Role of Insurance Companies in Hong Kong Pensions Business

Presented by

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Agenda

- Introduction of Hong Kong Pensions Business
  - ORSO vs MPF
  - Insurance Policy vs Trust Based
  - Running of a Pension Scheme
  - Pension Products
  - Type of Service Providers
  - MPF Statistics
- Characteristics of Pension Service Providers
- Summary of Current HK MPF Market
- Going Forward
## Hong Kong Pensions Market

- Exempted ORSO Scheme vs Mandatory Provident Fund (MPF)

<table>
<thead>
<tr>
<th>Exempted ORSO Scheme</th>
<th>MPF</th>
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<tbody>
<tr>
<td>Voluntary</td>
<td>Mandatory</td>
</tr>
<tr>
<td>No minimum contribution rate</td>
<td>Effective December 1, 2000</td>
</tr>
<tr>
<td>Contributions based on basic salary</td>
<td>Min. 5% / 5% contribution rate</td>
</tr>
<tr>
<td>Benefits can be received in cash upon termination of employment</td>
<td>Contributions based on relevant income</td>
</tr>
<tr>
<td>Vesting as per scheme rules</td>
<td>Benefits subject to portability and preservation</td>
</tr>
<tr>
<td><strong>Trust or Insurance Policy based</strong></td>
<td>100% immediate vesting</td>
</tr>
<tr>
<td>Few investment restrictions</td>
<td><strong>Trust based</strong></td>
</tr>
<tr>
<td>Employer benefits taxable if exceeds IRD proportionate benefits (vesting scale)</td>
<td>Many investment restrictions</td>
</tr>
<tr>
<td></td>
<td>Employer benefits tax free</td>
</tr>
</tbody>
</table>
Trust Based MPF

- How Insurance Company Copes With This Change?

Why Trust Based?
- Universal Accepted Concept – Easy to sell to general public
- Standardized Legal Structure – More confident to end users
- Trend in Asia – PRC, Hong Kong, Taiwan, The Philippines, etc.

Trust Based vs Insurance Policy – Does It Really Provide Extra Assets Protection?
- Not Necessary
  - Separate Account – “Implied Trust”
  - Underlying Investment

How Insurance Company Cope With This Change?
- Setup a separate Trust company to be the Approved Trustee of the MPF Scheme
Running of a Pension Scheme
- Mechanism

- Employer
- Employee
- Employee

Contributions

Trustee / Administrator

Investment Return + Scheme Benefits

Investment Manager

Regulator

Auditor
Pension Products

Funds Type
(Unitized Funds / Policy)
- Lifestyle Funds
- Bond Funds
- Equity Funds
- Guaranteed Funds
- Capital Preservations

Annuity Type
(Not a developed market in Hong Kong)
Hong Kong MPF Environment
- Types of Service Providers

- Banks
- Insurance Companies
- Securities Companies
% Share of Individual Registered Intermediaries by Major Line of Business of the Intermediary’s Primary Sponsoring Corporation
As of Dec 31, 2004

Source: MPFA, Mandatory Provident Fund Schemes Statistical Digest - Dec. 2004
Top 5 Service Providers for HK MPF
- As at Dec 2004

<table>
<thead>
<tr>
<th>Top 5 Service Providers</th>
<th>Type of S.P.</th>
</tr>
</thead>
<tbody>
<tr>
<td>AIA-JF</td>
<td>Insurance-Securities</td>
</tr>
<tr>
<td>Bank Consortium</td>
<td>Bank</td>
</tr>
<tr>
<td>BOC Prudential</td>
<td>Bank-Insurance</td>
</tr>
<tr>
<td>HSBC / Hang Seng Bank</td>
<td>Bank</td>
</tr>
<tr>
<td>Manulife</td>
<td>Insurance</td>
</tr>
</tbody>
</table>

- Total Asset Under Management for HK MPF Market: HK$120,183 million*
- The top 5 service providers together capture 72.9% market share in terms of AUM#

* Source: MPFA - Mandatory Provident Fund Schemes Statistical Digest Dec 2004
Characteristics of Pension Service Providers
- Insurance Companies

**Strength**
- Distribution
  - Mainly **Agency** and **Direct Sales**
  - Strong agency distribution network covers small to medium companies.
  - Some form alliance with 3rd party distributors (e.g. securities house)
- Product – Ability to offer investment funds with **guaranteed** natures
- More focus on after sale services by both Agency and/or designated customer services executives
- More willing to package better products to customers via partnership with other professional entities e.g. professional FMC and custodian
- Good brand names and high credit rating
- Other value added bank services packaged, e.g. Insurance products, and/or Credit Card, etc.

**Weakness**
- Inconsistent services due to varying quality of agents
- Not perceived to be strong in Fund Management
Characteristics of Pension Service Providers
- Banks

**Strength**
- Distribution
  - Mainly **Direct Sales** (Corporate RM or Branch Staff)
  - Large corporate clients base
  - Extensive branch network for market penetration
- Good brand names and high credit rating
- Other value added bank services packaged, e.g. Credit Card, higher credit limits, etc.
- Usually with closed architecture with distribution, administration and fund management by Bank and/or their related affiliates.

**Weakness**
- Less focus on after sales services
- More focus on offering in-house products only
- Not perceived to be strong in fund management
- Normally not offering funds with guaranteed nature except those with associate and/or affiliate insurance Cos.
Characteristics of Pension Service Providers
- Securities Companies

**Strength**

- Distribution
  - Mainly **Direct Sales** for large corporations
  - Strong on consultancy referral businesses
  - Limited coverage on small to mediums companies
  - Some form alliance with bank or insurance company to extend the distribution coverage
  - Strong brand name as professionals for delivering superior fund performances and better services
  - Clients are usually of large company with good size of AUM
  - More services oriented with high quality of staff

**Weakness**

- Unable to offer funds with guaranteed nature unless packaged with other service providers.
- Limited investment on technology for supporting MPF as SME are not perceived to be their core market segment
Summary of Current HK MPF Market

- Banks has got over 50% of overall MPF market share, with insurers and securities companies sharing the remaining on approximately 2:1 ratio.

- The top 5 MPF service providers have got over 70% of the overall MPF market share.

- Common Characteristics of Successful MPF Service Providers are:
Summary of Current HK MPF Market

Common Characteristics of Successful MPF Service Providers are:

- Guaranteed Funds Available via Insurance Companies
- Strong In-House Distribution Networks
- Single Fund Manager Products
- Simple Products (i.e. Guaranteed Funds, Capital Preservation Funds, Life-Style Funds, etc.)
- Strategic Partnership (i.e. Bank-Insurance Companies, Insurance-Securities Companies)
- Major Investment into Systems/Technology Development for those with In-House Administration Capabilities
- Professional Trustee Services
Going Forward

- **Retail Market**
  - Deferred Accounts
  - Voluntary Contributions – use MPF as a low fee investment savings vehicle

- **Annuity**
  - What to do with the lump sum payout?
  - What if retirees want a secured stream of income after retirement without worrying about investment?
  - How can government discourage retirees to use the lump sum payout for gambling?

  Answer: Annuity but

  Need Lobbying for Tax Benefits to Generate Public interest