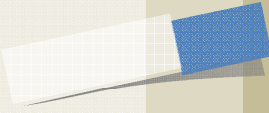# The elderly poverty and the reform of the public pension system in Korea

Kim, Won Sub (Korea University)

# Contents

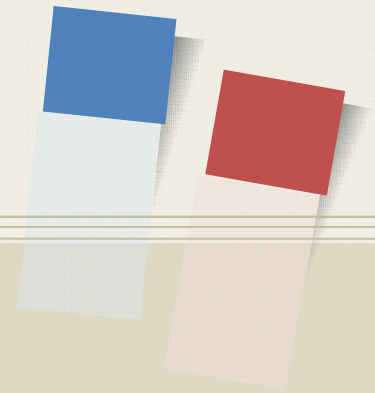# I. CHARACTERISTICS AND COURSES OF ELDERLY POVERTY IN KOREA
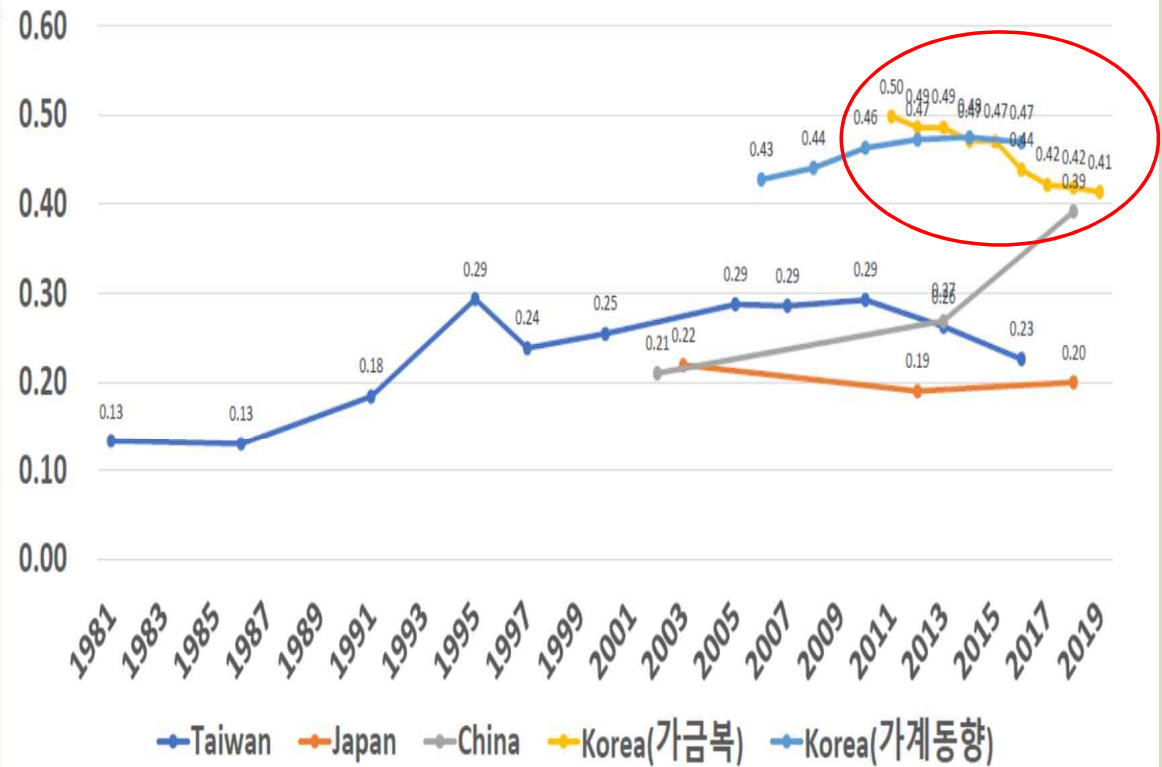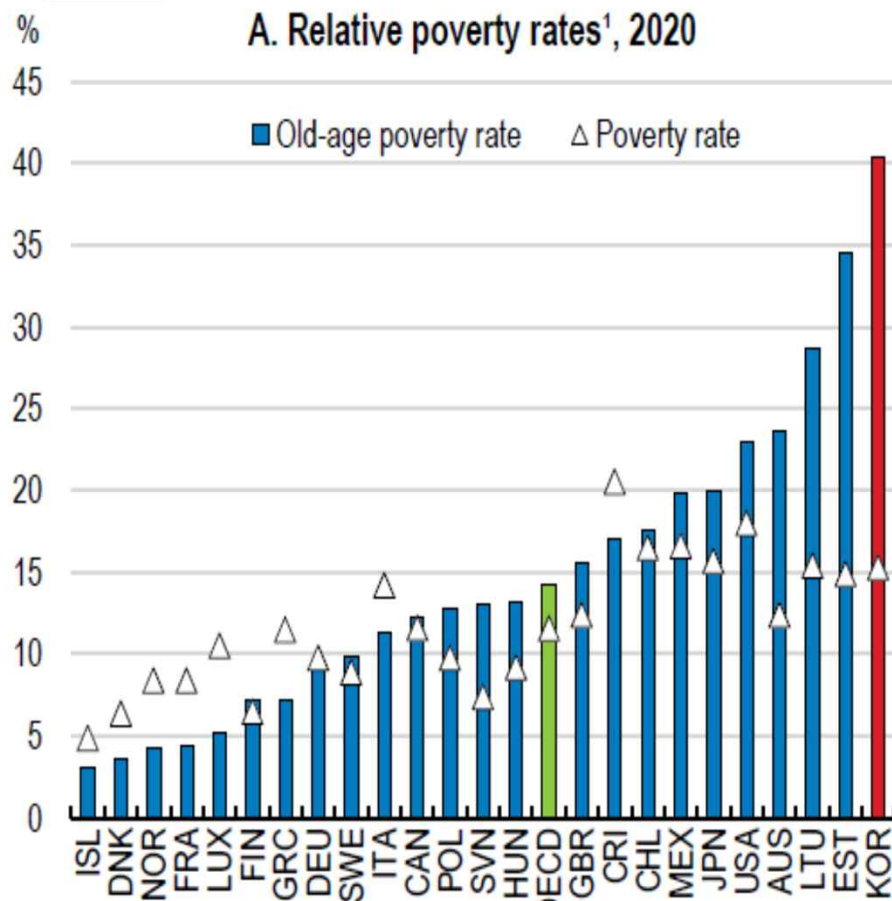
# Old-age poverty



1. Poverty line as half the median household income of the total population. Source: OECD, 2022

# Employment rates of workers aged 55-59, 60-64, 65-69 in 2018
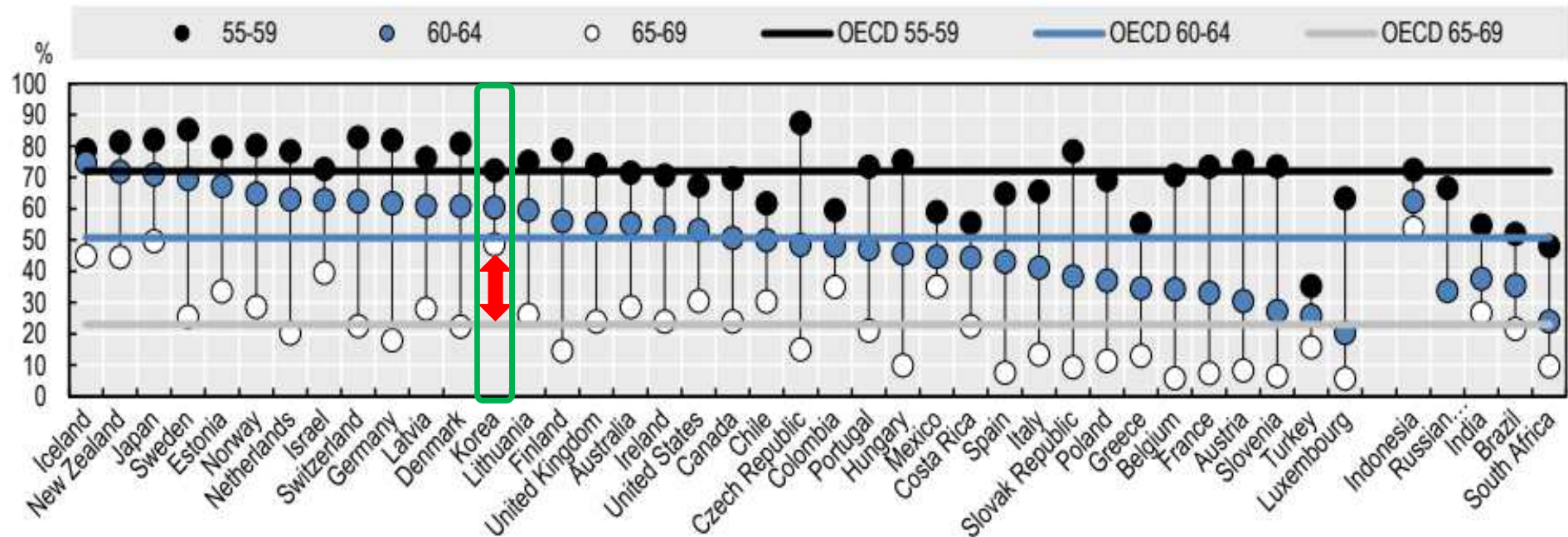


Note: Data for India and Indonesia refer to year 2019. Age group 65-69 data for Russian Federation are unavailable.
Source: OECD database Labour Market Statistics by sex and age: employment-population ratio.

StatLink https://stat.link/rm6z5a

OECD 2021
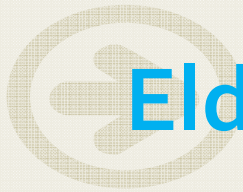
# Elderly Poverty Rate by Income Source in 2013



Ku, I. 2021

Pension Expenditure in GDP (2019 or latest available)
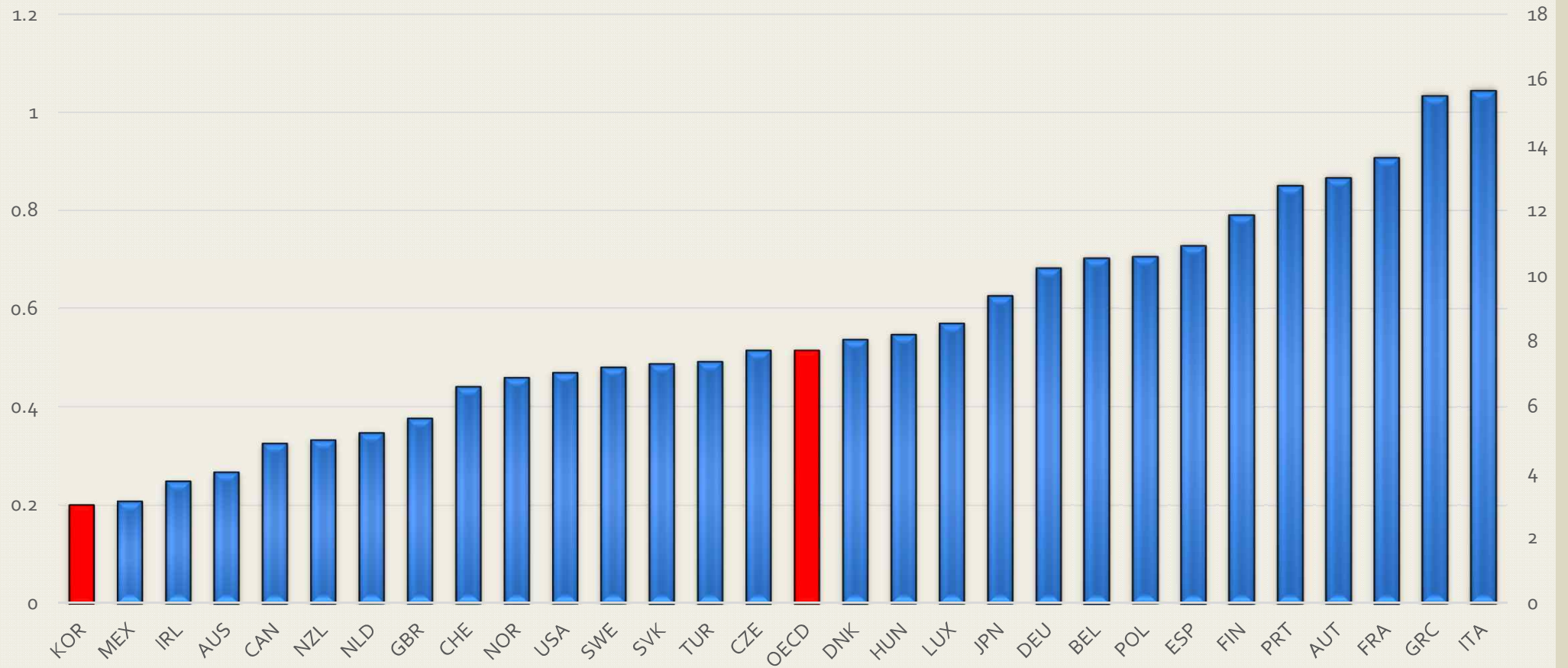
OECD. Data

# Real Pension Expenditure in GDP/old age ratio



Legend: France, Germany, Japan, Korea, United Kingdom, United States

OECD.stat
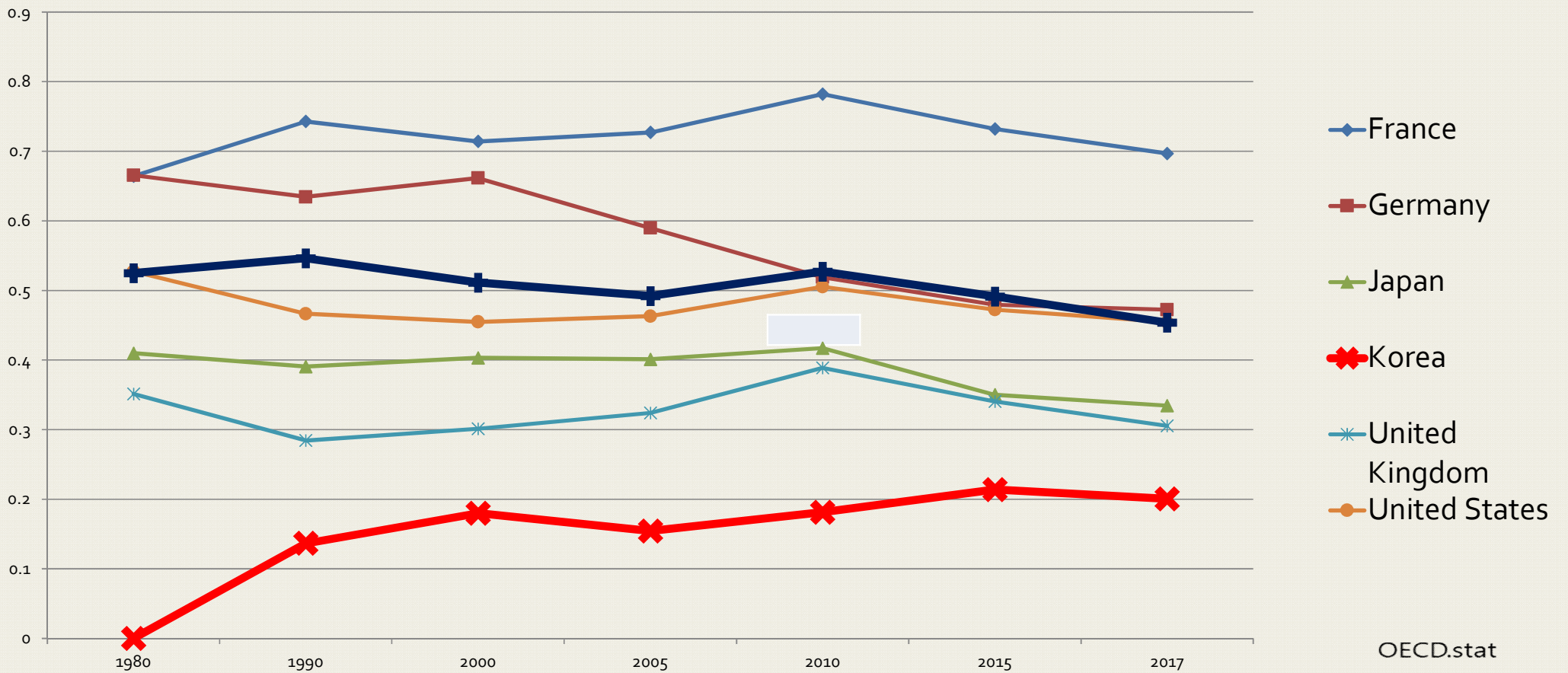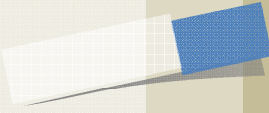
# II. MAJOR REFORM ISSUES OF THE PENSION SYSTEM IN KOREA
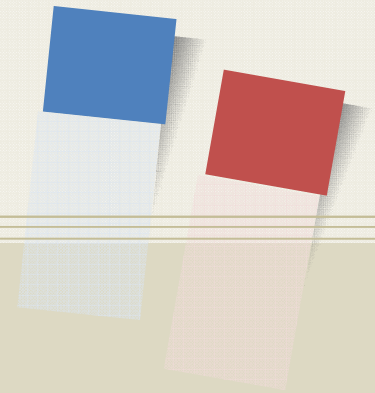
# Korea's Multi-pillar pension system

| | | | |
|---|---|---|---|
| **3 tier** | Personal Pension (2,57Mil.) | | |
| **2 tier** | Retirement Allo. | Retirement Pension or Allo (8.3%, 25~30%: 5,81Mil. | |
| **1 tier** | Pension for special occupational Groups (18%, 61.2(68)%: 1,52M. | National Pension Scheme (9%, 40%: 21,718Mil.) | Basic Pension Scheme (5,094Mil., 12%) |
| **0 tier** | Social Assistance | | |
| | Special G. | Workforce | Non Workforce |
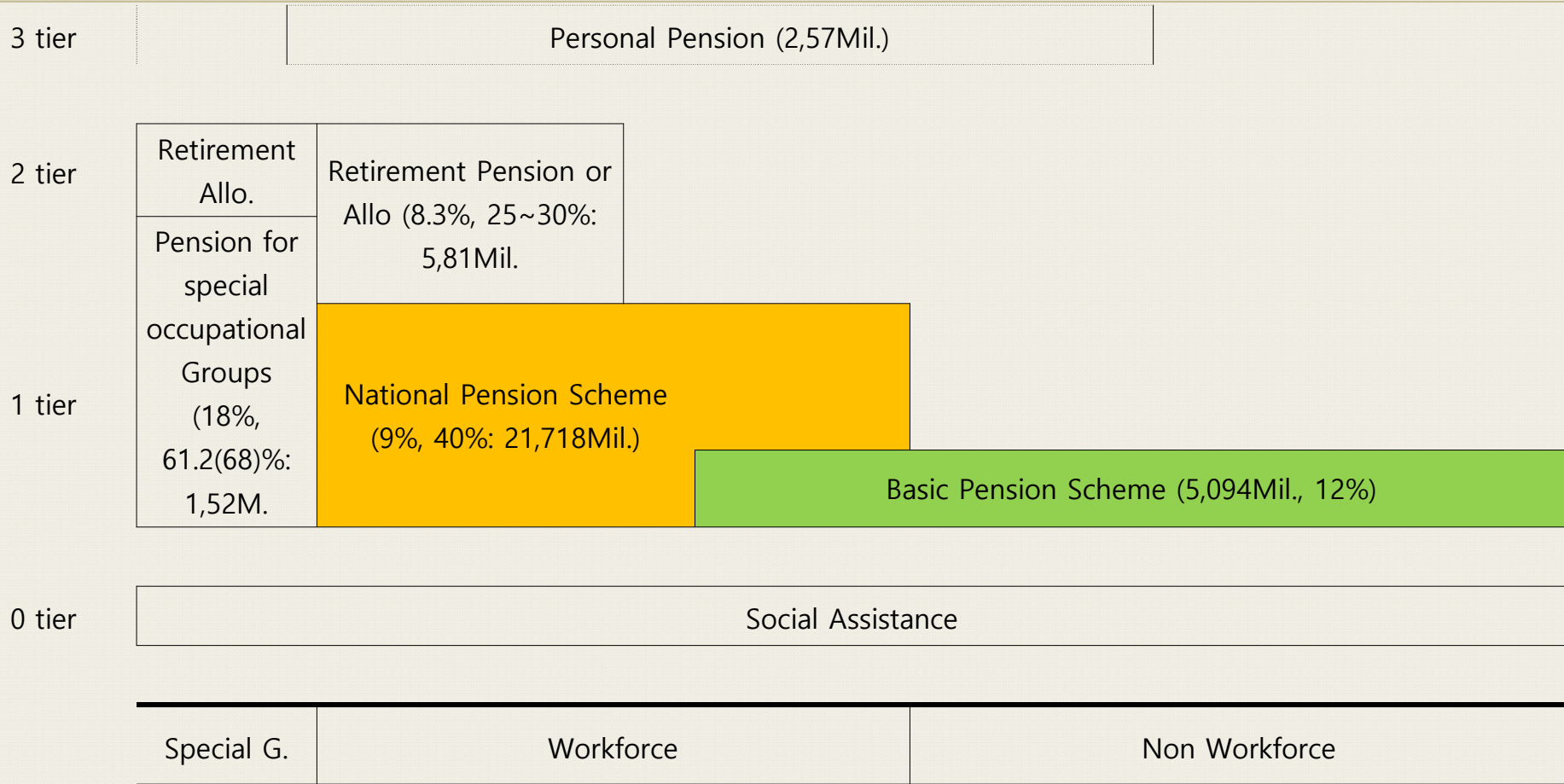
# Characteristics of NPS: Coverage and Management

❑ **Compulsory insurance of Wide Coverage:** whole population between the age 18 and 59

- Some groups excluded: spouses with no earnings of the insured and beneficiaries of any

  public pension schemes, beneficiaries of the NBLSS, and so on.

❑ **Managed** by the NPS under the supervision of the MfHW.

❑ Retirement age: 62 in 2022, 63 from 2023, 64 from 2028, 65 from 2033

❑ **Partially funded system:** the benefit: financed by fund and its profits and contributions: The benefit

  level very high, contribution rate very low. **long term financial instability problem.**

❑ **Pension reform in 1998: benefit level from 70% to 60 % and contribution rate from 6 to 9%.**

  **Extension of retirement age,** exhausting year of pension fund delayed from 2031 to 2047.

❑ **Pension reform in 2007:** benefit level gradually from 60% to 40% by 2028

# Perspective on finance of NPS after reforms
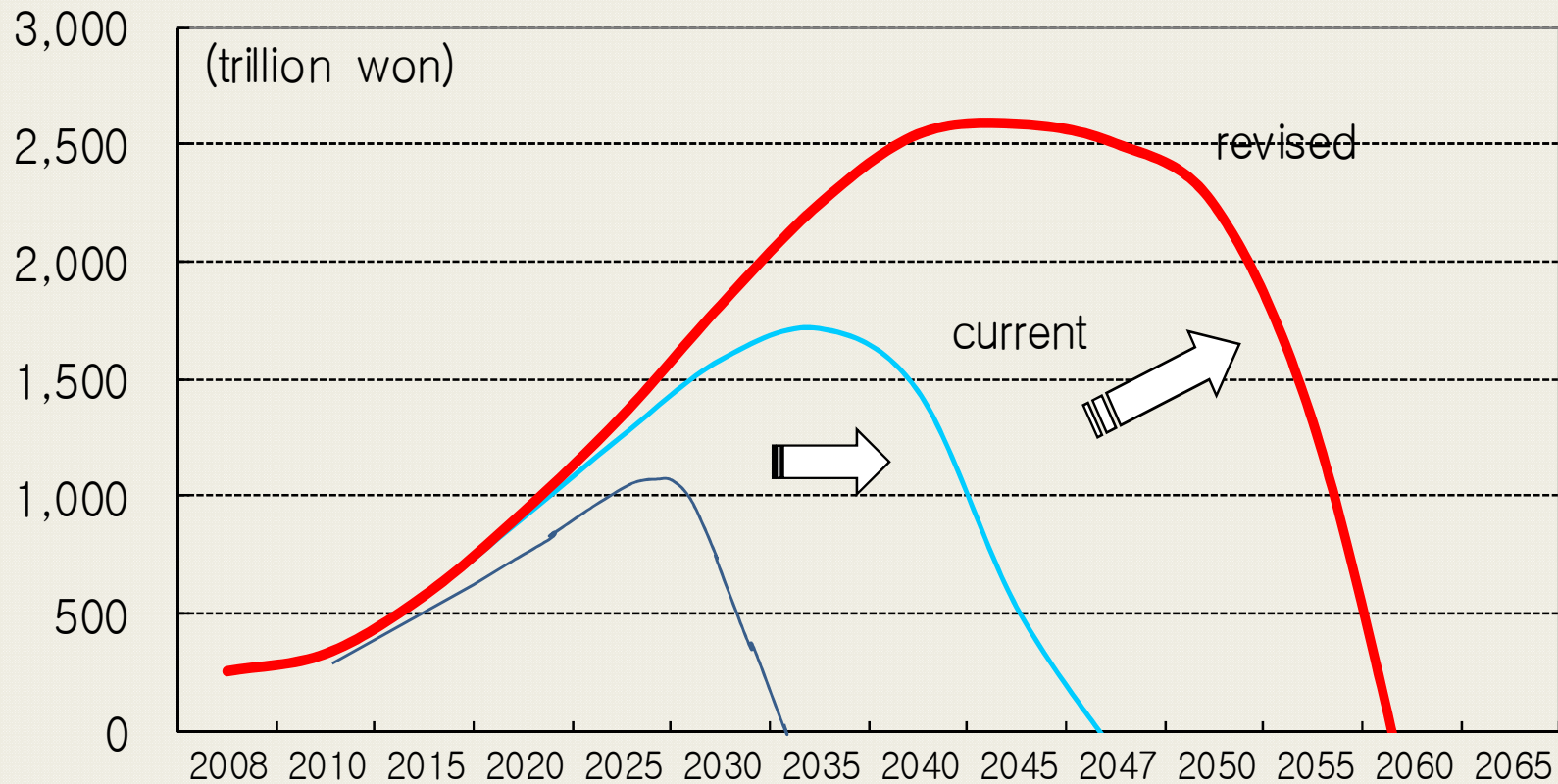
# Characteristics of NPS: Income redistribution effect

**1.2(A+B)\*(1+0.05n)/12 (From 2028)**

n = contribution years of more than 20 years

❑ the basic **A**: decided by the average monthly wages of all insured

❑ the additional amount **B**: based on the average amount of the monthly wages of the insured individual

❑ Combination of the earnings-related system with the flat-rate system.

❑ Strong income redistribution effect: the insured less well-off receive more benefit

| Income level | 0.5*AI | Average Income | 2*AI |
|---|---|---|---|
| Replacement rate | 43.1 | 31.2 | 18.6 |

# Characteristics of Basic Pension Scheme (BPS)

❑ In 2013, the BPS substituted the Basic Old Age Pension Scheme introduced 2007.

❑  Means-tested but Coverage wide by 70% of the elderly aged 65 or more (actually 67.6%)

❑ Quasi-flat rate benefit and price indexed

 - benefit level: 307 T. KW (213.5 US$) for single, 492 T. KW (341.6 US$)

 - Benefit reduction for recipients with high benefits, The more benefit from NPS, the less benefit from basic pension, actually flat rate benefit for 90% of beneficiaries.

 - 20% Reduction for the elderly couple

# Policy Issue1: Coverage gap of NPS (12. 2020)
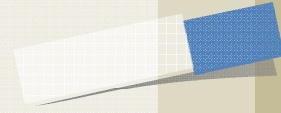
| 18-59 population as of 12. 2020: **31,672** | | | | | |
|---|---|---|---|---|---|
| Economically inactive population | Economically inactive population 70.7% | | | | |
| | National pension application 68% | | | | special pension |
| | payment exception | Income declaration 58% | | | |
| | | Non-pay. | Contribution Payment | | |
| 26% | 9.7% | 3.2% | 55% | | 5.4% |
| 12,485 (39.5%) | | | 19,187 (60.5%) | | |
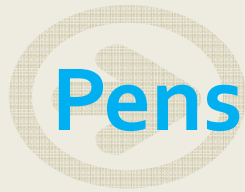
# Pension Beneficiaries by Pension system (2021.12)

| | | | | | |
|---|---|---|---|---|---|
| NPS | | ○ | ○ | X | sp. |
| BPS | ○ | ○ | | X | |
| Population aged 65 and over: 8,835 Mil. | 3,294 Mil. | 2,65 Mil. | 1,121 Mil. | 1,77 Mil. | |
| **100%** | **37.6** | **30** | **16.8** | **15.6** | |

Choi, O. 2022

# Projection of actual coverage of the old age pension in NPS (Thousand)
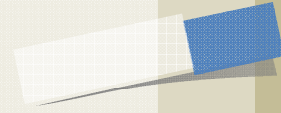
| Year | All Beneficiary aged above 65 | Beneficiaries of old age pension | Actual Coverage(%) |
|------|------|------|------|
|  | A | B | B/A |
| 2025 | 5,230 | 4,496 | 42.8 |
| 2030 | 7,212 | 6,220 | 48.0 |
| 2040 | 11,919 | 10,526 | 61.5 |
| 2050 | 15,328 | 13,734 | 73.0 |
| 2060 | 16,483 | 15,008 | 81.0 |
| 2070 | 15,740 | 14,626 | 84.4 |

MOWH 2018

# Policy Issue2: Low benefit level

## Distribution of pensioners by pension amounts 2020.12



2020년 12월
연금수급자 : 5,306,318명
월평균급여액 : 541,033원
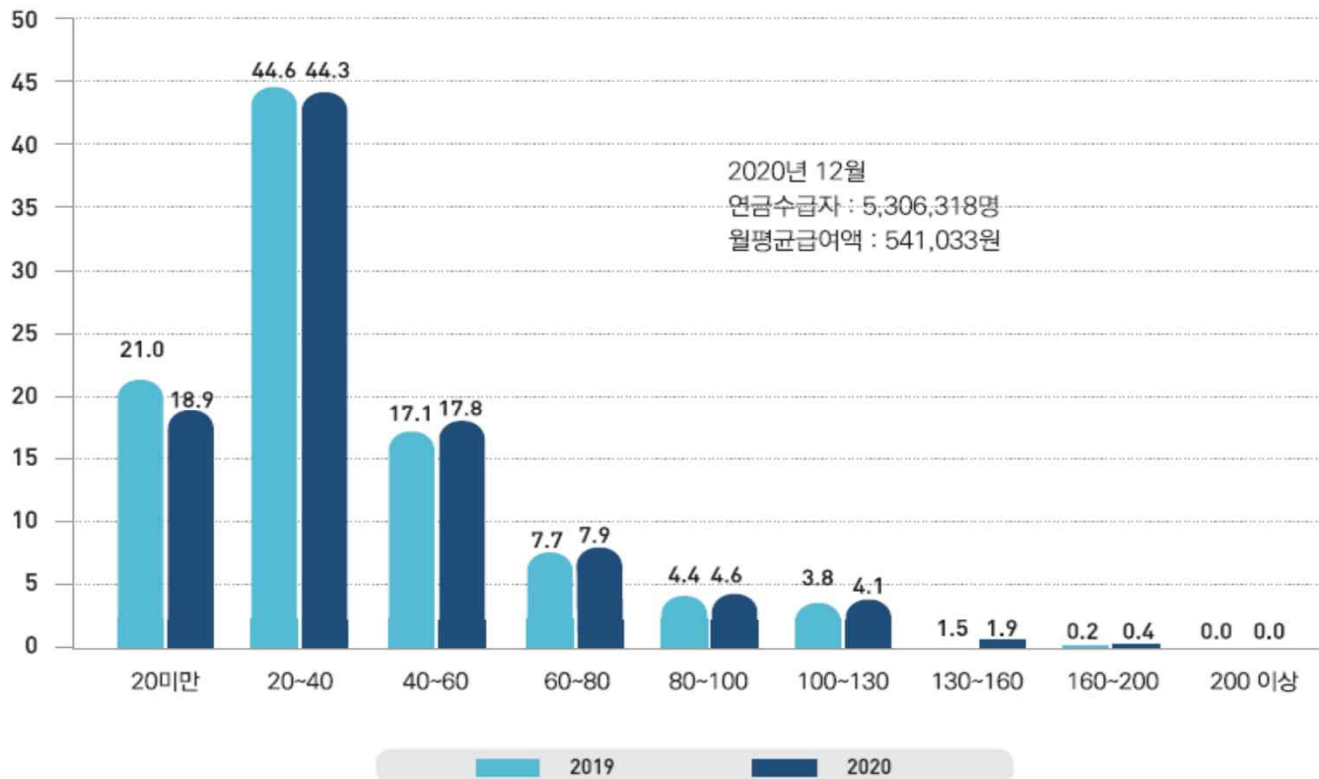
Average benefit amount
540 KW (779 US$),

63% less than 400 T. KW
(577 US$)

NPRI 2021

# Policy Issue 3: financial sustainability

**System dependency ratio**: projected subscribers and pensioners
(Unit: thousand)

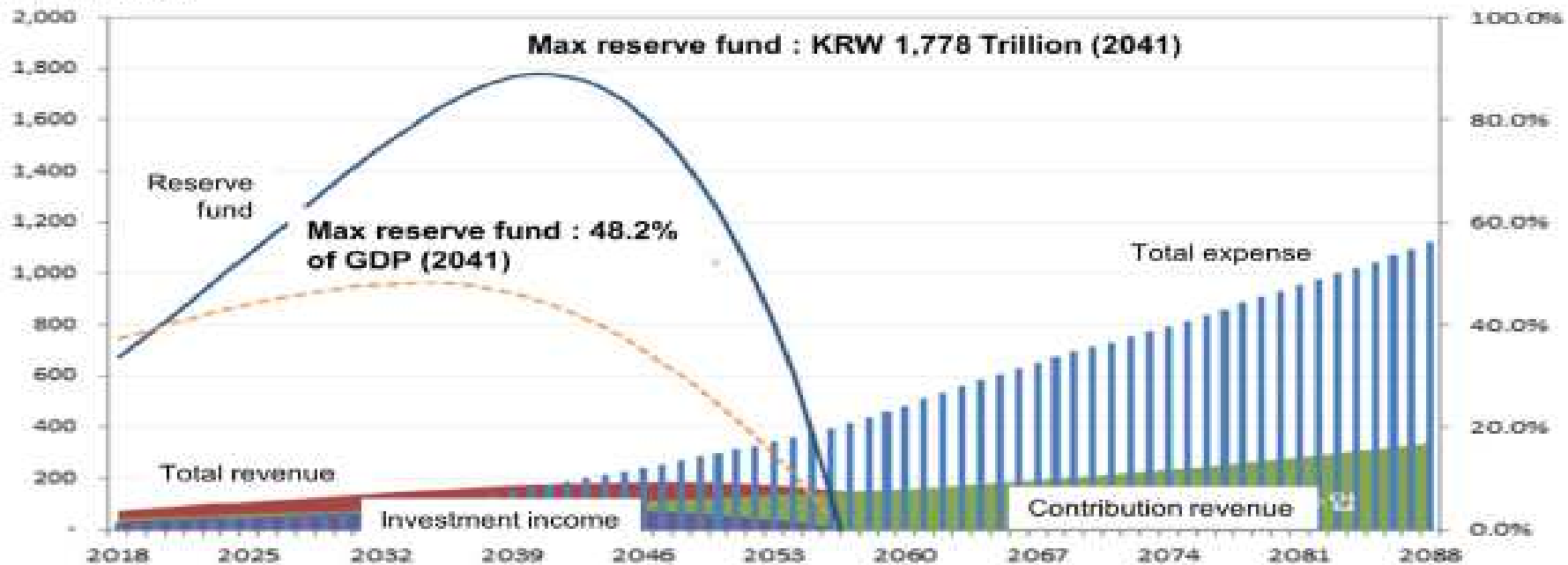|  | 2015 | 2025 | 2035 | 2045 | 2055 | 2065 |
|---|---|---|---|---|---|---|
| Subscriber | 17649 | 16703 | 14298 | 12771 | 11726 | 10741 |
| Pensioner | 3689 | 6063 | 8865 | 11730 | 13433 | 14358 |
| Dependency ratio | 0.210 | 0.363 | 0.620 | 0.918 | 1.145 | 1.337 |

# Public Pension Funds Projection (2018)



**According to the 4th Financial Estimate,**
  - the reserve fund will run out in 2057 under the current system

Unit: Trillion (KRW)

Max reserve fund : KRW 1,778 Trillion (2041)

Reserve fund

**Max reserve fund : 48.2% of GDP (2041)**

Total expense

Total revenue

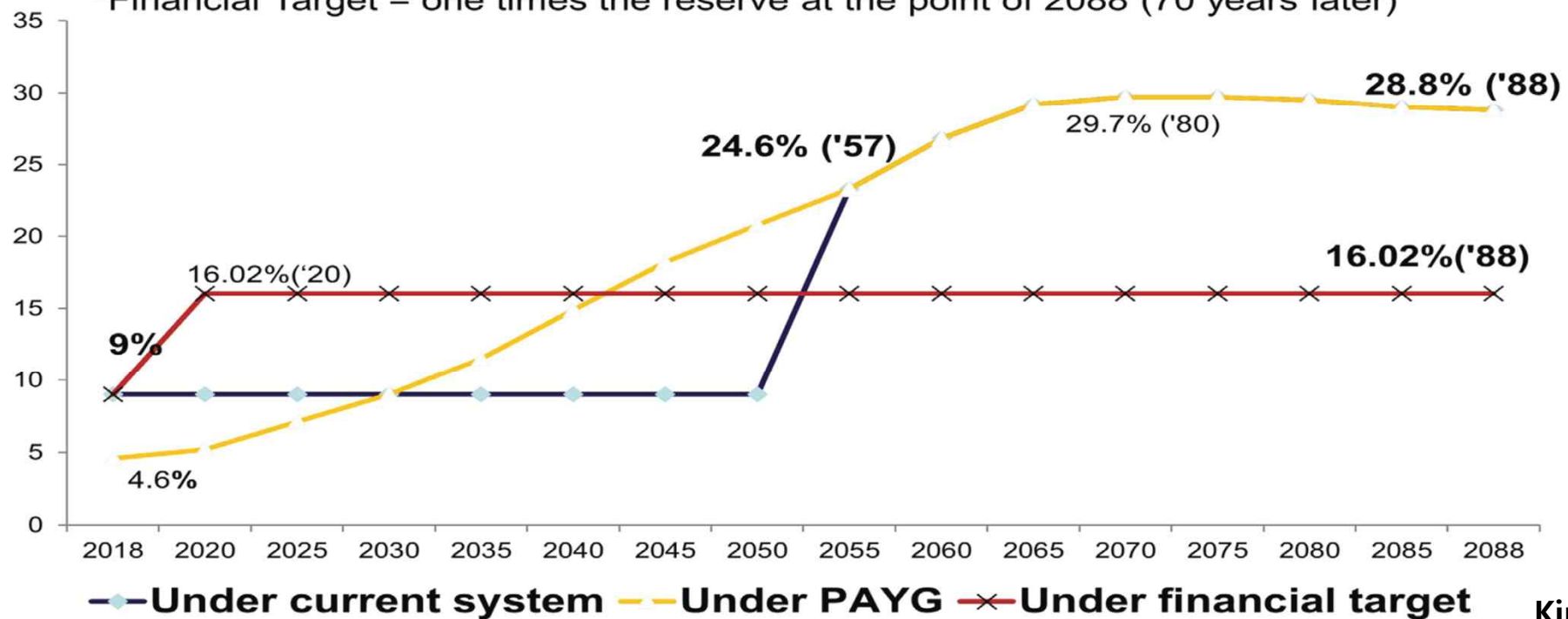Investment income

Contribution revenue

# Public Pension Financial Sustainability
## : Public Pension Funds Projection (2018)

**According to the 4th Financial Estimate**,
- the PAYG contribution rate will reach 28.8%, (cf. currently 9%)
  and the required contribution rate for financial target is 16.02%



*Financial Target = one times the reserve at the point of 2088 (70 years later)

28.8% ('88)

29.7% ('80)

24.6% ('57)

16.02%('20)

16.02%('88)

9%

4.6%

Under current system — Under PAYG — Under financial target

**Kim, S. 2018**

# III. REFORM MODELS AND ALTERNATIVE
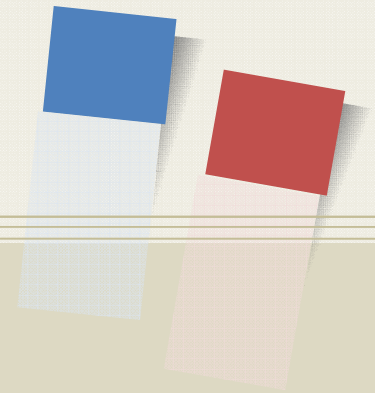
# Reform Model 1: NPS-centered Model
# NPS + Minimum Income Guarantee

100만

55만원

**Minimum Income Guarantee**

NPS
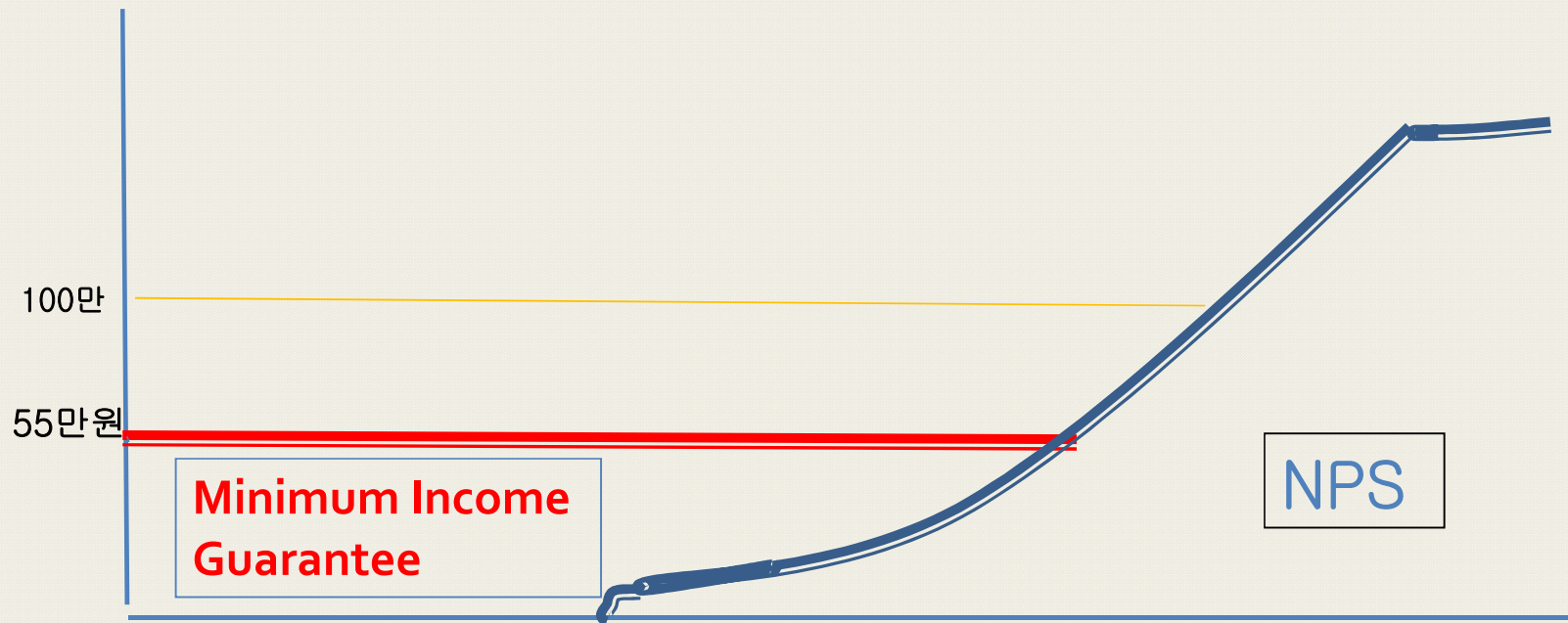
Maintenance or expansion of the NPS; Increasing contribution rate

Replacing BPS with Minimum Income Guarantee

# Reform Alternative 1:
# NPS + Minimum income Guarantee

| Strength | Weakness |
|---|---|
| ❑ Relief of financial burden and strengthening of cost-effectiveness | ❑ **Can't solve the low benefit level Problem of NPS: 30% of the elderly receiving NPS and basic pension at same time.**<br><br>❑ Problem of incentive to enroll in the NPS<br><br>❑ People's Resistance to the reduction of BPS<br><br>❑ Employer's Resistance to increasing contribution rate<br><br>❑ **Expansion of Social Assistance Pension System: Weakening of Social Rights** |

# Reform Model 2: BP-centered Model
# NPS + Reinforced BPS
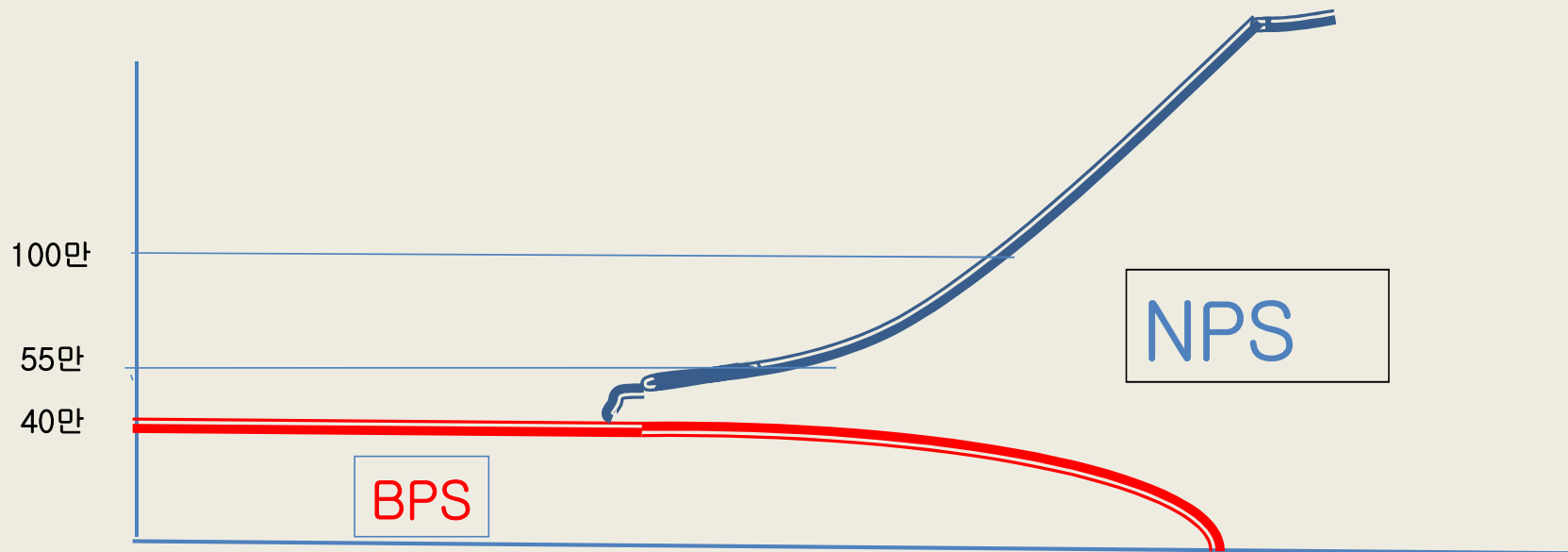


Maintenance of the NPS; Increasing contribution rate

Increasing benefit level of BPS to 400 t. KW (568 US$); extension of BP coverage to more than 80% of the elderly aged 65 or more

# Reform Model 2: NPS + Reinforced BPS

| Strength | Weakness |
|---|---|
| ❑ Resolving low benefit level problem of NPS<br><br>❑ People's support for increase of BPS' benefit level | ❑ With only a basic pension, still difficult to escape poverty: less poverty alleviation effect than expected.<br><br>❑ Increase of financial burden<br><br>❑ Employer's Resistance to increasing contribution rate |

# Prospects for Pension Reform

❑ The former administration reforms based on Model 1: Raising the NPS contribution rate and benefit level. Failed because it did not receive the company's consent.

❑ The current conservative Yun administration also promised reform: raising the benefit level of the basic pension, but no specific model. The opposition Democratic Party alternatives based on Model 2.

❑ Most political parties and experts support increasing benefit level of the basic pension and raising contribution rate of NPS.

❑ In July 2022, a special committee on pension reform in the National Assembly and discussions began.

❑ **Unfavorable reform conditions**: Reform not accomplished without the consent of the opposition, since it holds the majority. Recently, however, the government and opposition parties fighting rather than cooperating.
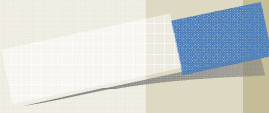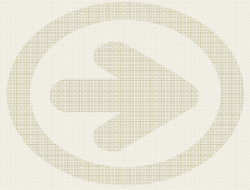
# Conclusion

❑ the elderly poverty rate in Korea chronically high, Caused by a weak public pension system.

❑ The current issues: the poor income security function of public pension system of NPS. Basic pension not sufficient to solve these problems. In addition, the increasing expenditure of NPS and basic pension caused by rapid population ageing

❑ In recent reform debate, two reform models: NPS-centered model and Basic pension system-centered model.

❑ The incumbent government attempting a pension reform, but the political conditions unfavorable

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# Thank you for your attention!!