

Life Insurance Products for Pensions in Vietnam

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Abstract: In addition to the Government's social insurance, pension products by life insurance companies provide more options for individuals for retirement preparation. This article aims to give a brief overview of life insurance products for pensions in Vietnam. It describes the pension system in Vietnam and shows the needs for private pension products. The article summarizes the basic information about the development of life insurance and pension products in Vietnam. The article also highlights various features of life insurance products for pensions such as initial conditions for participation, guaranteed interest rate, main benefits and costs. The author then makes some recommendations for Vietnam in developing pension products to cope with the market demand.

Keywords: Pension products, insurance company, Vietnam.

1. Introduction

Social insurance is one of the most important policies in stabilizing the socio-economic conditions of a country. Vietnam social insurance includes old-age pensions and short term benefits. There are various forms of pensions provided by both the government and life insurance companies. However, there has been no research aiming to systemize life insurance products for pensions in Vietnam. A systematic overview of those products will be essential for policy makers in drafting policies for pension market development. It will also facilitate further research in social insurance as a whole and pensions in particular to better understand the structure and components of the system.

This research analyzes social insurance and pensions in Vietnam to point out the inevitable trend of giving a greater role to private insurance companies in providing pension products. It also gives an overview about current pension products provided by life insurance companies in Vietnam and analyzes the characteristics of those products. The article concludes with some recommendations for Vietnam in diversifying pension products to better serve pensioners.

2. Social insurance and pensions in Vietnam and the needs of pension products

2.1. Social protection, social security and social insurance

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According to the Social Protection Strategy 2011-2020, social protection (also known as social security or the social safety net) in Vietnam includes three main pillars: (i) the labor market policies; (ii) social insurance and social health insurance; and (iii) social assistance. Among them, labor market policies are to prevent risks in a person’s life; social insurance and social health insurance policies aim to mitigate those risks once they occur; and social assistance policies help people overcome their risks [1].

The Vietnam Social Security System was established in 1947. In the 1974-1995 period, the contributory pension system in Viet Nam only focused on the public sector. However, since 1995 the system was expanded to cover workers in the private sector and designed as a pay-as-you-go, defined benefit scheme including both mandatory and voluntary schemes. In 2010, the mandatory scheme covered about 9.3 million people (20 per cent of the country’s labor force) while the voluntary

scheme covered only 62,000 persons. State sector workers accounted for 80 per cent of active contributors. Contributions to the pension scheme are from both employers and employees. Both contributions and pension benefits are tax exempt for corporations and individuals. Investment income is one source of financing the scheme [2].

2.2. Challenges to the pension under the social insurance scheme and the needs of private pension funds and pension products

Governments of countries around the world typically rely on a three-pillar social security system, namely (i) government-run; (ii) employer-mandated; and (ii) employee voluntary. From this viewpoint, social security in Viet Nam could be considered underdeveloped as it relies exclusively on the first pillar [3]. The expected demographic and economic changes, as well as administrative capacity create many challenges for the current scheme.

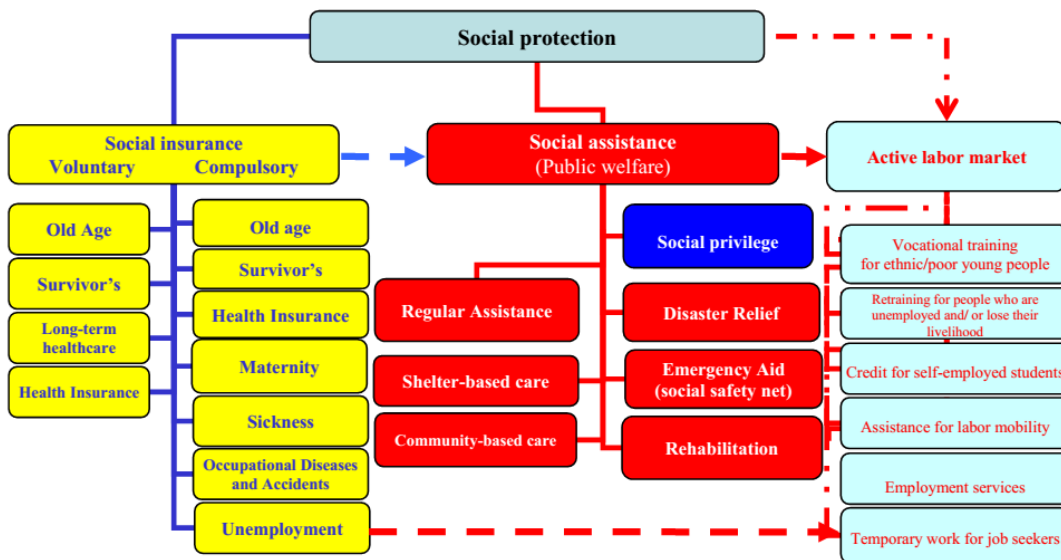


Figure 1: Social protection system in Vietnam.
Source: Giang, 2010.

Firstly, the coverage rate of the scheme has been persistently low; particularly, the coverage rate for informal sector workers via the voluntary scheme is trivial. Secondly, there are wide participation gaps between rural and urban dwellers, between the poor and non-poor, and between ethnic minorities and the Kinh. The latter groups are usually more vulnerable to risks than the former, so that such a low participation may not be able to help them to mitigate risks since more than half of their income sources are mainly from household business or agricultural production. This means that a great number of people, who are more vulnerable to poverty, are not covered by the current scheme [1]. Thirdly, the current formulas for benefit estimation are unfair between males and females, and between the public and private sector. For example, with the same actuarial benefits, the public sector workers may enjoy higher levels of benefits than private sector workers. Fourthly, most of the social insurance fund investments are generating a lower rate of return than the market rate. Lastly, the long-term financial sustainability of the fund may be deteriorated by the fact that the population in Vietnam entered an aging phase in 2008 when the percentage of aging persons accounted for 10 percent of the total population. As the population ages, life expectancy of elderly people at retirement will also increase, which in turn increases the number of years of benefit payments.

As a result, the current operation of the social insurance scheme in general, and the pension scheme in particular, are not sustainable because of unsuitable benefits and financial instability. The International Labor Organization projects that the pension fund will be depleted by 2027 [4].

As discussed by Giang (2012), Vietnam should transform the current pension system to a system of individual accounts while simultaneously building a social assistance scheme for low-income persons [5]. A voluntary pension scheme and cash transfer programs should be considered as supplementary social protection pillars. Voluntary pension schemes can play an important role in supplementing public pensions and would add to the domestic pool of capital available to invest in the local currency bond and equity markets [4]. In August 2013, a circular was issued to enable the provision of pension insurance products by life insurance companies. Since then, life insurance companies started to provide pension products in Vietnam, allowing people to have more options in their retirement preparation.

3. Vietnam life insurance market and pension products

3.1. Life insurance market development

According to the Insurance Supervisory Authority (ISA), under the Ministry of Finance (MOF), as of 31 March 2015, there were 61 insurance enterprises in Vietnam, including 29 non-life insurance enterprises, one branch of a foreign non-life insurance enterprise, 17 life insurance enterprises, 12 insurance brokers and 2 re-insurance companies. In 2014, total insurance revenue reached VND 54,718 billion which is equal to 114.89% of the insurance revenue in 2013 [6]. The key performance indicators of Vietnam's insurance sector are presented in Table 1.

Nearly all 12 life insurance companies in Viet Nam are 100% foreign-owned, financially

sound, and well managed. The market is concentrated, with the top three players holding a combined market share of circa 80%. The biggest companies in the life insurance market include Prudential, Bao Viet Life, Manulife and Dai-ichi life. Their total premium and market share in the first half of 2014 can be seen in Figure 2.

Under the Law on Insurance Business of the National Assembly dated 23 July 2013, insurance products in Vietnam are divided into three categories: (i) life insurance products, (ii) non-life insurance products, and (iii) health insurance products. Insurers can offer the following seven types of life insurance products: (i) whole life insurance, (ii) pure endowment insurance, (iii) term life insurance, (iv) endowment insurance, (v) annuity insurance, (vi) investment-linked insurance, and (vii) pension insurance. The terms, conditions and premium scales of life insurance products must be approved by the MOF before they can be offered to the public. Life insurance providers cannot sell non-life insurance products, and vice versa.

For the first half of 2014, the total revenue of the life insurance market was 12,109 billion

VND, increasing 22.2% in comparison to the previous year's period in which individual contracts accounted for 12,005 billion VND (an increase of 21.8%) and enterprise contracts accounted for 104 billion VND (an increase of 62.5%).

The average premium per life insurance products is 2.3 million VND. In the first half of 2014, the most popular life insurance products are endowment policies, which attracted about 60% of the segment's total written premiums. Investment products are on the rise and account for 41% of the total premium. The details of total premium products can be seen in Figure 3.

3.2. Pension products in Vietnam

Because private pension product development in Vietnam is now at the beginning phase, the choice for customers is limited. Table 2 presents the pension products and other products marketed by the life insurance companies. In July 2015, life insurance companies (LICs) in Vietnam provide 145 insurance products. Among them, only 12 are products for retirement, which is a very small number given the potential of the Vietnam market.

Table 1: Key performance indicators of Vietnam's insurance sector in 2014

	Non-life Insurance (VNU billion)	Life Insurance (VNU billion)	Total (VNU billion)
Revenue	27,391	27,327	54,718
Insurance compensation	10,776	8,976	19,752
Investment from insurance company	28,403	103,276	131,679
Asset value	39,500	114,384	153,884
Equity	17,730	23,163	40,893
Reserve	12,700	81,287	93,987
Insurance brokerage fee		482	

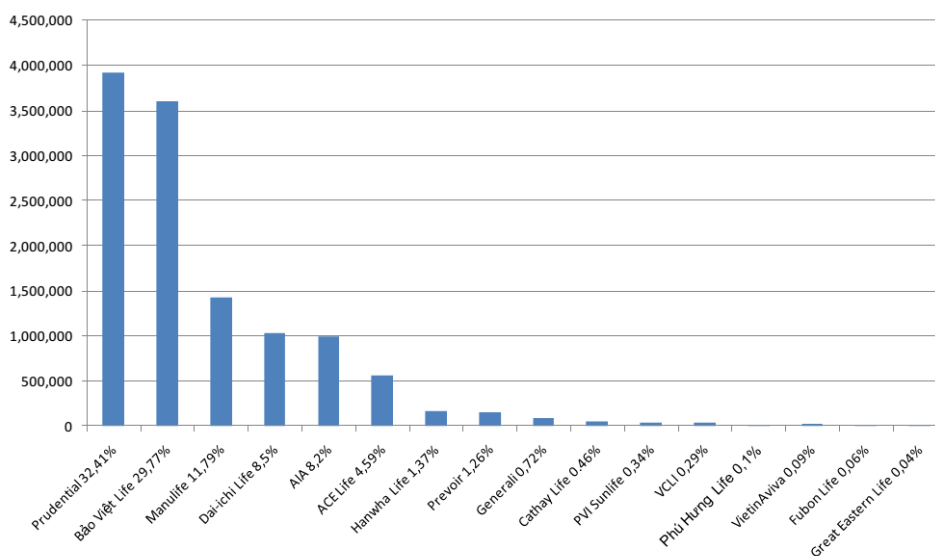


Figure 2: Total premium and market share of life insurance companies (in VND Million).
 Source: Association of Vietnamese Insurers (2015) [7]

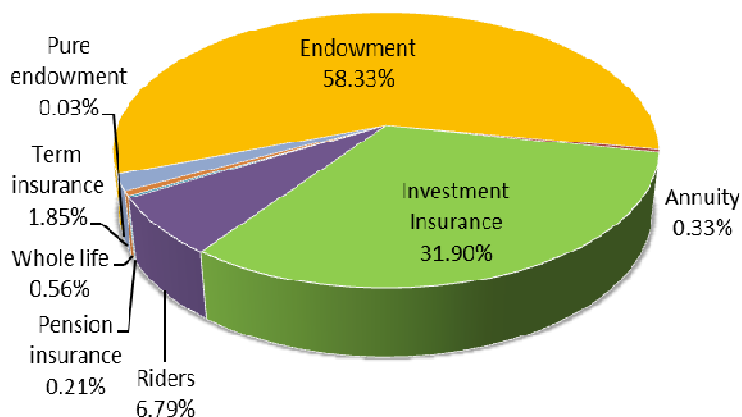


Figure 3: Total premium by products in the first half of 2014.
 Source: Association of Vietnamese Insurers (2015) [7]

Table 2: Pension products and others products in the life insurance companies

Total main products in insurance companies	145
Total accumulate, saving and invested products	65
Total pension products	12
Number of individual products	8
Number of enterprise products	4

Source: Author, 2015

Table 3: Number of life insurance companies providing pension products

Total life insurance companies on the market	17
Companies deploying at least a pension product	9
Companies only deploy individual products	5
Companies only deploy enterprise products	1
Companies deploy both individual and enterprise products	3

Source: Author, 2015

From the data in Table 3, it can be seen that among 17 life insurance companies in Vietnam, nine of them are deploying at least one pension product. Eight LICs are offering individual pension products. AIA is the only LIC that offers enterprise pension products.

4. Features of a typical personal pension product

Because of the predominance of individual pension products over enterprise products in terms of number and policy value, this article focuses on describing the main features of the individual pension products.

4.1. Prerequisites for participation

In order to participate in a contract of pension products, individuals must meet some prerequisites. These prerequisites include age requirement and the total insured money.

a. Age requirement of the beneficiary

The beneficiary is the person who directly or indirectly signs the contract with the insurance company. Most pension products require participation from the age of 18 onwards, however not exceeding an age of 55 years for a woman and 60 years for a man.

b. Total insured money

Some LICs set a minimum insured amount (e.g. with Fubon life the minimum requirement is VND 30 million) or a maximum insured amount (e.g., with Cathay Life the maximum of insured money is VND 2.5 billion).

4.2. Time of contract, benefit, expense and premium

a. Policy term and accumulation period

The policy term is the period of coverage provided by an insurance policy, and the accumulation period is the period of time during which an annuitant makes premium payments. They are two basic terms of any pension product. However, the conditions for the policy term and the accumulation period are quite flexible and depend on the agreement of the two parties to the contract. There are two main types offered in the market.

The first type has the policy term equal to the accumulation period. This type accounts for nearly 20% of the products and the policy term usually ranges from 15 to 20 years. Under this type, every year of the contract the beneficiary has to pay the premium, but companies maybe pay them reversion money. The premium is paid annually but the reversion money depends on the product's features. The typical frequency for reversion money is every two or three years.

In the second type the policy term lasts more than the accumulation period. Under this type, the policy term is divided into two parts. The earlier part is an accumulation period and the latter is a decumulation (i.e. annuity) period. In the accumulation period, the beneficiary pays an annual premium. This amount of money will be accumulated in their account and ends when the annuity date comes (the annuity date must be a date on which the beneficiary is at the age of 55 to 65). In the annuity period, the

beneficiary receives a monthly or annual amount of money from their account for their retirement that lasts for 10 or 15 years depending on the product.

b. Premium payment frequency

The time between two consecutive premium payments is quite flexible. Most companies give customers the right to choose when and how much money they pay each period. However, the most preferred payment frequencies are once or twice per year (6 or 12 months period).

c. Minimum requirement for each premium payment

Similar to the premium payment frequency, the minimum requirement for each premium payment is also flexible. Approximately 50% of the products do not have detailed regulations about this term. The rest are divided into two types. The first type includes products that regulate the minimum amount for each premium payment. Cathay Life and Fubon Life are examples of that type, with the regulation being a minimum of VND 300,000 for each premium payment. The second type includes products that do not specify a minimum amount for each payment but instead set a minimum amount of premium each year. For example, Hanwha Life prescribes the minimum amount of money each year at VND 2 million.

4.3. Costs and expense

When signing a contract for pension products, the terms of costs and expense are a big consideration of customers. Costs and expenses generally include initial the expense, the fund management fee, policy fee, and the cost of insurance and surrender charges.

a. Initial expense (original cost)

The initial expense usually charges for both the initial and additional premium, calculated as a percentage of the premium. For the initial premium, the initial expense is usually specified in the contract, depending on the regulations of the insurance company. Generally, the initial expense for the early years is very high (approximately 25-50%). After the contract reaches a certain date, generally from the 5th year onwards, the initial expense will drop to 0-5% and stay unchanged throughout the remaining years of the contract. For the additional premium, the initial expense has the same calculation and feature as for the initial premium but the percentage of this premium is less than for the initial one. The example in Table 4 gives a realistic view on this issue:

b. Fund management fee

All LICs set a fund management fee at 2% per year. This may make pension products less attractive as this fee is quite high in comparison to those of mutual funds now in the Vietnamese market, such as MB Fund Capital (0.9% per year), and Vinawealth (1.5% per year).

c. Policy fee (contract management fee)

The contract management fee is generally calculated on a monthly basis depending on the product of each company. Most of contract management fees range from VND 300.000 to VND 400.000 per year (approximately from VND 25.000 to VND 33.000 per month). Some companies offer a fixed contract management fee while others increase that fee over the year, with an increase of approximately 5% per year. The fee must be approved by the MOF before being applied in the market.

d. Cost of insurance (hedging expenses)

This cost is very flexible. Most companies charge based on age, some based on age and gender, some based on the value of contracts, etc.

e. Surrender charge (cost of canceling the contract)

Surrender charge is the loss to beneficiaries in case of contract cancellation. This cost is based on the basic premium. It is usually very high in the early years of the contract (up to 100%) and decreases to 10-20% over the following year. Table 5 presents an example for the surrender charge of PVI Sun life.

4.4. Benefits

Benefits are the most important factors of a pension product. Most pension products are designed to emphasize their benefits in order to attract more customers. There are two main benefits for pension products, namely maturity benefit and periodic cash benefit.

a. Maturity benefit

Maturity benefit is the gain which the beneficiary receives when the contract expires. It usually applies for products with the policy term equal to the accumulation period. At the maturity date, the beneficiary will receive approximately $(100 + x)$ % of the total insured money, in which x depends on the companies and type of products. X usually has the value of 50, in some cases, it can be as high as 100. About 20% of pension products have maturity benefit.

b. Periodic cash benefit

Periodic cash benefit is the amount of money the beneficiary receives each period. This is the most basic and the core benefit of a retirement product. All of the pension products on the market now contain this benefit. The payment of the periodic cash benefit is usually annual, bi-annual or tri-annual when the beneficiary is at the age of 55 to 65. However, there are differences in the calculation of periodic cash benefits among products. Based on periodic cash benefit calculation, we can classify pension products into three groups.

Group 1 includes products that have the policy term equal to the accumulation period. During the contract time, while the beneficiary has the obligation to pay the annual premium, the insured person also has the right to receive a specified amount of money at a regulated time until the end of the contract. There are two principles of receiving money. First, the periodic cash benefit is made every period, usually two or three years each. Second, the received money is prescribed and calculated as a percentage of the total insured money, ascending from the first period to the final one, but generally not exceeding 10% each. Table 6 shows an example of Phu Hung Life (16 years-contract product).

Table 4: Initial expense of Dai-ichi Life products based on initial and additional premium

Year of contract	1	2	3	4	5	6	7+
% Initial premium	25	25	25	0	0	0	0
% Additional premium	9	7	7	5	5	2	0

Source: Dai-ichi Life, 2015

Table 5: Surrender charges of PVI Sunlife

Year of contract	1st - 5th	6th	7th	8th	9th	10th onwards
Surrender charges (%)	100	90	70	50	30	0

Source: PVI Sun Life, 2014

Table 6: The periodic cash benefit of Phu Hung Life (16 years-contract product)

Year of contract	3rd	5th	7th	9th	11th	13th	15th
The periodic cash benefit (% total insured money)	4	4	5	5	6	7	8

Source: Phu Hung Life, 2014

Group 2 includes products for which the policy term is 10, 15, 20 or 25 years longer than the accumulation period. The insured person must not withdraw any cash until the end of the accumulation period. Each year from the year in which the premium payment is finished to the maturity date of the contract (usually 10 to 15 years), the insured person will receive an annual amount of money. There are two ways for calculating this money. In the first way, the annual amount of money is fixed and equal to the total

insured money divided by the number of annual cash years as designated in the formula (1).

This way of calculation does not consider the increase of the account value from year to year. That is a serious disadvantage for the beneficiary and thus only one product in the market now applies this calculation method.

The second way alternates the annual amount. Each year, the company will make the distribution based on the formula (2).

$$\text{The annual fixed amount of money} = \frac{\text{The total insured money}}{n} \quad (1)$$

Where n equals the number of annual cash years, i.e.,
 $n = \text{The policy term (years)} - \text{The accumulation period (years)}$

$$\text{The annual payment each year} = \frac{\text{The value of policy owner's account at the beginning payment year}}{\text{Number of remaining period (years)}} \quad (2)$$

Group 3 covers products having characteristics of those in group 1 and group 2. In this type of product, cash will be received once in a period, maybe every two or three years. The amount of periodic cash is regulated in the contract depending on the time of payment; generally ascending from the first one to the last one. Beside the periodic cash benefit, this type of product usually has a maturity benefit (usually equal to 100% of the total insured money). The description of the Cathay Life pension product in Table 7 is a typical one in this group.

c. Death and permanent disability benefits

These benefits are likely a kind of form to make the pension products more attractive. When an insured person dies or encounters a permanent disability, the beneficiary will receive 100% of the total insured money. To become more appealing to customers, some products offer 150% or even 200% of the total insured money. In addition, some products regulate a specific additional amount of money based on a specific situation (time and cause of death or permanent disability).

Table 7: Maturity benefit and periodic cash benefit of Cathay Life pension product

Policy term	20 years		
Received periodic cash benefit each	3 years		
Amount of periodic cash (% of total insured money)	1st to 5 th	6th to 10th	11th onwards
	5%	8%	10%
Maturity benefit	100% total insured		

Source: Author, 2015

d. Other benefits to increase the attractiveness of products

Beside death and permanent disability benefits, in order to have the greater commitment of customers, some products offer financial incentive programs. Those benefits may include longevity benefits (a 1-2% of total insured money bonus when the insured person passes a certain age, usually their 70th/ 80th/ 90th birthday anniversary), contract maintenance benefits (5-10% of the total insured money depending on the time of the contract) and severe diseases benefits (usually 50% of the insured money), etc.

e. Guaranteed rate

The guaranteed rate is one of the most important features for attracting customers. At present, guaranteed interest rates are around 5%, which is quite low compared with the interest rates for saving deposits offered by commercial banks. The calculation of the guaranteed interest rate is quite diverse in the market. There are two main kinds described below:

The first one is where the guaranteed interest rate stays unchanged for the whole duration of the contract. (E.g. Cathay Life, 5% during the contract). About 20% of pension products apply this type of guarantee due to concerns about macroeconomic risks (the Vietnamese economy experienced erratic fluctuations in the period 2007-2014).

The second one is where the guarantee interest rate may fluctuate from year to year. There would be at least two guaranteed interest rates, normally 5% for the first period and 3% for the remaining time of the contract. This kind of guaranteed interest rate helps insurance companies avoid the macroeconomic risks but it is less attractive to customers than the previous one. For example, PVI Sun Life offers a guaranteed interest rate of 5% for the first 5 years and 3% for subsequent years. Dai-ichi Life sets a guaranteed interest rate of 5% for the first 10 years and 3% for subsequent years.

5. Conclusion

Vietnam now is at an early stage of solidifying the social protection system, with the system relying heavily on the government pension system. However, there is a need for private pension products from life insurance companies.

By reviewing the current situation, this article shows that the pension products offered by life insurance companies are very limited in terms of both quantity and variety. Most pension products now on the market are pure saving products and lack investment characteristics, which is one of the most essential features for any modern retirement system. Furthermore, most pension products focus on the pre-retirement period (before 60 years of age) while the post-retirement period is neglected. There is no rating system to compare pension products against each other. Such a rating system can help people make the best investment decisions for their retirement.

To develop a modern pension system, as soon as possible the Vietnam government should have a plan to construct a more comprehensive legal framework for voluntary pension funds - which is the next pillar

according to the World Bank's Pension plan conceptual framework. On the one hand, Vietnam should accelerate the law-making process by taking into consideration the experience of other countries; especially the countries in the ASEAN (e.g. the successful Private Retirement Scheme of Malaysia). Broad reforms are necessary to realize the insurance sector's potential in general and pension products in particular. Pension products that cater to all segments of society should be supported by better regulation and supervision, and in the longer term. Regulations should be strengthened to incorporate international standards, especially with regard to capitalization and reserves [4].

On the other hand, the Vietnam government should support life insurance companies to continue deploying pension products and enrich product variety. This support can be in the form of preferential policies such as tax exemption on the premium payments or the encouraging of government employees to join private pension schemes offered by life insurance companies.

Further research about the pension system in Vietnam should focus on seeking customer insights and identifying customer tendencies when participating in a pension product's contract. The exploration of enterprise pension products and their effectiveness is

also a relevant topic and may have many practical implications for the Vietnamese pension system.

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