

At dawn, look to the East



04 April 2017

China is not known for a generous or well-designed pension system, but a look to the East could nevertheless shed some light on how to manage retirement in the face of an inadequate welfare system.

In China, the state retirement age is exceptionally low – 60 for men and 50 for women, while the life expectancy is 74 and 79, respectively. A typical Chinese retiree receives about 2,250 Chinese yuan. This would correspond, in terms of purchasing power, to £441 per month which is 70% of the UK state pension. Only those few lucky ones who used to work in big, often state-owned, enterprises have an occupational pension.

The current state pension system is under pressure by the low retirement age and the rapidly increasing life expectancy. The demographic change is not helping either. After 35 years of one-child policy China is facing a rapidly aging population. By 2050, over a quarter of the population will be older than 65. Unlike western countries, China is getting old before it gets rich. This means that the state pension, in terms of purchasing power, will erode over the next couple of decades.

Without much choice, Chinese people seek out their own ways to manage retirement:

- **Double income with high savings:** China has a high female labour force participation rate at 64% and it is common for women to hold full time jobs. Double income is financially essential for the family and this has led to improved gender equality. On top of that, expecting that they won't be looked after by a generous state pension or a strong welfare system, Chinese households create their own "pension" and precautionary buffer by saving approximately 38% of their after-tax, after-social contribution income – a world record.

- **Intergenerational contract:** it is the social norm in China that workers send money to their parents, and even grandparents, regularly. This is part of an unwritten intergenerational contract in which the parents take care of the children including paying for university and sometimes the up-front payment of their first car or house. In return, the kids provide financial support to their parents when they retire.

- **Multigenerational living:** it is not uncommon to see three generations living under the same roof in China. The retired grandparents babysit their grandchildren, do grocery shopping, cook and clean for their working son or daughter. This internal arrangement reduces the family expenses and the elderly are likely to feel happier and more appreciated. This is not without its own problems – the resultant household conflicts have been an endless inspiration to Chinese TV script writers.

In the West, most of the intergenerational familial roles have been replaced by a societal contract. The provision of personal finance, nursery services, and old age care has been institutionalised and is performed largely outside of the larger family unit. This can mainly be attributed to three factors: economic advancement, high labour mobility, and an individualistic culture. In contrast, the Chinese model relies heavily on inter-personal and inter-generational dependence. This familial rather than societal arrangement is more than just a cultural phenomenon. It is admittedly also a cost-saving decision driven by the economic reality. However, in a world of aging population, increasing longevity, and growing labour mobility, neither of these two solutions seem sufficient. The recipe for a sustainable future pension provision needs ingredients from both solutions. The main question is: where will the West and the East meet?

¹ 55 for female civil servants

¹ Based on OECD data, please see
<https://data.oecd.org/conversion/purchasing-power-parities-ppp.htm>

¹ It has been eased to allow two children since 2016

¹ Source: *The Economist*, please see
<http://www.economist.com/node/21553056>

¹ Source: The World Bank, please see
<http://data.worldbank.org/indicator/SL.TLF.CACT.FE.ZS>