

## Income replacement rate as an indicator of pension adequacy

Globally, one of the key indicators of pension system adequacy is the **Income Replacement Rate (IRR)**, which reflects the ratio of a pension to a citizen's previously earned income. According to ILO (International Labour Organization) recommendations, a pension is considered adequate if the IRR is **at least 40%**. In OECD (Organization for Economic Co-operation and Development) countries, the average combined IRR is **approximately 60%**.

In Kazakhstan, the current IRR, calculated as the ratio of the average combined pension to the average wage in the country, is **approximately 44%**. This IRR level corresponds to the ILO minimum recommendation, but is lower than in OECD countries.

More than half of the combined IRR is provided by the paid-in pension. However, as the length of service before 1998, which is taken into account when calculating the paid-in pension, decreases for new retirees, the **funded pension** is becoming increasingly important for them.

The increasing role of pension savings is a **global trend**. This is due to changing demographics and labor markets, leading to the financial instability of pay-as-you-go (practice-based, insurance-based) systems. According to international studies, the number of countries that have implemented mandatory pension savings for citizens has grown from 17 in 1999 to more than 50 today.

In a funded system, the size of a future pension directly depends on the amount of savings in an individual pension savings account. Savings grow through pension contributions and investment income; **they are owned by citizens**, which encourages them to save.

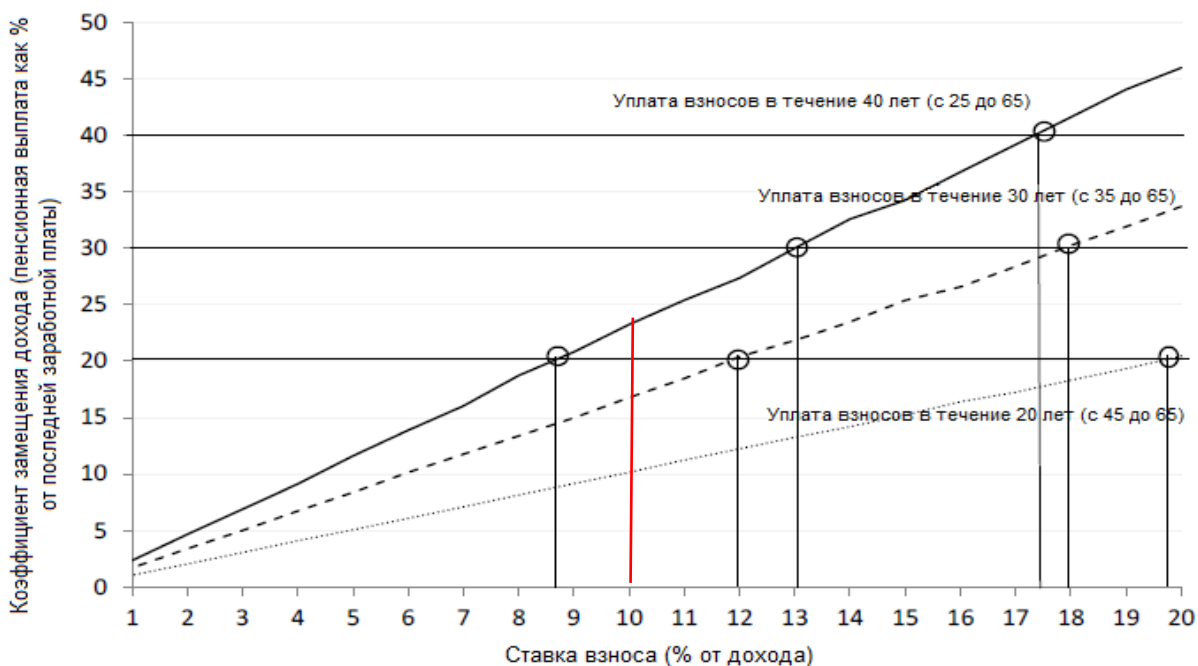
To ensure a decent pension, **three key conditions** are essential:

- **duration** of participation in the system throughout one's working life;
- **regular** payment of contributions (preferably monthly, 12 times a year);
- **full** payment of contributions from all earned income.

Long-term actuarial calculations by the OECD<sup>1</sup> demonstrate the dependence of the IRR on the pension contribution rate, duration, and regularity of contributions (diagram below). OECD calculations show that continuous participation in a funded pension system and regular contribution payments over a long period significantly increase future pensions.

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<sup>1</sup> Source: OECD REVIEWS OF PENSION SYSTEMS: MEXICO © OECD 2015



*Income replacement rate, contribution rate and frequency*

As the diagram shows, to achieve an IRR of at least 30% from funded pensions alone, pension contributions must be paid:

- 1) at a rate of at least 13% for 40 years;
- 2) or at a rate of at least 18% for 30 years.

It should be noted that the contribution rates used in international practice correspond to the OECD calculations. For example, in OECD countries, the average pension contribution rate is 18.8%, while in countries with advanced pension systems included in the Mercer CFA Institute Global Pension Index (MCGPI) 2025, the average rate is approximately 17-18%.

Kazakhstan is implementing measures to gradually increase the minimum basic pension from 2023 to 2027 (from 54% to 70%, and the maximum pension from 100% to 120% of the subsistence minimum).

In many countries, pension systems involve not only employees but also employers, who also make contributions to their employees. Therefore, in line with international practice and calculations, Kazakhstan has introduced employer's compulsory pension contributions (ECPC) in addition to employee's compulsory pension contributions (CPC), with a gradual increase in the contribution rate from 1.5% to 5% from 2024 to 2028. The contribution rates (10% CPC and 5% ECPC) are now in line with international practice and OECD actuarial calculations.

As a result, in Kazakhstan's multi-pillar pension system, responsibility for pensions is shared between the state, employer, and employee.

*UAPF was founded on August 22, 2013 on the basis of GNPF APF JSC. The founder and shareholder of the UAPF is the Government of the Republic of Kazakhstan represented by the State Institution Committee of State Property and Privatization of the Ministry of Finance of the Republic of Kazakhstan. Trust management of UAPF pension assets is carried out by the National Bank of the Republic of Kazakhstan. In accordance with the pension legislation, the UAPF attracts compulsory pension contributions, employer's compulsory pension contributions, compulsory occupational pension contributions, voluntary pension contributions, as well as carries out enrollment and accounting of voluntary pension contributions formed at the expense of the unclaimed amount of guaranteed compensation for the guaranteed deposit, transferred by the organization carrying out mandatory guarantee of deposits, in accordance with the Law of the Republic of Kazakhstan "On mandatory guarantee of deposits placed in second-tier banks of the Republic of Kazakhstan", ensures the implementation of pension benefits. The Fund also carries out accounting of target assets and target requirements, accounting and crediting of target savings (TS) to target savings accounts, payments of TS to their recipients in bank accounts, accounting for returns of TS in the manner determined by the Government of the Republic of Kazakhstan within the framework of the National Fund for Children program (More details at [www.enpf.kz](http://www.enpf.kz))*