



TUAC meeting on pensions, 2.12.2015

COMMENTS ON PENSION FUND ISSUE RAISED IN  
CHAPTER 3 OF OECD BUSINESS AND FINANCE OUTLOOK 2015:

# PENSION FUND “SEARCH FOR YIELD?”

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\* The presentation does not necessarily reflect the views of the OECD nor its member countries.



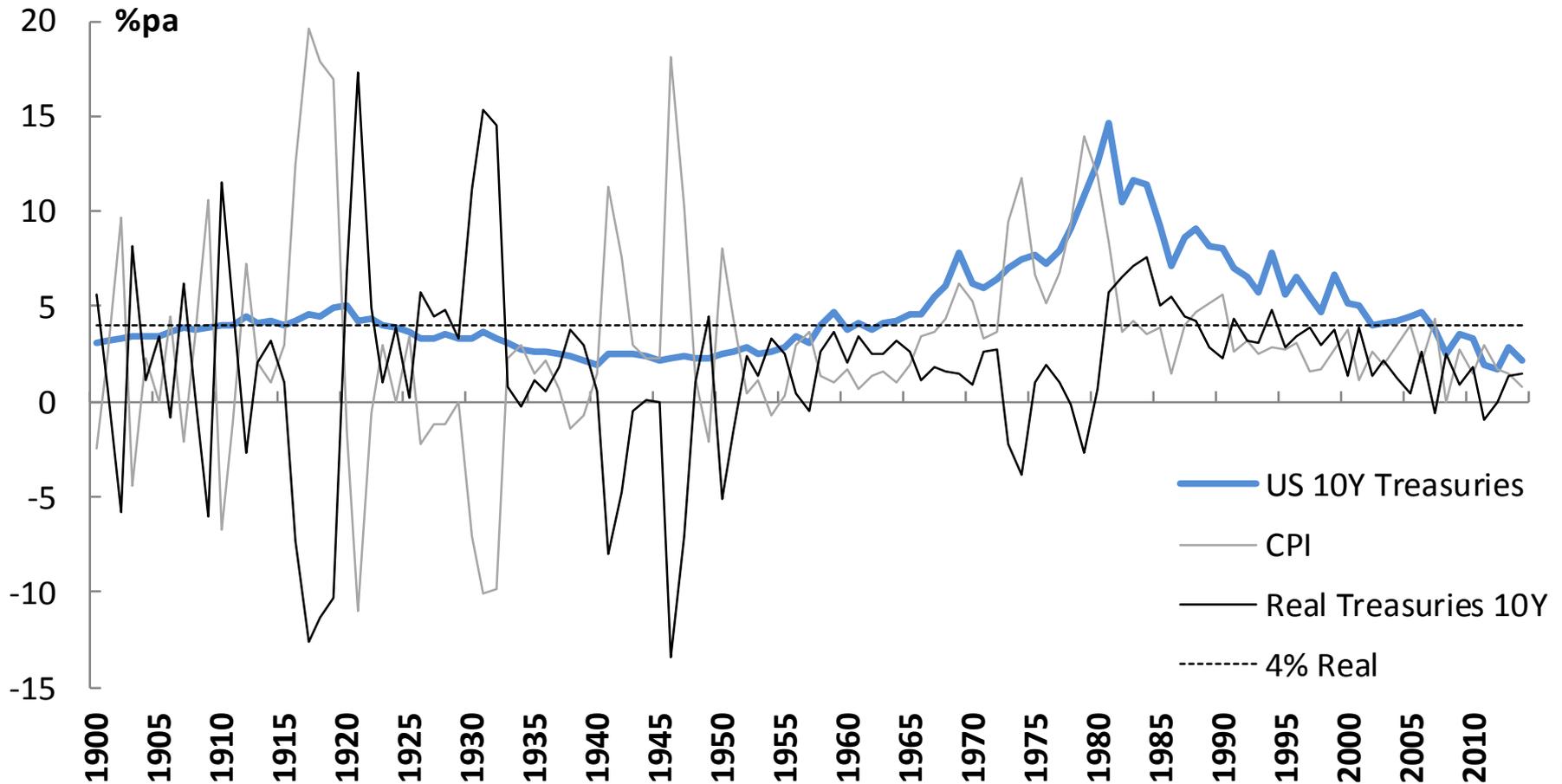
## Overview: Presentation...

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- ...recalls some arguments from chapter 3 of the OECD *Business and Finance Outlook 2015 (henceforth B&F Outlook)*, which
  - observes that interest rates can stay at low levels for a long time,
  - argues that a number of financial contracts are threatened, including in particular those with return guarantees,
  - warns that pension funds might engage in excessive “search-for-yield”.
- ...provides selected updates regarding the interest rate environment, and
- ...adds recent observations regarding evidence for pension fund “search for yield”, based on the OECD *Pension Market in Focus 2015* (November 2015).



# B&F Outlook June 2015: Low interest rates could persist for a long time

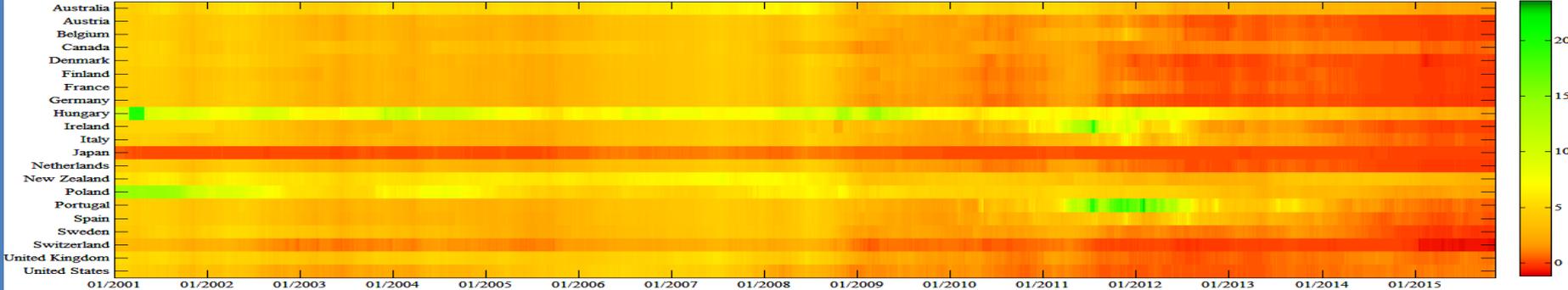


Source: OECD *Business and Finance Outlook 2015*

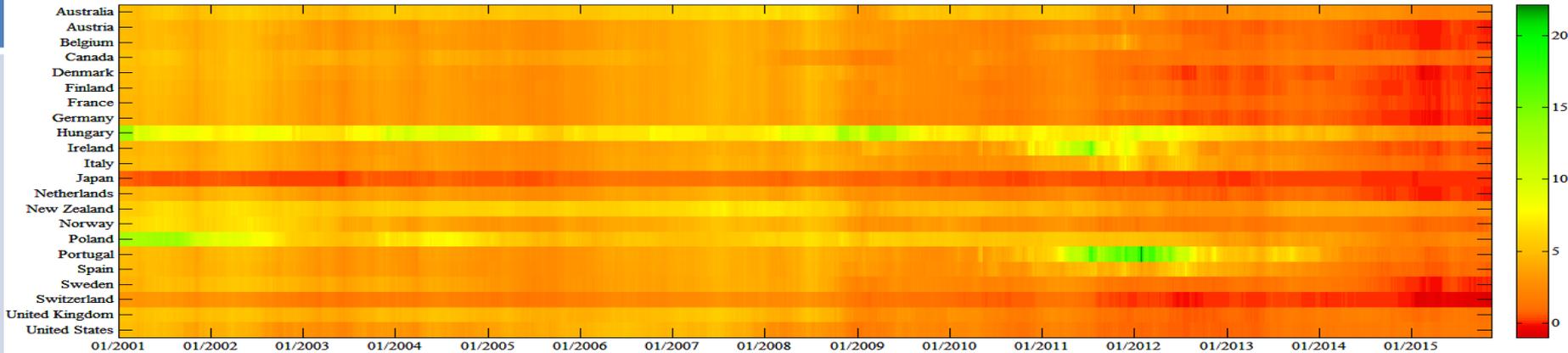


# Update (I): Market rates along the maturity spectrum are oftentimes negative

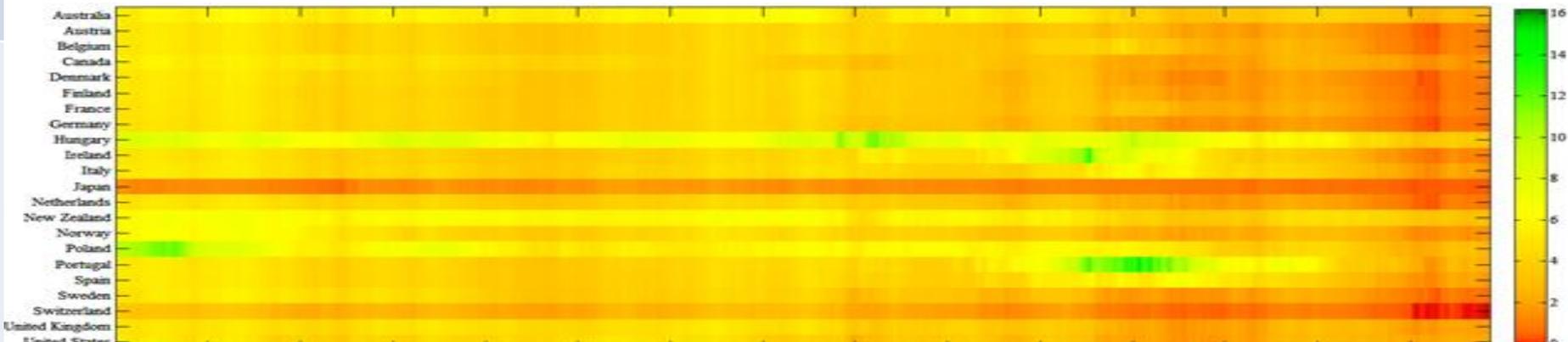
3  
years



5  
Years



10  
years





# Update (II): Illustration of how interest rate levels matter for accumulation of pension savings



Note: Example of time path of asset accumulation and decumulation as a function of real interest rate assumptions, assuming 9.2% saving of annual income (growing at 3%) every year from 20 to 63 years of age. Source: Brühl and Walz (2015).



## What types of financial contracts are threatened?

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- Fixed explicit or implicit fixed payment guarantees
- Risk management challenges reflect in particular the nature of promises, especially mix between defined-benefit (DB) and defined-contributions (DC) elements.
- Pension risk: Not achieving goal of ensuring pension members receive an adequate pension income when in retirement (key risks longevity and investment risk).



# OECD Pension Market in Focus 2015 complements analysis of B&F *Outlook 2015*

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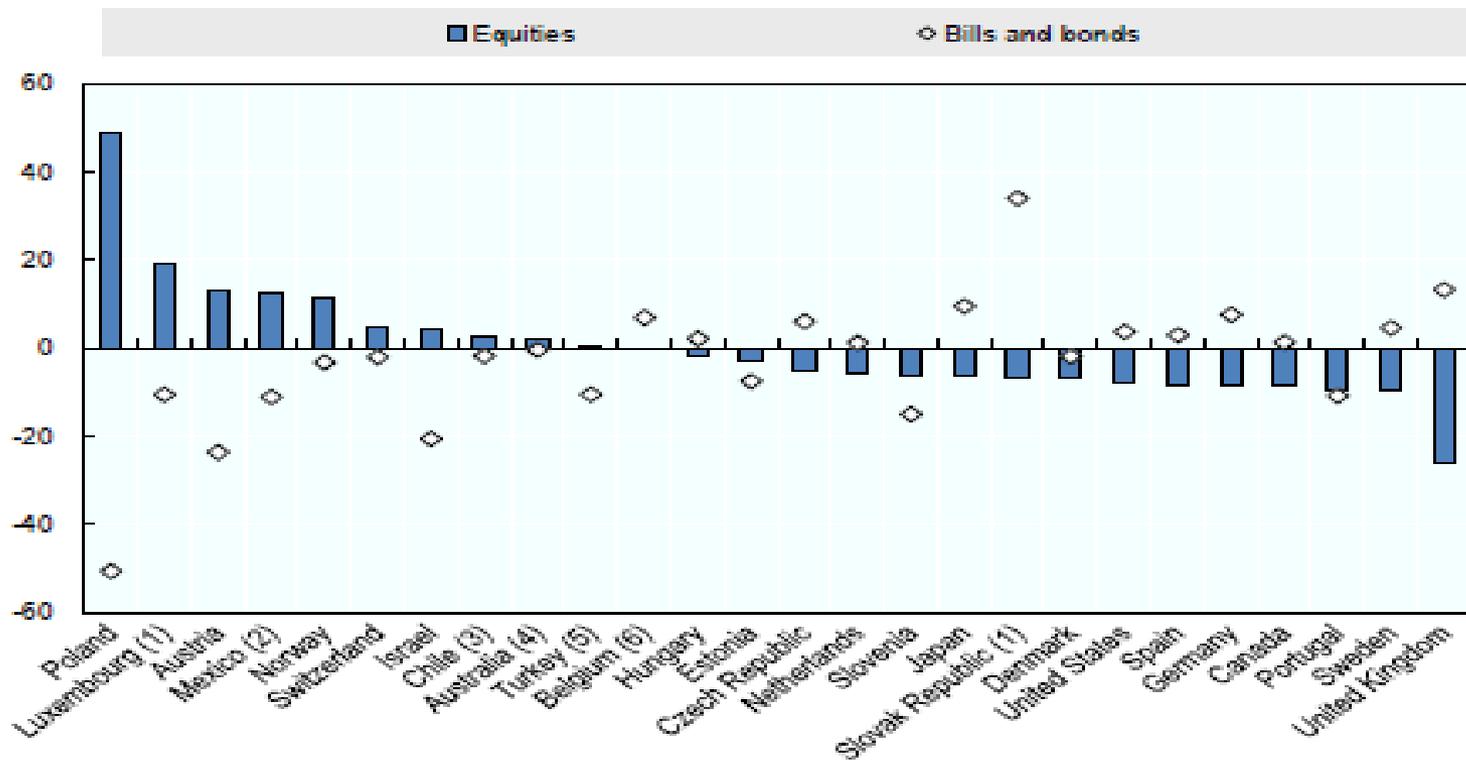
- Pension Market in Focus (PMF) November 2015: *“The analysis in the OECD Business and Finance Outlook did not detect any substantive evidence of a “search for yield” at the OECD aggregated level.”*
- PMF provides complementary analysis, attempting to detect such evidence via:
  - i) shifts from bonds to equity,
  - ii) shift from traditional to non-traditional investments,
  - iii) change in composition of non-traditional investments,
  - iv) increase in foreign investments.



# OECD Pension Market in Focus 2015 (I)

**Figure 12. Variation of investments in equities and bills and bonds over 2004-2014 (or longest time period available), in selected OECD countries**

In percentage points

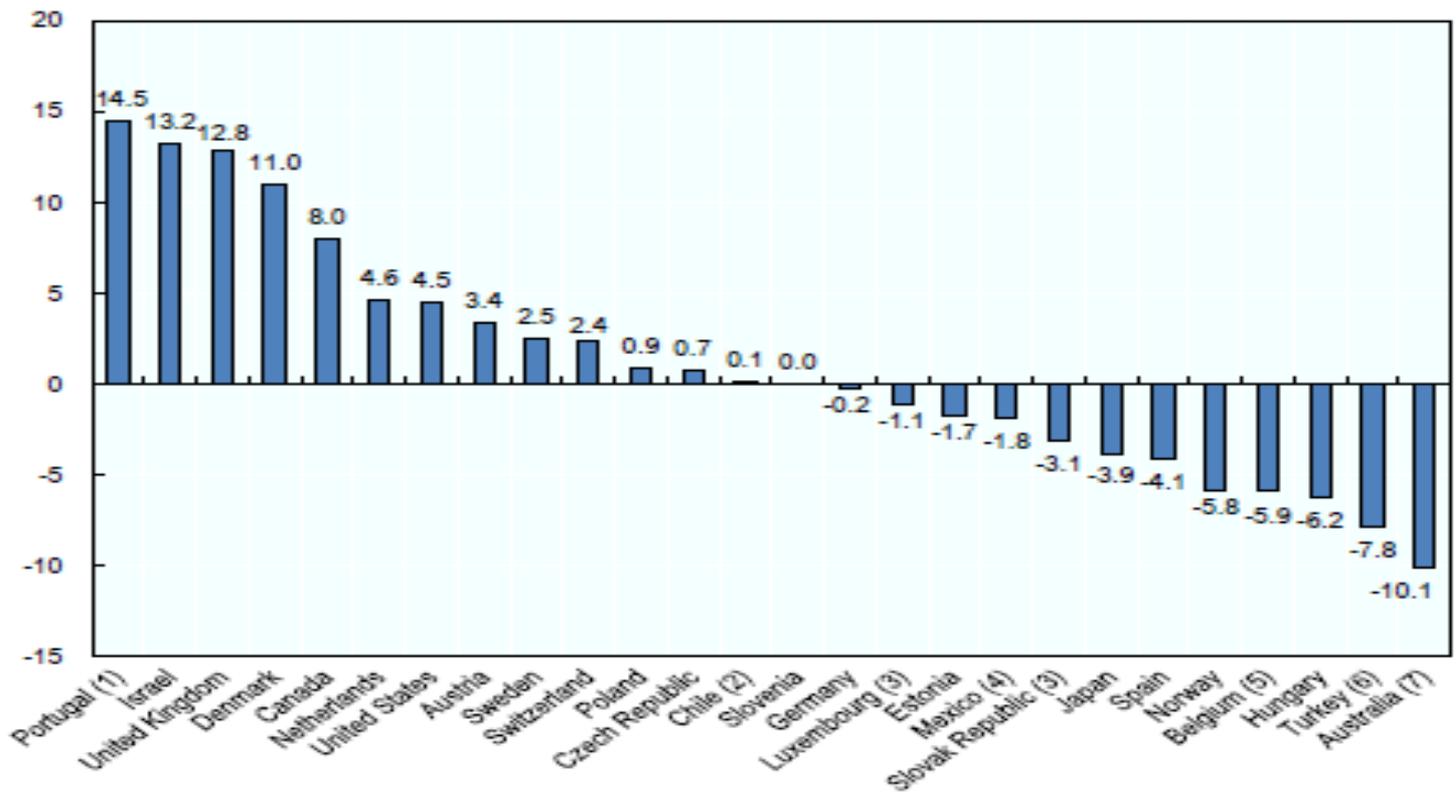




# OECD Pension Market in Focus 2015 (II)

**Figure 14. Variation of investments in alternative asset classes over 2004-2014 (or longest time period available), in selected OECD countries**

In percentage points

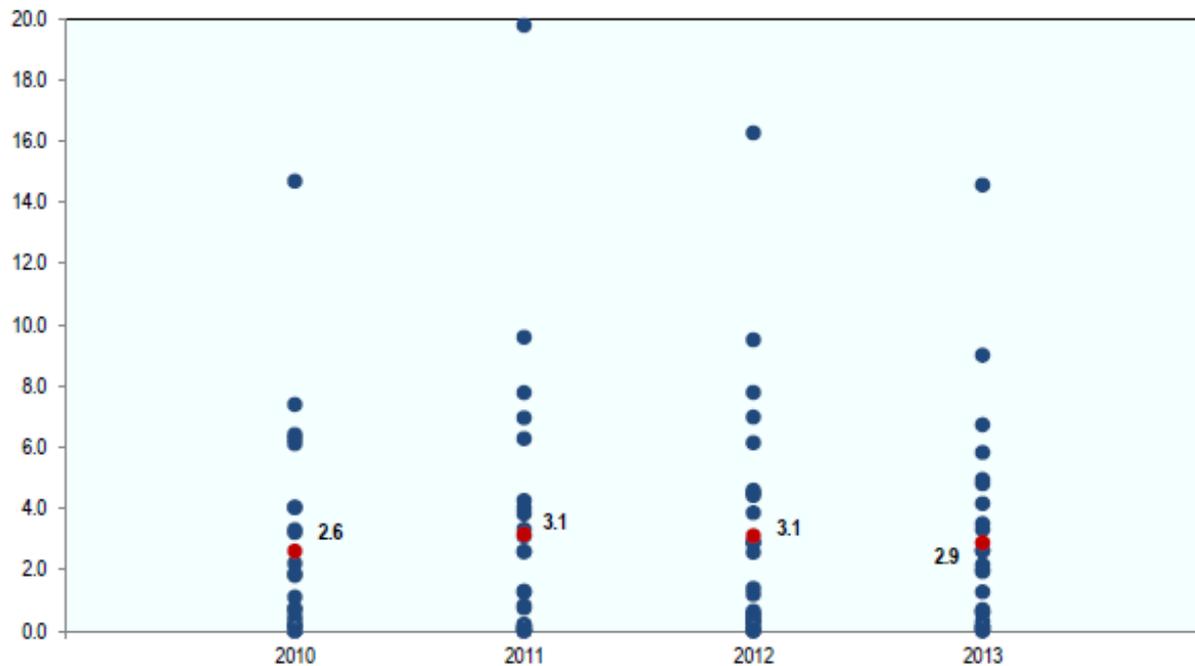




# OECD Pension Market in Focus 2015 (III)

**Figure 17. Investments in hedge funds in selected large pension funds and public pension reserve funds, 2010-2013**

As a percentage of total investment

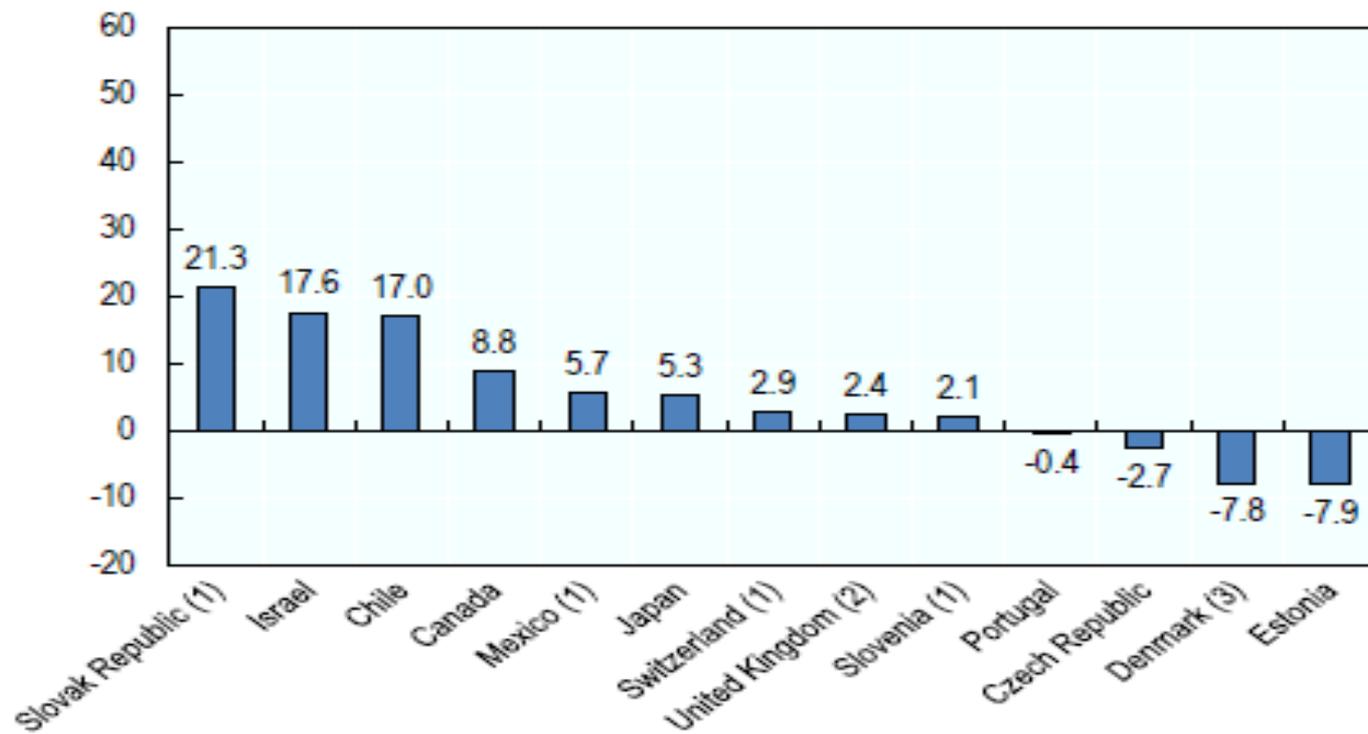




# OECD Pension Market in Focus 2015 (IV)

**Figure 20. Variation of pension fund foreign investments over 2004-2014, in selected OECD countries**

In percentage points





## Concluding remarks

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- OECD *B&F Outlook* of June 2015 warns about excessive “search for yield” and/or that explicit or implicit “pension fund promises” might be broken.
- Based on recent data (November 2015 OECD *Pension Market in Focus*), no clear evidence for “search for yield” -- yet.
- Notwithstanding this observation, fundamental question of how promises can be fulfilled remains valid.



# Selected references

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This presentation:

- OECD (2015a), *Business and Finance Outlook 2015*, June, <http://www.oecd.org/daf/oecd-business-and-finance-outlook-2015-9789264234291-en.htm>
- OECD (2015b), *Pension Markets in Focus 2015*, November, <http://www.oecd.org/finance/private-pensions/pensionmarketsinfocus.htm>.

Selected background reading:

- Antolin, P., S. Schich and J. Yermo (2011), “The economic impact of protracted low interest rates on pension funds and insurance companies”, OECD Journal: Financial Market Trends, Vol. 2011/1.
- Brühl, V. and U. Walz (2015), “Das anhaltende Niedrigzinsumfeld in Deutschland“, CFS Working Paper No. 506, [https://www.ifk-cfs.de/fileadmin/downloads/publications/wp/2015/CFS\\_WP\\_506.pdf](https://www.ifk-cfs.de/fileadmin/downloads/publications/wp/2015/CFS_WP_506.pdf)