



Reforming the Pension System in Thailand

Current Pension System

As one of the developing countries, Thailand is faced with a rapidly aging population due to demographic transformation resulting from falling fertility rates and rising life expectancies. Currently, the retirement system is confronted with a continuous increase of the old-age dependency ratio, eventually pushing the Government to consider reforming the current pension system. While Thailand has a well-developed social protection system, a fragmented structure and weak legal and regulatory framework hamper it from fully realizing its objectives. In addition, several factors, such as an aging population, low contribution rate, and a high accrual rate, are threatening the system's sustainability.

In publicly managed, unfunded, or first pillar pension scheme, also known as a pay-as-you-go (PAYG), the contributions of the current generation of workers pay the pensions of current pensioners. Such scheme, however, can result in problems in the long run specifically in terms of financial balance and sustainability of the pension system. Many countries across the world with PAYG schemes have introduced, or are planning to introduce, a mandatory privately-managed, fully-funded, and defined-contribution second pillar pension scheme, providing individual accounts. Moreover, through income tax concessions, many countries encouraged so-called third pillar pension schemes comprising private or occupational pensions.

Reforming the Pension System through ADB Assistance

With the sharp decline of birth rates coupled with rising life expectancy, the Government of Thailand accorded high priority to the reform of its pension system. The basic pension (Pillar 1) provided by the Old Age Pension (OAP) office was insufficient as it replaces only 35% of the average pay for pensioners. Hence, there was a need to

introduce a defined mandatory contribution (Pillar 2) to supplement the OAP with a target replacement rate of another 15%–20% of average pay for a total replacement rate of 50%–55% of average pay—deemed an adequate pension to prevent poverty in old age.¹

The Government also considered it important to encourage savings necessary to stimulate financial and capital markets' development as well as labor market efficiency. Consequently, it carried out a systematic analysis of pension issues and options through a technical assistance on financial sector reforms provided by the Asian Development Bank (ADB) in 1997. Based on this, in 2000, the Government formally approved an action plan for the introduction of Pillar 2 and authorized further work to determine its design and the time frame for its implementation.

In support of reforming the pension system in Thailand, ADB provided another technical assistance (TA) in 2002 to help develop a pension system that is institutionally sound, socially adequate, and financially sustainable over the long run and providing maximum social protection at the least cost in terms of budgetary resources and allocative distortions.² The TA was intended to prepare the groundwork for expansion or introduction of the mandatory provident fund system (Pillar 2), establishment of an independent supervisory and regulatory body, and was relevant to the need for pension reform of the Government.

The technical assistance contributed to the Government's deeper understanding of the complex issues associated with the design of a comprehensive pension system.



Recommendations Toward a Sustainable Pension System

The TA resulted in important recommendations on how the Government of Thailand can further proceed on adopting a sustainable pension system. In particular, the TA contributed to the Government's deeper understanding of the complex issues associated with the design of a comprehensive pension system. It also noted the need for ADB to continue supporting the Government in the remaining two phases of the pension reform once the Government decides on its implementation.

Through the TA, a system was developed for the delivery of annuity products and instruments. This system will be operated in conjunction with the existing OAP System, Provident Fund System (which includes

Retirement Mutual Funds), and a mandatory system. A draft legislation was also formulated for the establishment of the Mandatory Provident Fund and creation of a Pension and Provident Fund Agency, the supervisory and regulatory body of the pension system. A National Provident Fund Preparatory Committee (NPF Working Group) was established as part of the NPF design and implementation efforts. Recommendations were also made for creating a NPF for formal sectors as well as modifications to the existing OAP, integration of OAP and NPF, together with all existing Thai pension systems to promote labor mobility. The creation of a Pension and Provident Fund Authority to regulate all Thai pension programs was also recommended.³

Endnotes

- ¹ Asian Development Bank. 2008. *Technical Assistance Completion Report on Pension System Design (TA 4011-THAI)*. Manila.
- ² ADB. 2002. *Technical Assistance to Thailand for Pension System Design (TA 4011)*, December 2002.
- ³ ADB. 2008. *Technical Assistance Completion Report on Pension System Design (TA 4011-THAI)*. Manila.

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