

**ASHK Hong Kong Pension Actuary Symposium 2015**

**The Actuarial Society of Hong Kong**

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Good morning, Ladies and Gentlemen,

I would first like to thank the Actuarial Society of Hong Kong for inviting me to this Symposium. The theme of the Symposium this year is “Evolution of Retirement Saving System”. I wish to take this opportunity to share with you the trends and developments of the MPF System and the work ahead.

The MPF System came into operation on 1 December 2000, and in less than three months, we will celebrate its 15<sup>th</sup> anniversary. As some of you may be aware, I have always been a keen advocate of the MPF System. The launch of the System is a milestone in the development of Hong Kong’s retirement protection policy. In these 15 years, we witnessed the MPF System from birth to adolescence, yet to mature but already yielding considerable results.

Coverage of the Working Population

The actuarial profession is well known for its expertise in, among others, applying and analysing quantitative information. My MPFA colleagues have prepared for me some numbers about MPF to share with you.

Before MPF was implemented, it is estimated that only about one-third of Hong Kong's employees (about one million) were covered by any sort of occupational retirement protection scheme. Post-MPF, as at end of June 2015, about 90% of Hong Kong's employees (over 3.2 million) were covered by the MPF System or some other forms of retirement scheme, such as the occupational retirement schemes ("ORSO schemes"). The remaining ones are mainly those who are not required by law to join any retirement scheme. Coverage of the working population in Hong Kong is in the forefront internationally.

### Rapid Growth of MPF Assets

In essence, MPF is a saving vehicle for retirement purpose. Its value hinges on the amount of retirement savings that could be generated for scheme members.

We have seen a significant growth of MPF assets in the past 14 years. Total MPF assets broke the first \$100 billion mark in July 2004. In April 2015, MPF assets exceeded \$600 billion.

As at end of June 2015, total assets under the MPF System amounted to \$620 billion. Of this, more than a quarter, or \$165 billion, was investment returns.

The MPF System's annualized rate of return since its inception is 4.5%, significantly higher than the 1.7% annual inflation rate over the same period. I must emphasize that 4.5% is the net return, after fees and charges.

Naturally, the actual returns for individual scheme members' MPF accounts will vary from this average figure, depending on their fund choices and the amount and timing of their contributions. But it can be seen that, overall, the MPF System had added substantially to the retirement savings of employees.

I am pleased to note that the value of MPF has been increasingly recognized by employees and employers, as more and more voluntary contributions are being made by them on top of their mandatory contributions. The amount of voluntary contributions has jumped from \$700 million in the fourth quarter of 2005 to \$3.8 billion in the second quarter of 2015, representing a fourfold increase and now accounting for 23% of overall MPF contributions. This shows that confidence of the population in the MPF System is growing.

As for ORSO schemes, although the number of ORSO schemes and enrolled members have been falling since the launch of MPF schemes, they remain an important part of the retirement saving system in Hong Kong. As at end June 2015, there were 4 045 ORSO registered schemes with total net assets of \$290 billion. These schemes covered a total of 6 400 employers and 386 000 employees.

### Expansion of Fund Choices

The MPF System is characterized by the availability of a wealth of fund choices. The number of MPF funds rose substantially, from 299 in March 2001 to 457 in June 2015. On average, there are now about 12 MPF funds under each MPF scheme.

Most people like more choices, but we have also heard the voices of some who prefer simpler solutions. Having too many funds may also limit the scale efficiencies that can be achieved by individual funds, making it harder for fees to come down.

## Trends of Fees and Charges

There has been much public debate about whether the fee level charged by MPF operators is reasonable. Regardless of whether fees are objectively high or not, we have always been maintaining the position that lower fees are in members' interests and this should be a natural target of the MPFA and all stakeholders concerned.

Over the past decade, the MPFA has made use of different means to bring fees down, including enhancing fee disclosure, implementing Employee Choice Arrangement ("ECA") to facilitate better working of market force, streamlining and simplifying administrative processes, requesting trustees to offer low fee funds, and working with trustees to merge less efficient schemes and funds. All these have been achieved under the backdrop that MPFA has not been empowered by law to control fees.

We are pleased to see a steady downward trend of fees. The average MPF Fund Expense Ratio ("FER") dropped from 2.10% in December 2007 to 1.62% in June 2015, representing a reduction of about 23%.

At present, almost 40% of all funds are low-fee ones, charging a management fee of 1% or lower, or an FER of 1.3% or lower. Employees could make use of ECA to move their part of MPF to any of these low-fee funds.

## Default Investment Strategy ("DIS") with Fee Controls

Looking forward, I have two important tasks set as priorities for the next two years. First and foremost, I hope to see the default investment strategy ("DIS") launched by the end of 2016, subject to smooth passage of the supporting

legislation and the readiness of the necessary preparatory work.

At present, if a scheme member does not make any fund choice for his MPF investments, the trustee of the scheme will invest the contributions of the scheme member in the default fund of the scheme. There is no standardized default fund, and hence the performance and risks of default funds under different schemes vary widely.

After comprehensive studies and reviews, we have come to the view that an important next step in reforming the MPF System is to improve the investment choice framework by ensuring that all schemes make available a well-designed DIS that represents good value for scheme members.

The DIS will have its management fees capped at 0.75% through legislation. The fee cap, the first time ever under the MPF System, will directly benefit scheme members whose MPF investments are in the DIS. The impact of the fee cap may also be felt across all MPF funds and create an opportunity for some cost-efficient service providers to enter the MPF market.

The investment approach of DIS will be designed in a way that best manages the long-term risks associated with investing retirement savings. It will therefore simplify what may be a difficult investment decision process for some scheme members as to which funds are suitable for them. The performance of funds used in the DIS will also be benchmarked against an agreed portfolio to increase transparency and consistency across schemes.

We are now working closely with the MPF industry on the details, such as fund structure, disclosure requirements and fee calculation. We are also working with the Government on drafting a bill on the DIS, which we plan to introduce

to the Legislative Council later this year.

### Standardization, Streamlining and Automation of Scheme Administration

The MPF System involves numerous scheme administration processes, and each trustee has its own platform for handling these administration matters. An important task for us is to explore ways to reduce the complexity of the System.

We have already appointed a consultant to conduct a study on investigating into different options, including their feasibility as well as the costs and benefits, for the development of what we now tentatively call “eMPF”, an initiative to streamline, standardize and automate scheme administration as far as possible.

We have a few basic ideas with “eMPF”. First, it would allow the centralized collection of MPF contributions through an e-channel. Second, it would involve setting up a central register for automatic calculation of the amount of contributions and for automatic submission of contribution information to trustees. Third, it would have a one-stop e-portal for members to access all relevant information about their accounts.

When implemented, “eMPF” will bring significant and fundamental changes to the administration of the MPF System, leading to better operational efficiency and lower administration costs. Even more importantly, it will allow scheme members to manage their MPF more conveniently and access the most updated information about their accounts at any time.

The study is expected to be completed by the end of this year, and we will work on a blueprint for taking the proposals forward thereafter.

## Developing the MPF System from a Solid Footing

How to ensure the working population will have a reasonable standard of living after retirement is a major challenge faced by many societies. Hong Kong has adopted the multi-pillar retirement protection model recommended by the World Bank, and the MPF System is the second pillar of this framework.

About 15 years ago, Hong Kong was among the forerunners of operating a 2<sup>nd</sup> pillar system. Today, 2<sup>nd</sup> pillar systems are in operation in more than 30 countries/regions. One major advantage of 2<sup>nd</sup> pillar systems, including the MPF System, is that it helps the current generation to take care of part of their own arrangements for retirement protection, rather than simply passing the burden onto the next generation.

We are committed to enhancing the MPF System to meet the evolving needs of the society, but we will not underestimate our limitations and challenges.

The MPF System is employment-related and only offers protection to persons who are employed or self-employed. To meet the retirement needs of the whole population in Hong Kong, the MPF System must be complemented by other pillars.

All in all, the MPF System has been developing on a strong footing. Our mission ahead is to capitalize on its strengths and build a retirement savings system that Hong Kong people value.

Thank you very much.