) and the average across the 5 years before retirement 18,784.

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