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Fact Sheet(

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China: building a three-pillar system[1]

Historically, pensions in China were provided by the state-owned enterprises. Since the late-1990s, however, China's pension system has seen far-reaching structural reforms, as the government strives to adapt to changing demographic and economic conditions.

With regard to the demographic outlook, the Allianz Global Investors report shows that the population is ageing rapidly due to reduced fertility and increasing longevity. The old age dependency ratio – the number of persons aged 65+ for every 100 people of working age (15-64) – will rise from its current level of 11 to 39 by 2050.

A significant consequence of China's economic growth has been the trend towards urbanisation due to the growth of industrialisation and the development of a major service sector. The subsequent fragmentation of the extended family is weakening the informal financial support system, whereby workers provide for parents in their retirement or old age.

As a result of these developments, it was essential for China to implement formal pensions plans. To date, reform has focused on the urban areas. Here, the two main funded systems are the mandatory "1B" individual funded accounts section of the public pension system, and enterprise annuities (EAs), which are voluntary occupational plans that can be run by employers participating in the public pension system. There is also a national reserve fund to help support the pension system in future. In more detail:

- In 1997, a mandatory public pension (social insurance) system was introduced for urban areas. The public pension (social insurance) system is in two parts:
    - 1A is defined benefit (DB) pay-as-you-go, funded by employer contributions of 20% of wages.
    - 1B is a system of individual defined contribution (DC) accounts, funded by employee contributions of 8%. At present 141.3 million employees participate, representing 50% of the urban workforce. Initially, 1B suffered when local governments used the capital in accounts to cover deficits and to pay benefits related to 1A. This "empty accounts" problem is now being addressed through fiscal transfers from local and central government.

[1] For full details, see the section on China in *Asia-Pacific Pensions 2007*, starting on p. 38.

- In 2004, the enterprise annuity (EA) was launched – a voluntary occupational defined contribution (DC) plan, which is expected to become the main private pension arrangement in the urban workplace. The maximum employee/employer contribution is one-sixth of total wages. Only licensed financial institutions can manage these funds. Quantitative investment restrictions apply, for example investment in equities is capped at 20% at present.
- "Legacy" voluntary occupational funds that pre-date the EA are being transferred from state social security bureaux to private sector financial institutions. Technically, these legacy funds are classed as part of EA assets.
- In 2000, the National Social Security Fund (NSFF) was launched to cope with the impact of demographic change on the pension system. This is funded by fiscal transfers from central government, proceeds from the stockmarket listing of state-owned enterprises, lottery proceeds, and investment income. An increasing element of the fund is outsourced to external asset managers – 37.3% in 2006, up from 24.1% in 2003.
- Individual voluntary pensions do not qualify for tax relief and this market is underdeveloped at present, although research suggests that up to 50% of people in the urban areas are willing to buy retirement products. Life assurance products benefit from modest tax relief.
- Participation in the rural pension system is voluntary and at present coverage is low with about 54 million members in 2003, representing just 9% of the rural population (compared with 50% coverage in urban areas). In 2006 a pilot scheme was launched in rural Beijing to raise participation rates.

Allianz Global Investors expects pension assets in China to grow dramatically by 2015:

- 1B accounts, currently worth EUR 53.4 billion (RMB 549 billion), are expected to grow at a compound annual growth rate (CAGR) of between 23.4% and 25.6%. Assuming a CAGR of 25.6%, funds will grow to EUR 414.4 billion (RMB 4.3 trillion) by 2015.
- Enterprise annuities, currently worth EUR 8.9 billion (RMB 92 billion), 82% of which is in "legacy" funds), are expected to grow at a rate of 21.2% to reach EUR 49.8 billion (RMB 512 billion) in 2015.
- NSFF, currently worth EUR 27.5 billion (RMB 283 billion), could grow to EUR 97 billion (RMB 1 trillion) over the next two decades but the rate cannot be predicted with any certainty, as the fund is subject to political decisions.

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