

An Open Letter to Members of the Legislative Council on Retirement Protection

7 March, 1995

Dear Legislator:

In the LEGCO tomorrow members will decide whether to support the motion to urge the Government to introduce as expeditiously as possible a mandatory, privately managed occupational retirement protection system with provision for the preservation and portability of benefits. The issue of retirement protection has been discussed for a long time in the community without result. We believe the current proposal is the best way forward for providing meaningful protection for retirement. It is a sound approach and avoids the disastrous problems that have inflicted retirement protection and old age pension schemes the world over. We urge you to support the proposal for the following reasons:

(1) One key consideration in setting up any retirement protection system is the rate of return. The rate of return on privately managed retirement funds have been high in Hong Kong over the long run. Even poor performing funds have an average return of 4% after inflation. Average performing funds have a return between 7-8% after inflation. These rates of return surpass the performance of the Central Provident Fund in Singapore with a return of 2% after inflation. These rates of return are far better than that implicit in the Old Age Pension Scheme proposed earlier by the Government. This is not surprising because in privately managed retirement schemes, funds are invested, generating investment returns and creating wealth, whereas in the Old Age Pension Scheme, funds are transferred from one generation to the next with no wealth being created through investment.

(2) A high rate of return on investment is particularly important for the poor with little savings, because it provides them in the long run with the biggest bang for each dollar they save.

(3) Another concern is the issue of risk that arises from bad investment decisions and fraud. In fact, both centrally and privately managed provident funds are exposed to such risk without exception. The key issue here is incentives for prudent risk management. Guarantees backed by the government using the public purse encourage fund managers to take excessive risk and should not be supported. We are convinced that privately managed retirement funds that compete with each other and operating under a proper regulatory framework provides adequate incentives for prudent risk management.

(4) In the final analysis, the nature of government guarantee amounts to providing an almost risk free rate of return, for example, the long term deposit interest rate. This can be easily provided for even when retirement funds are privately managed in two simple ways. First, by allowing individuals to choose to invest some proportion or all of their savings in funds that only hold almost risk free assets such as fixed deposits. Second, by requiring investment funds to purchase a co-insurance policy that would guarantee some specified low risk rate of return.

(5) A provident fund system does not address the problem of inadequate old age provision for those who have already retired or are near retirement age. We believe that there is a good case for relaxing the restrictions of the public assistance scheme and enhancing the cash payments to the elderly. Such provisions should be means tested to achieve equity and efficiency in the spending of public revenue.

(6) We believe that enhancing the public assistance scheme will not lead to unlimited growth in entitlements provided that the mandatory, privately managed provident fund system is in place. Once the system is implemented and in place, we believe the Government will be more receptive to improving the benefits for the elderly poor under the public assistance scheme because its financial commitment will be controllable and not unlimited. On the other hand, if the present motion is not supported by the LEGCO, it may be several more years before the Government or the future SAR Government will come back again to address this issue. Our elderly poor will be left waiting again. For this reason it is important to have the system established as soon as possible in the interest of the elderly poor of today.

Signed:

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