

Private pensions in the Central and Eastern European Countries

Investment Restrictions

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General information

- Croatia has 4,2 million inhabitants
- Pension system based on III pillars
 - I. Pillar State pension fund ; contributions paid 15% of gross salary (or 20%)
 - II. Pillar Compulsory; contributions paid 5% of gross salary (currently government considers to make it voluntary for those who were older than 40 at a time of implementation of combined pension system)
 - III. Pillar Voluntary; Two types of Voluntary Pension Funds:
 - For individuals (also called open pension funds)
 - Occupational pension funds (established by sponsors)
- 1,4 million members of Compulsory Pension Funds
- App. 120.000 members of Voluntary Pension Funds. To make voluntary pension funds interesting for people tax allowances and state subsidies for individuals exist
- Only DC Pension Funds

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Current situation

- Pension Funds (II. Pillar) are treated as a part of social security system and as such many quantitative limits exist (but also for voluntary pension funds which are not a part of social security system)
- Within set limits prudent person rule applies
- Strong home country bias not only because of the restrictions implemented by the law (max 20% foreign investment, min 50% in Croatian government securities)
- Management company guarantees certain return of the pension fund. Guaranteed return is based on average performance of pension funds; consequence → similar asset allocations
- Currently very limited possibilities to hedge portfolios
- All the assets must be managed internally
- It is strictly forbidden to buy securities issued by related parties

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Turnover on ZSE

Shares	Market cap. mil HRK	Daily avg. Turnover	%
HT d.d.	16.313	9,65	11,5
Pliva	15.814	6,85	11,1
ZaBa	11.531	0,19	8,1
INA	11.499	6,82	8,1
Privredna banka	8.235	0,72	5,8
Splitska banka	7.037	0,012	5,0
Erste banka	5.095	0,140	3,6

Total market capitalization of ZSE as per 23 March 2009= 161 billion HRK
Total assets of compulsory pension funds as per Jan 2009 = 22,9 billion HRK
Total assets of investment funds as per Feb. 2009 = 8,1 billion HRK

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Asset allocation of pension funds

Domestic assets 93,93%		Foreign Assets 6,07%	
Shares	10,03%	Shares	1,54%
Government Bonds	68,82%	Government Bonds	3,56%
Municipal Bonds	0,36%	Municipal Bonds	0,00%
Corporate Bonds	4,05%	Corporate Bonds	0,14%
Closed-end Investment Funds	0,26%	Closed-End Investment Funds	0,00%
Open-end Investment Funds	1,52%	Open-end Investment	0,83%
Short Term Securities	1,50%	Short Term Securities	0,00%
Deposits	5,88%	Deposits	0,00%
Cash	1,40%	Cash	0,00%

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Investment limits (Croatia)

- **Up to 10% of the assets can be held in term deposits with the bank or certificates of the deposits**
 - Croatian and EU banks
 - Not more than 2,5% of the pension fund's assets can be held with a single bank
 - Only short term deposits (up to one year)
- **More than 50% of the assets pension fund must hold in securities issued by Croatian government**
 - Partly to cover transitional costs
 - Before pension funds were established, domestic fixed income market was almost non existent; all issues were either Eurobonds or for domestic market Euro linked
 - Today domestic pension funds are the main owners of government debt; secondary fixed income market is again illiquid but primary market is solid
- **Up to 30% of the assets can be invested into corporate bonds, municipal bonds and bonds issued by local governments**
 - In practice issues are small compared to pension funds' assets
 - Secondary market totally illiquid; even before crisis bid/ask spreads were very high; often the only traders on secondary market were underwriters

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Investment limits (Croatia)

- Up to 30% of the assets can be held in domestic and foreign shares
 - Domestic shares
 - First tier quotation: one limit is 10% of the company and sum of pension fund's assets invested into companies where pension fund holds more than 5% of the company must not exceed 15% of the fund's assets; second limit pension fund can invest up to 5% of fund's assets into single company but invests more than 3% of the fund's assets into shares of a single company than sum of such investments must not exceed 15% of the fund's total assets
 - Regular market (JDD quotation): to be investible for pension fund market capitalization of the company has to be higher than 100 million EUR at a time of the first investment, after it is investible if market cap. is higher than 87 million EUR, and if market cap. falls below 80 million EUR pension fund is forced to sell the stake; there is also a limit concerning a free float of the company
 - Foreign shares
 - Shares must be listed on official market
 - EU and OECD countries with credit rating not below Croatian
 - Market capitalization must be higher than 300 million EUR
- ❖ Limits concerning Regular market (JDD quotation) currently make problems to market. Due to financial crisis a market caps of a number of companies fell below minimum and consequently pension funds will be forced to sell; regulators temporarily postponed forced selling but fear on the market exists and prices fall even further
- ❖ According to the new Capital markets law, companies listed on regular market can easily delist (those companies were forced to list in a period of mass privatization)

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Investment limits (Croatia)

- Up to 30% of the pension fund's assets can be invested into units of open-end investment funds and shares of closed-end investment funds registered in Croatia, EU or OECD countries.
 - Up to 5% of the assets can be invested into investment funds of a single management company
 - Net Asset Value of domestic investment fund must be higher than 100 million HRK (13,3 million EUR), Net Asset Value of foreign investment funds must be higher than 100 million EUR
 - Pension fund's share of a particular investment fund can not exceed 20% of NAV
- Up to 2% of the pension fund's assets can be invested into private equity funds

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Investment limits

- Derivatives
 - According to the law pension funds are allowed to invest into (only for hedging purposes):
 - Futures
 - Options
 - FX Forward contracts

Currently pension funds can use only FX forward contracts. Concerning all other derivatives mentioned above precise regulation by Regulators must be issued

- Capital Guaranteed Products are allowed by the law but additional regulation is needed
- Hedge Funds are not allowed
- Direct investments into real estate is not allowed
- Up to 20% of the assets (25% for voluntary pension funds) can be invested into eligible foreign securities (EU and OECD countries)

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Changes

- After Croatia joins EU concerning investment limits Croatia and EU countries will, be equalized

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Overwiev open end investment funds for 2007-2008

Investment fund Market cap bill. HRK	2007	2008	February 2009
equities	14,419	2,753	2,239
balanced	9,784	2,150	1,763
bond	0,674	0,510	0,485
cash	4,140	3,907	3,547
total	29,026	9,307	8,036