



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.

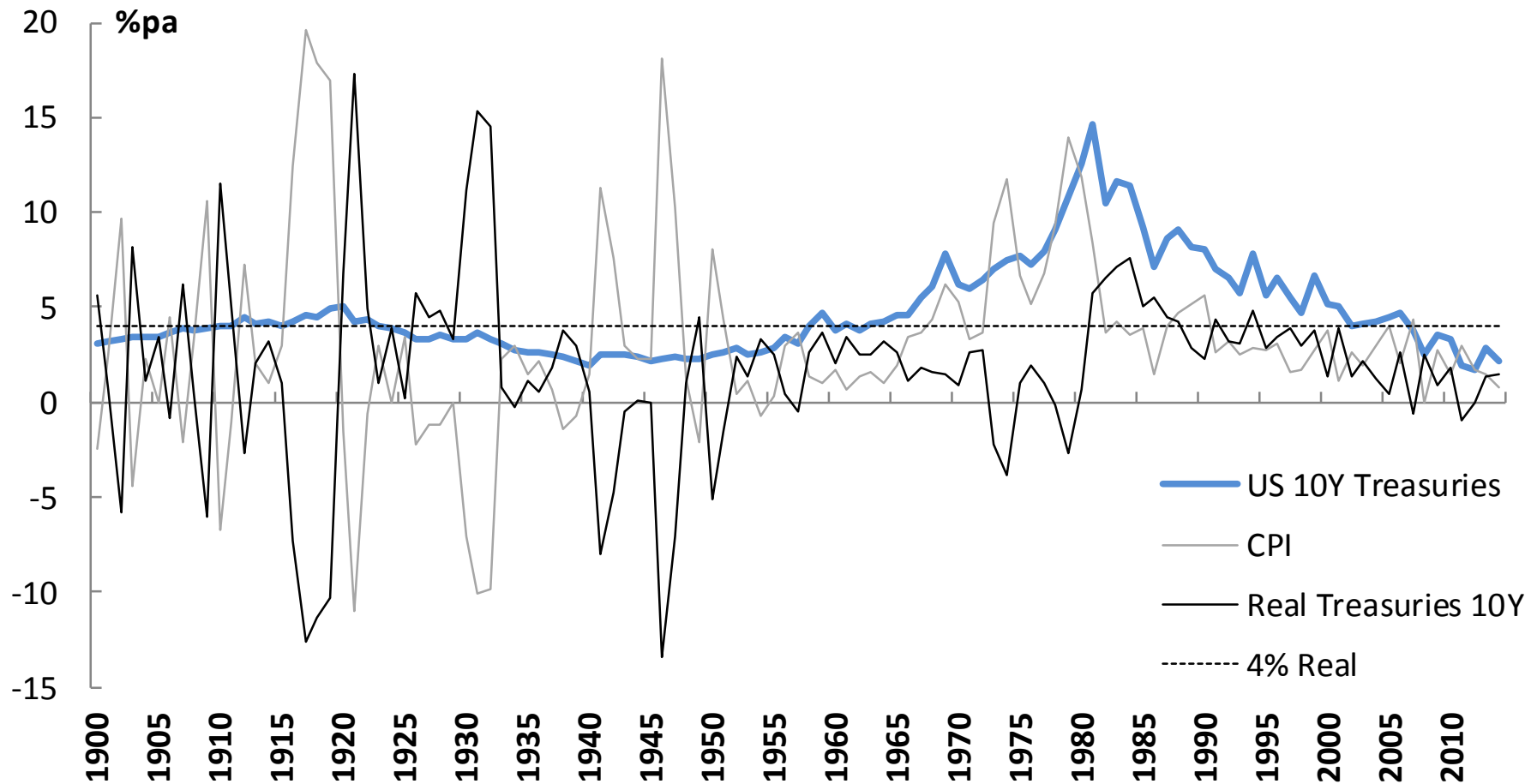


Overview: Presentation...

- ...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

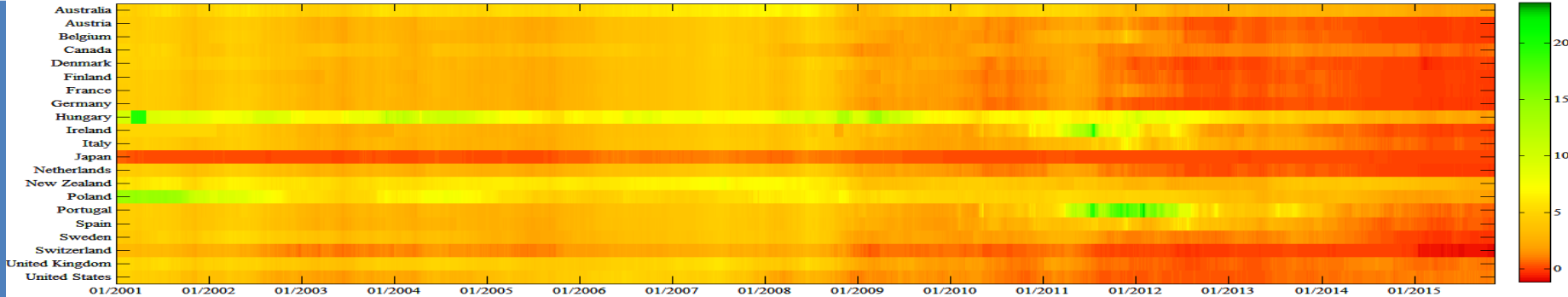


Source: OECD *Business and Finance Outlook* 2015

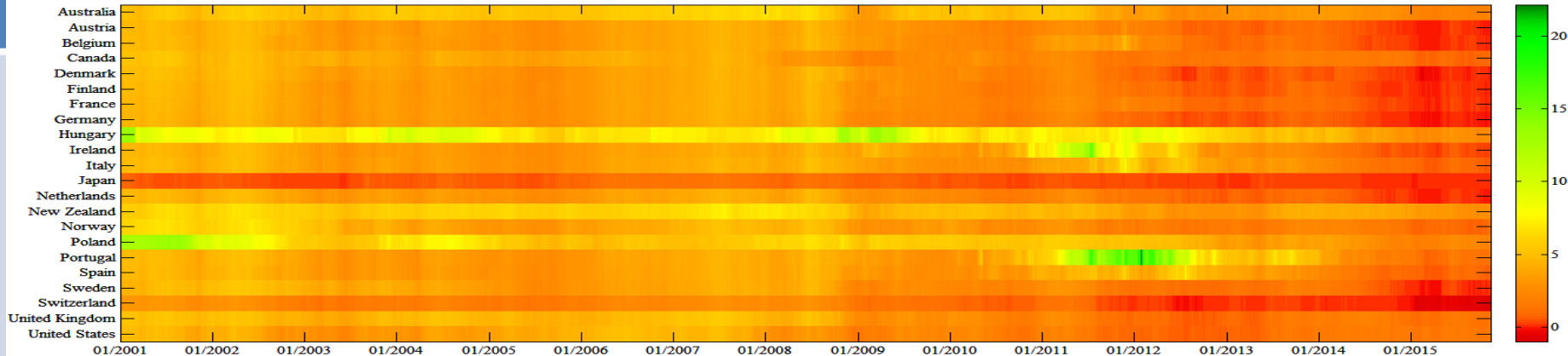


Update (I): Market rates along the maturity spectrum are oftentimes negative

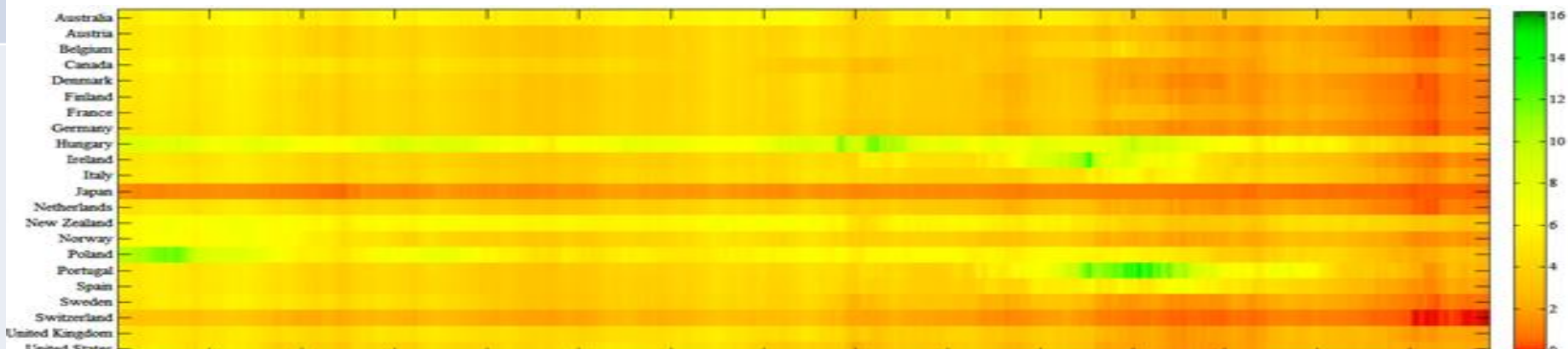
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Update (II): Illustration of how interest rate levels matter for accumulation of pension savings



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?

- 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*

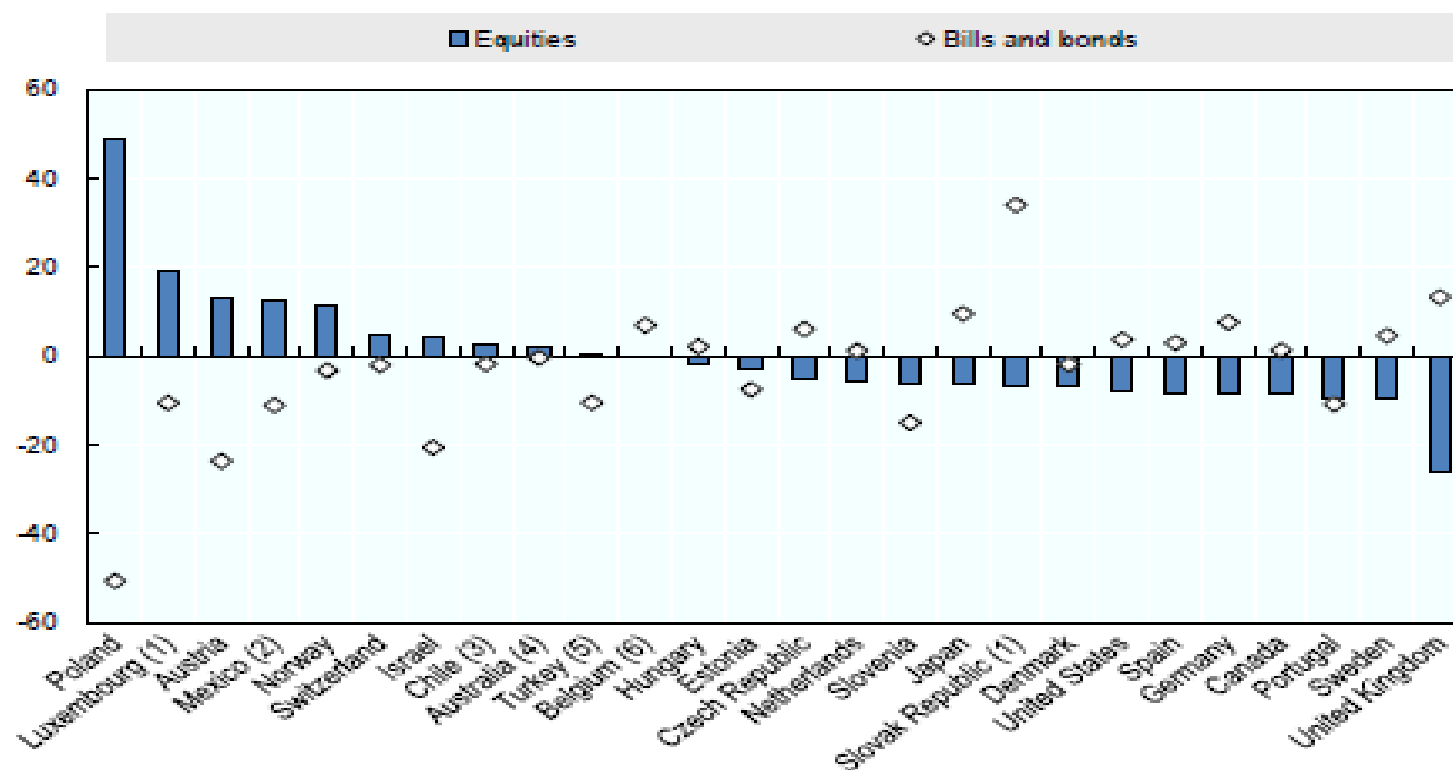
- Pension Market in Focus (PMF) November 2015: *“The analysis in the OECD Business and Finance Outlook did not detect any substantive evidence of a “search for yield” at the OECD aggregated level.”*
- PMF provides complementary analysis, attempting to detect such evidence via:
 - i) shifts from bonds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

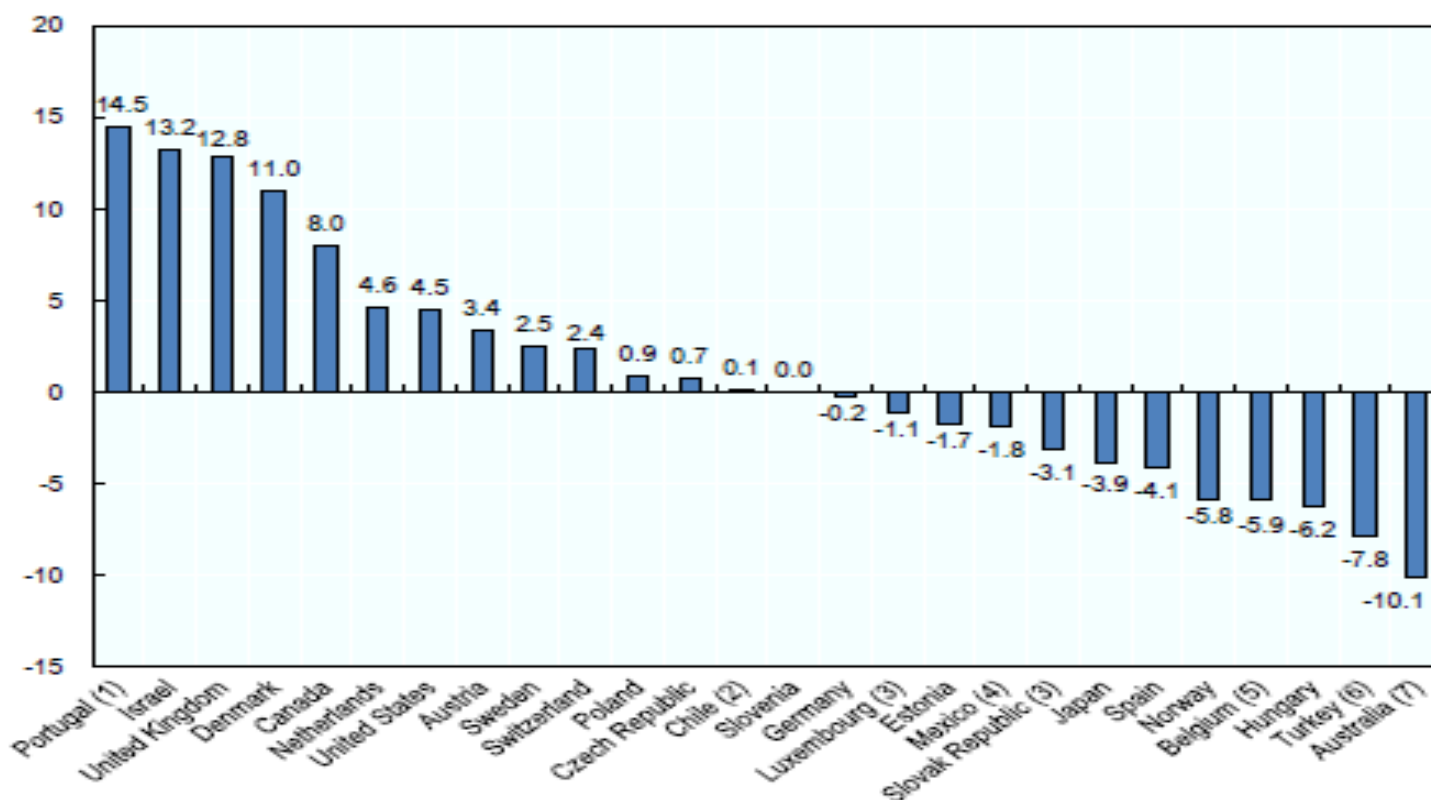




OECD Pension Market in Focus 2015 (II)

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

In percentage points

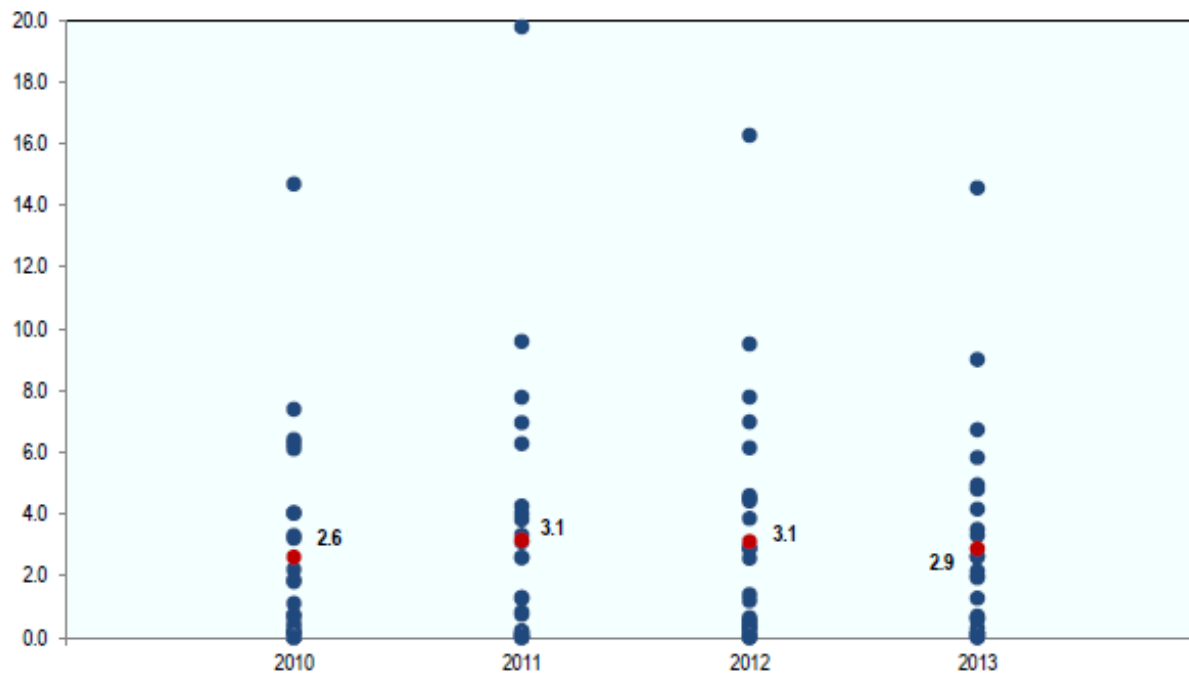




OECD Pension Market in Focus 2015 (III)

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

As a percentage of total investment

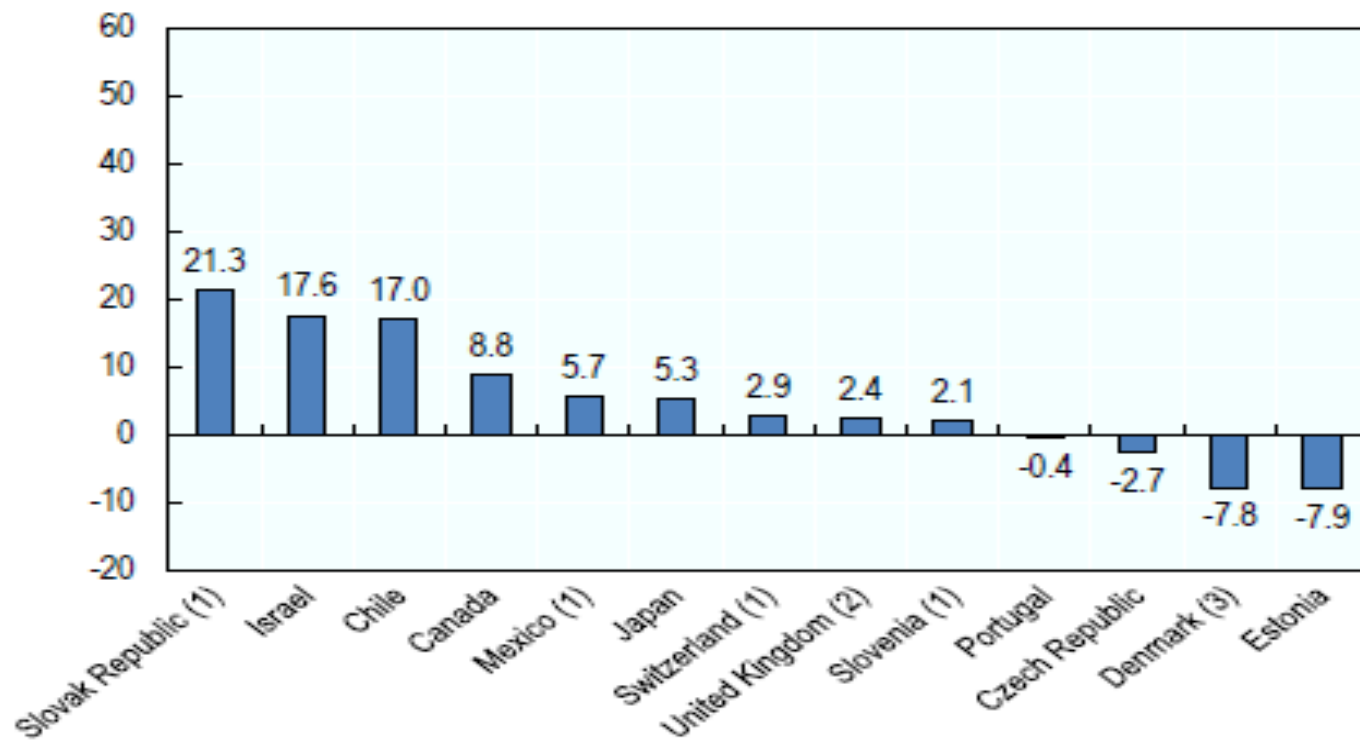




OECD Pension Market in Focus 2015 (IV)

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

In percentage points





Concluding remarks

- 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

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