Retirement After the COVID-19 Crisis

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Introduction

After almost six decades of planned development and the emergence of the formal employment sector, retirement planning in Bhutan remains very sketchy, both at national and at individual levels.

At the individual level, perhaps this has to do with the strong social safety net in the form of our extended family system and community vitality that has been part of our socio-cultural landscape. At the national level, Bhutan has a very young population and we are currently reaping its demographic dividend. Therefore, ageing has never featured in our policy-making and planned programmes.

However, things are changing and will continue to change. Our traditional social safety nets are breaking down and can no longer be a source of comfort, either for us as individuals or for policy makers. Our largely agrarian society with large extended families surviving on subsistence farming has changed, and younger generations of Bhutanese have transitioned to the childhood-education-working-retirement model. The extended family system -- the mainstay of our social safety net in terms of home-based child and elderly care system -- has given way to the nuclear family. While it has not happened in terms of elderly care, our childcare system is rapidly becoming institutionalised.

As per the national report of the Population and Housing Census of Bhutan, 2017, the median age of our population increased from 22.3 in 2005 to 26.9 in 2017. As per the report, "an increase in median age is observed when there is declining fertility and increasing life expectancy in a country. This increase shows that even though the population is still youthful, it is steadily getting older."

The Ageing Index, which is the ratio of the number of persons aged 65 years and above for every 100 persons aged under 15, has also increased, from 14.2 in 2005 to 22.7 in 2017. This means that, in 2017, for every 100 persons under the age of 15, there were approximately 23 persons who were 65 years and above.

The age dependency ratio is another indicator that looks at the economic burden borne by the productive population, which is the sum of the child dependency ratio and the old age dependency ratio. It may be worthwhile to report that, while our child dependency ratio is falling, our old age dependency ratio has increased, from 7.5 in 2005 to 8.7 in 2017.

These facts are indicative of the current opportunities in terms of our demographic profile that will allow us long-range planning, but they also show that we cannot ignore the fact that our population is steadily ageing. Against the backdrop of these indicators, we have to be increasingly aware of the need for a planned approach to retirement, and prepare for an inevitable future.

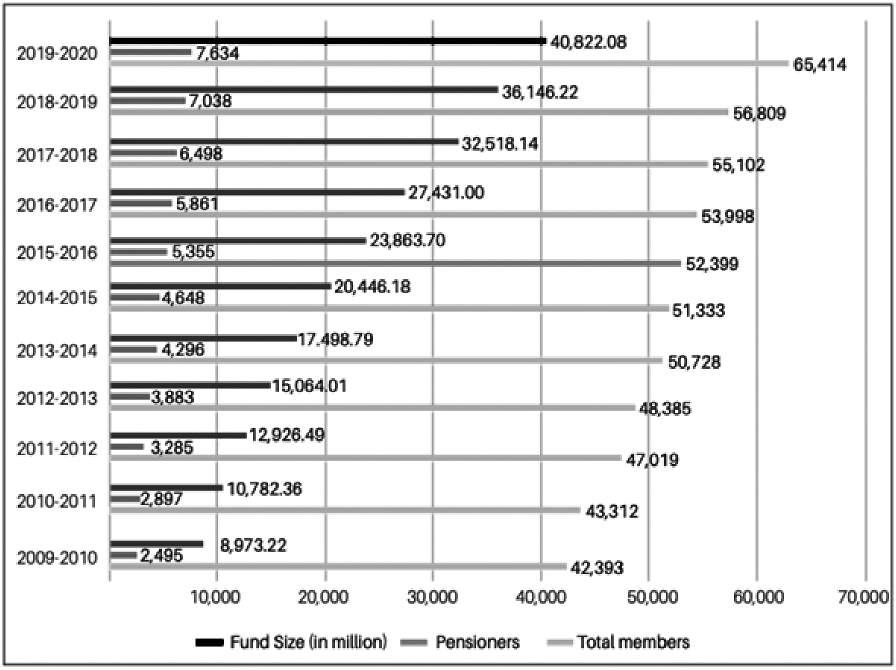
The Existing System and its Systematic Issues

The foundation for a retirement system in Bhutan had been in place as far back as 1962, with the introduction of the Gratuity scheme, but it underwent many revisions. Today, a retired public servant receives a lumpsum gratuity payment based on the formula of the last basic pay and the number of years in service (without any ceiling).

In 1976, the Government Employee Provident Fund (GEPF) was introduced as a formal mechanism to institute a retirement scheme, and was managed by the Royal Insurance Corporation of Bhutan Limited (RICBL). The current retirement system has been restructured from the GEPF, based on a Royal *Kasho* issued by His Majesty the Fourth Druk Gyalpo to enhance the retirement scheme for public servants.

The National Pension and Provident Fund (NPPF) was established to administer and manage the civil service pension, and provident fund schemes available to civil servants and public servants in State-owned Enterprises, and the armed forces pension and provident fund schemes available to members of the armed forces in Bhutan.

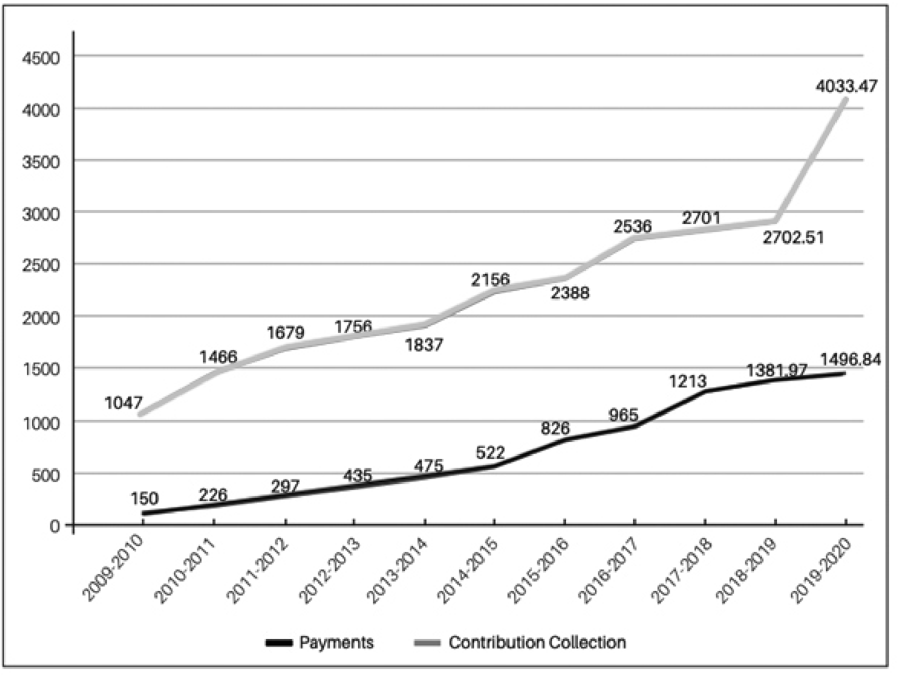
The NPPF today administers a combination of Defined Benefit (DB) and Defined Contribution (DC) schemes, available to members upon retirement. It is structured as a Pay as You Go (PAYG) scheme, the structural basis of a public pension scheme, carrying the implicit guarantee of the State, should the pension fund ultimately face funding shortages.



Source: Annual Report, 2019-2020, National Pension and Provident Fund

The above table shows how the NPPF has grown over the years. As of June 2020, it caters to more than 65,000 active or contributing members, and provides pension benefits to more than 7,600 individuals. The total fund size (DC and DB funds) at the end June 2020, stands close to Nu. 41,000 million. What can be summarised from the above table is that, as of today, the number of contributing members far exceeds the inactive members or pensioners and, therefore, it is contributing to the substantial growth in the fund size.

The following graph also supports the above data, wherein it shows that contributions coming in far exceed the payments being made to pensioners and exiting members (DC members who take lumpsum amounts). However, it is noteworthy that, while the contribution rate is increasing at a smaller percentage (average of 10% over the last 10 years), the growth in the rate of payments is much higher (average of 21% over the last 10 years). The steep spike in the contribution of Nu. 4,033 million in the year 2019-2020 is mainly on account of the increased contribution rate with the revision of salary. The impact (increased) on payouts is a lagging indicator, which will come in the latter years.



Source: Annual Report, 2019-2020, National Pension and Provident Fund

The national statistics of the Population and Housing Census of Bhutan and those of the NPPF corroborate the story of a country that is at the peak of enjoying the "demographic dividend". However, it will wane over time, and the pension fund will be faced with the issue of sustainability.

Often, when the sustainability issue of the current pension fund is raised, there seems to be a general lack of awareness. It must be understood that all contributions made by members have been accumulated, invested, and grown over time, which is evident from the above statistics. As the population ages, as well as the members, the fund will start experiencing a reverse scenario. The number of pensioners will overtake the number of contributing members, and payments will exceed the contributions coming in.

In such a situation, at some point in time, the fund will completely deplete. Perhaps because humans have myopic tendencies, there seems to be a lack of appetite to acknowledge such future scenarios and take proactive actions to prevent problems, until we collide head on with the problem itself. Such is the issue when we talk of the sustainability of pension funds.

On reflection, the current retirement system was designed and implemented at a point in time when the civil service and the armed forces were the only formal as well as major forms of employment in the country. These retirement schemes have been in existence for over two decades, during which the country witnessed rapid socio-economic development.

Over time, with the development of the private sector, the Labour and Employment Act mandated the provision of a retirement benefit scheme for employees in the formal private sector. However, the application of such schemes is for the formal sector with the employment of five or more people. There is also a lack of incentives to encourage people to save for retirement, in that retirement accounts can be liquidated when people change jobs or take temporary resignation. The nature of lumpsum withdrawal of funds upon retirement also really do not serve the actual purpose of providing for consistent income during old age in the retirement period.

The retirement system in Bhutan lacks the coherent framework of a holistic system. The legal and regulatory framework surrounding retirement benefit schemes in Bhutan is fragmented, with a very sectoral approach to the provision of retirement schemes. For example, the Labour and Employment Act of Bhutan has a section that mentions that an employee, upon retirement from service, shall be entitled to a gratuity and Provident Fund or Pension. The Civil Service Act of Bhutan has no such provision; pay and allowances of civil servants are left to be determined by the government. The Pay Revision Act of Bhutan, applicable to the civil service, has provisions on contribution rate, pension payout, and ceiling, as well as the eligible gratuity on retirement.

It is clear that the current legal framework promotes contributory schemes in the formal sector, and there is no holistic legal framework that takes a "whole of population" approach to retirement schemes in Bhutan. Ageing is a reality for everyone, and all people desire a peaceful and dignified old age dedicated to spiritual pursuits, especially in the case of many Bhutanese.

It must also be understood that, with the growth, development and diversification of economic activities, the public service is limited as a source of employment, and the private sector is increasingly touted as the growth engine of the economy. Within the private sector, there exists formal, informal and semi-formal set-ups. As the younger generation come of age, there is also a surge in the gig economy. Therefore, an inclusive retirement system must also be able to cater to all these varying groups, with the main purpose of securing the retired life of all the people in their old age and preventing old age poverty.

The current system is structured as a PAYG system, which is usually in the nature of a public pension system. However, the system caters to select occupational groups that cover only around 8% of the population. A PAYG system is problematic because it is unfunded, meaning that there is no earmarked assets or fund to cover the pension benefits when the incoming contribution from active members is not enough to pay benefits to pensioners.

The NPPF estimates a contingent liability build-up of close to Nu. 29,000 million on account of the current pension system, which is guaranteed by the State. This means that, as on the date of the valuation, if the pension fund is closed, approximately Nu. 29,000 million is not covered by the assets accumulated from the contributions received, which implicitly is covered by the State guarantee. A system like the PAYG usually does well when the population is young, with the debt problem starting to arise once these young workers migrate to the aged category. It is, therefore, evident that the contingent liability will continue to grow unless reforms are undertaken to correct the system.

The current system is unsustainable and unaffordable for a small country like Bhutan on many grounds. On the macro-economic and public finance aspects, it builds up public debt (as mentioned above), the burden of which is borne by the younger generation, leading to inter-generational equity issues. Moreover, a system that caters to an exclusive group with the burden arising out of it shared by the entire population can cause socio-political issues that can be very costly for the country. It need not be emphasised that the so-called "demographic dividend" will wane, as explained earlier. Such a system can collapse under the weight of an ageing population, again with painful consequences.

The issues surrounding governance and regulatory framework are very subtle and tricky. Because of the lack of a holistic legal framework, there is, at best, quasi-regulation, poor governance, and lack of capacity across the board in the proper understanding of regulation and governance of such a system, which can have serious long-term consequences.

Way Forward

Bhutan is a developing country, and our development priorities are numerous, competing for resources. At the same time, there are many reasons why we can be hopeful. For one, as His Majesty the King has always emphasised, our smallness is our biggest advantage. We should be able to take all our people under one umbrella and design a retirement system that is robust and dynamic in meeting the needs of our elderly population.

The draft report of the 21st century economic roadmap has laid out an ambitious vision for Bhutan to attain high-income nation status by 2030, which is very good news. Aligned to this vision, perhaps, it is time that we also design a roadmap for the development of a dynamic retirement system to meet the needs of the population of a 21st century Bhutan.

A retirement system for a country cannot be planned separately from the economic development of the country, since retirement plans do carry costs. Cases from Scandinavian countries show that a decent retirement plan for old age means that citizens pay high taxes to fund it. Globally, countries have moved to a multiple pillar retirement system. The tendency has been to move away from a PAYG system for an occupation pension system. Therefore, the following are recommended as a way forward.

1. Study and adopt an appropriate multi-retirement system by referring to some global best practices. Consideration can be made for the following:

   Pillar One -- a State-funded public pension system that is either universal or means tested. This pillar will form the foundation or the base pension, and it will be a national pension system. Based on affordability of the State, it can either be a universal pension available to all the population or to a targeted group (usually means tested for certain income levels) once they meet the retirement criteria.

Pillar Two -- an occupational pension scheme that is pre-funded and contributory. For example, in Canada, the Ontario Teachers' Pension Plan is the largest single occupation pension plan (for teachers) in Canada and, by regulation, it is required to always keep enough assets to meet its long-term pension obligation.

In this light, perhaps the current pension system in Bhutan, administered by the National Pension and Provident Fund for the few occupational groups, can be reformed so that it takes the shape and form of an occupational pension system. With strict regulatory requirements under an occupational pension scheme, one of the basic requirements is also the need for automatic adjustments in parameters. For example, as the life expectancy of people increases, countries also adopt an increase in the retirement age of people, so that active working years are made longer while years spent in retirement are shortened.

Pillar Three -- private pension schemes, or voluntary schemes, which encourage people to save, in addition to the above two schemes, for their retirement. This will be purely voluntary and can be accessed by people who can afford to save.

2. Design a robust legal, regulatory, and governance framework that promotes a dynamic system, while shielding it from political influence and conflicts of interest. Pension and insurance organisations are very different and complex players in the financial system. Most often, it carries inherent long-term risks which are not apparent in the short and medium terms. Therefore, regulation must be able to address such issues, helping people to protect their savings and secure their old age. For example, in some of the matured systems, regulation requires occupation pension plans to maintain a minimum of 90% funding level to protect members. It must also be mentioned that collective savings like pension funds are valuable resources that can be channelled to finance economic development of a country. Therefore the legal, regulatory, and governance aspects -- while ensuring that funds are correctly channelled for growth and investments -- must also be shielded from political interference, for long-term stability and general health of the system.

3. Financial market innovation to enable investment of retirement funds, since all accumulated funds must be invested and grown to ensure a healthy retirement system.

4. Retirement literacy programmes to enable people to plan for their retirement, as part of the larger financial inclusion programme. An average individual is a bad financial planner, especially when it comes to retirement, which is seen as being too distant in the future, until caught off-guard when an impending retirement date looms. Therefore, such financial education must be started as early as possible to help people approach it systematically.

In conclusion, Bhutan is a generous country, with free education and health being our greatest blessings, bestowed on us by our benevolent Kings. These are major aspects of State-financed social protection for citizens, enabling individuals to progress towards growth and development without having to worry about financial burden.

The discussion on the need for an organised retirement system and its financing heralds the dawn of a new reality that is a combination of the progress and milestones the country has achieved, the breakdown of certain social norms and the ever-changing expectation of citizens of its government. At the end of the day, a retirement system that enables our elderly population to lead a life of dignity, free from financial worry or poverty, is perhaps at the heart of our development philosophy of Gross National Happiness.

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