Supervisory regime for pension funds in Romania

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Private Pension Systems in the CEE Countries

APAPR – Who we are

- APAPR is the Association for Privately Managed Pensions in Romania (**www.apapr.ro**);
- 21 members: 16 pension management companies + 5 custodian banks;
- We represent over 99% of the pensions industry in Romania (both in terms of participants and assets);
- We care for the best interest of ~4.7m pension fund participants (2nd and 3rd pillar).

Agenda

1) Brief system design and private pensions institutions;

2) Current market status and challenges ahead;

3) Supervisory regime for PFs: focus on investment and guarantees.

1) System design: architecture

- 1st pillar: PAYG, 1:1 ratio (contributors: beneficiaries, down from 3.3:1 in 1990), 4.7m beneficiaries, contribution rate: 31% of gross wages; system is affected by rapidly aging population and abusive early retirement (mostly ‘90s), over 3.05m beneficiaries receive <175EUR as monthly pay;

Our private pensions system: multi-pillar, World Bank model, pure DC, fully funded, based on personal accounts, individual, non-occupational.

- 2nd pillar: mandatory for <35y, optional for 35y-45y, open only to employees paying social tax in 1st pillar, started in 2007 (4M campaign started in Sept.), 2% contribution (to reach 6% in 2016-2017), EET;

- 3rd pillar: open to all earners of income, started in May 2007, some tax incentive, contributions <15% of gross income, EET.

1) System design: institutions

- CNPAS: National House of Pensions – central collection agency for 2nd pillar;

- CSSPP: Private Pensions System Supervisory Commission, institution under Parliament control.

Challenges ahead:

- freeze in 2nd pillar contribution at 2% in 2009 (instead of increase to 2.5%): measure expected to shed EUR 1.1bn from pension funds until 2017;

- other populist measures tempt some circles – most visible proposal: imposing annual “inflation guarantee” of 2nd pillar funds’ performance, already rejected by Parliament.

2) Market status

- 2nd pillar:

	End 2008	March 2009	End 2009
Participants (mn.)	4.53	4.65	5?
Net assets (EUR mn.)	209	275	517

(2nd pillar market expected to reach EUR 20-25bn by 2020.)

- 3rd pillar:

	End 2008	March 2009	End 2009
Participants (thousd.)	150	165	200-220
Net assets (EUR mn.)	21.1	25.8	46.5

2) Investments & performance

■ 2nd pillar:

	2008	Feb. '09
T-bonds and T-bills	**60.49%**	**58.39%**
Municipal bonds		**2.93%**
Corporate bonds	**24.14%**	**25.31%**
Bank accounts	**13.2%**	**11.45%**
Listed shares	**1.72%**	**1.21%**
Mutual funds	**0.46%**	**0.7%**

2008: 6.96% nominal weighted average return between 20th May and 31st December (11.3% annualized);
First 9M: 8.9% nominal weighted average return between 20th May '08- 20th February (11.9% annualized).

■ 3rd pillar:

	2008	Feb. '09
T-bonds and T-bills	**65.16%**	**55.12%**
Municipal bonds		**10.36%**
Corporate bonds	**17.26%**	**18.95%**
Bank accounts	**12.43%**	**10.84%**
Listed shares	**4.26%**	**3.99%**
Mutual funds	**0.88%**	**0.74%**

2007: 2.55% nominal weighted average return (June – Dec.), that is 5% annualized;
2008: 2.71% nominal weighted average return;
Total (May '08 – Feb. '09): 6.06%

3) Supervisory regime for PFs

Very strict legislation and clear restrictions regarding:

- Instruments for investment by PFs;
- Investment limits (% ceilings by asset class);
- Converting contributions into PF units;
- Valuation of PF units;
- Maintaining investments within not only legal limits, but also within limits imposed by PF prospectuses;
- Guarantees: nominal capital preservation guarantee (2nd pillar only), market relative guarantee (2nd and 3rd pillar PFs).

3) Supervision: investment limits

- up to 20% of their assets in **bank accounts** and money market instruments;
- up to 70% in **state bonds** issued by Romania, a EU state or a European Economic Area (EEA) state, with a 50% sublimit for T-bills;
- up to 30% in **municipal bonds** issued by Romania, a EU state or a EEA state;
- up to <u>50% in **equity listed**</u> on stock markets in Romania, EU or a EEA state, with sublimits: 35% for Romanian shares, 35% for EU or EEA states;
- up to 30% in **corporate bonds** issued by Romanian, EU or EEA companies;
- up to 15% in **state bonds** issued by other states, with sublimits of up to 15% in US, Canada, Japan and 5% in other states;
- up to 10% in **municipal bonds** issued by other states, with sublimits of up to 10% in US, Canada, Japan and 5% in other states;
- up to 5% in **listed foreign bonds**;
- up to <u>5% in **mutual funds**</u> in Romania or other countries;
- up to <u>2% in **private equity**</u> (not allowed in private equity funds);
- up to 15% in **supranational bonds** issued by the World Bank, EBRD, EIB;
- up to <u>3% in **commodities** and derivatives on commodities</u>: crude oil and derivates, cotton, coffee, wheat, Cu, Al, Zn, precious metals, traded on regulated markets in the US or EU.

<u>**NOT allowed:**</u> real estate, mortgage bonds (or related), synthetic / structured financial products.

3) Supervision: Guarantees

- **Nominal capital preservation guarantee** (Germany-like), for 2nd pillar PFs only: at any payout from the system, the final account value must at least be equal to the sum of net contributions (contributions minus legal fees);

*[Only 3 fees/charges supported directly by members in PFs: **2.5% upfront fee** (from gross contributions), **0.6% p.a. AM fee** (from funds' net assets) and the annual audit fee. All other costs / fees / charges are to be supported by the pension company.]*

- **Market relative guarantee** (common in CEE multipillar): for 2nd and 3rd pillar PFs. Quarterly performance monitoring (starting with the 9th quarter of operation) against a benchmark calculated is relation to the 2year market weighted average return. 2nd pillar rules to be adopted, 3rd pillar: benchmark is min[50%*AVG ; AVG–400bps].

Thank you!

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