

OECD - Third Annual Roundtable

Task Force of Middle East and North African Stock Exchanges for Corporate Governance

The role of social security funds as investors in the
MENA capital markets: implications and challenges

2 December 2013 – Muscat, Oman

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“What is an Actuary”

"Actuaries are multi-skilled strategic thinkers, trained in the theory and application of mathematics, statistics, economics, probability and finance. They have been called financial architects and **social mathematicians**, because their unique combination of analytical and business skills are used to address a growing variety of **financial and social** challenges worldwide."

An iceberg floating in the ocean. The tip of the iceberg is above the water, and the much larger base is submerged. The water is a deep blue, and the sky is a lighter blue with some clouds. The iceberg is white and blue, with some snow on top.

Vision, Goals, Strategies, Plans, Systems

FINANCIAL UNCERTINTY

**Culture, Habits, Attitude,
Traditions, Economics,
Demographics,
Political**

Types of Pension Financing

- Pay as you Go
- Pre- funding basis
 - Partial funded
 - Fully funded

International Experience

- UK: 6,150 defined benefit occupational pension schemes (Source: 2013 Purple Book of the Pension Protection Fund)

	2007	2009	2011	2013
Number of Schemes	7,542	6,885	6,432	6,150
Total Assets in billion £	837.7	780.4	968.5	1,118.5
Asset Allocation				
Equities	59.5%	46.4%	41.1%	35.1%
Gilts & Fixed Interest	29.6%	37.1%	40.1%	44.8%
Cash and deposits	2.3%	3.9%	4.1%	6.7%
Property	5.2%	5.2%	4.4%	4.7%
Other	3.4%	7.4%	10.3%	8.7%

- Out of the 35% invested in equities, 50% is allocated to local quoted securities (£196 billion).
- Market Capitalisation was equal to £1.8 trn
- % of Market Capitalization held by DB occupational schemes = 11%

International Experience

- Japan Government Pension Investment Fund - the world's largest pool of retirement savings
- Japan public pension funds have been urged to overhaul their investment strategies, replacing bonds with stocks to support the effort to bring an end to almost two decades of deflation.
- Currently, 16.5% of the funds' portfolio is invested in domestic stocks and approximately 60% to Japan Government Bonds
 - ✓ Assets = \$ 1.2tn
 - ✓ Amount invested in domestic stocks = \$ 0.2tn
 - ✓ Japan capital market capitalization = \$3.7tn
 - ✓ % of Market Capitalization held by Japan Government Pension Investment Fund = 5.5%

Regional Countries Analysis

	Total Assets*	Assets Inv. in the Local Stock Market*	Market Capitaliz.**	% of Market Capitalization held by social insurance schemes/pens. funds
Oman	\$ 11.5 billion	\$ 3.8 billion (33%)	\$ 19.7 billion	19.3%
Bahrain	\$ 10.5 billion	\$1.6 billion (15%)	\$ 17.2 billion	9.3%
Kingdom of Saudi Arabia	\$ 204.5 billion	\$26.9 billion (13%)	\$ 339 billion	7.9%
Qatar	\$ 8 billion	\$2.3 billion (29%)	\$ 125.4 billion	1.8%
UAE	\$ 20 billion	\$370 million (2%)	\$ 93.8 billion	0.4%
Jordan	\$ 7.2 billion	\$4 billion (55%)	\$ 27.2 billion	14.7%

* Source: i.e. Muhanna & Co Data Base

** Source: 2012, OECD, The Role of MENA Stock Exchanges in Corporate Governance

Regional Countries Analysis

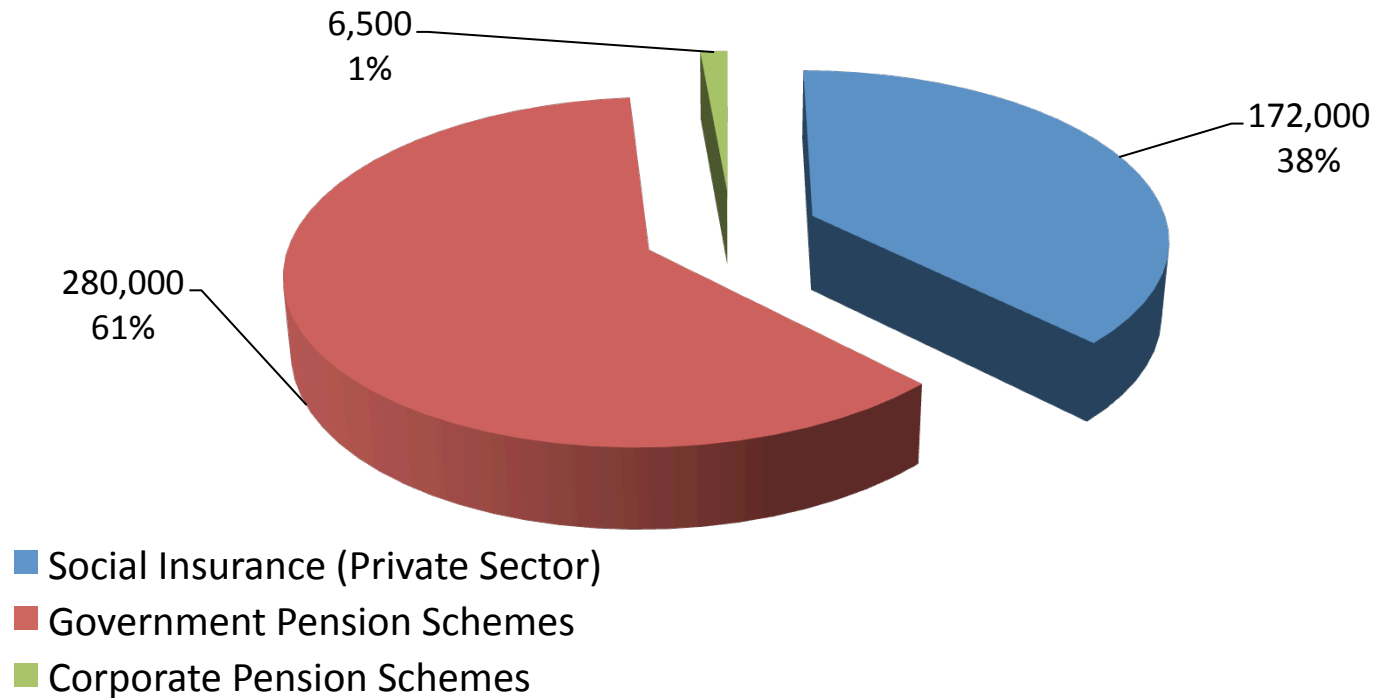
Country	Scheme	Employees Covered	Inception Year	Years since inc. (age)
Oman	Public Authority for Social Ins.	Private	1992	21
	Government Pension Schemes (8 schemes)	Government	Civil = 1986 Mil. = 1993	Civil = 27 Mil. = 20
Bahrain	Social Insurance Organization	Private and Civil	1975	38
	Military Pension Fund	Military	1975	38
Saudi Arabia	General Organization for Social Insurance	Private	1973	40
	Public Pension Agency	Civil & Military	1958	55
Qatar	General Retirement Social Ins. Auth.	Civil & Military	2002	11
UAE	General Pension & Social Sec. Auth.	Priv & Gov	1999	14
	Abu Dhabi Ret. Pensions & Benefits	Priv & Gov	2000	13
Jordan	Jordan Social Security Corporation	Priv & Gov	1978	35

Oman Pension Funds

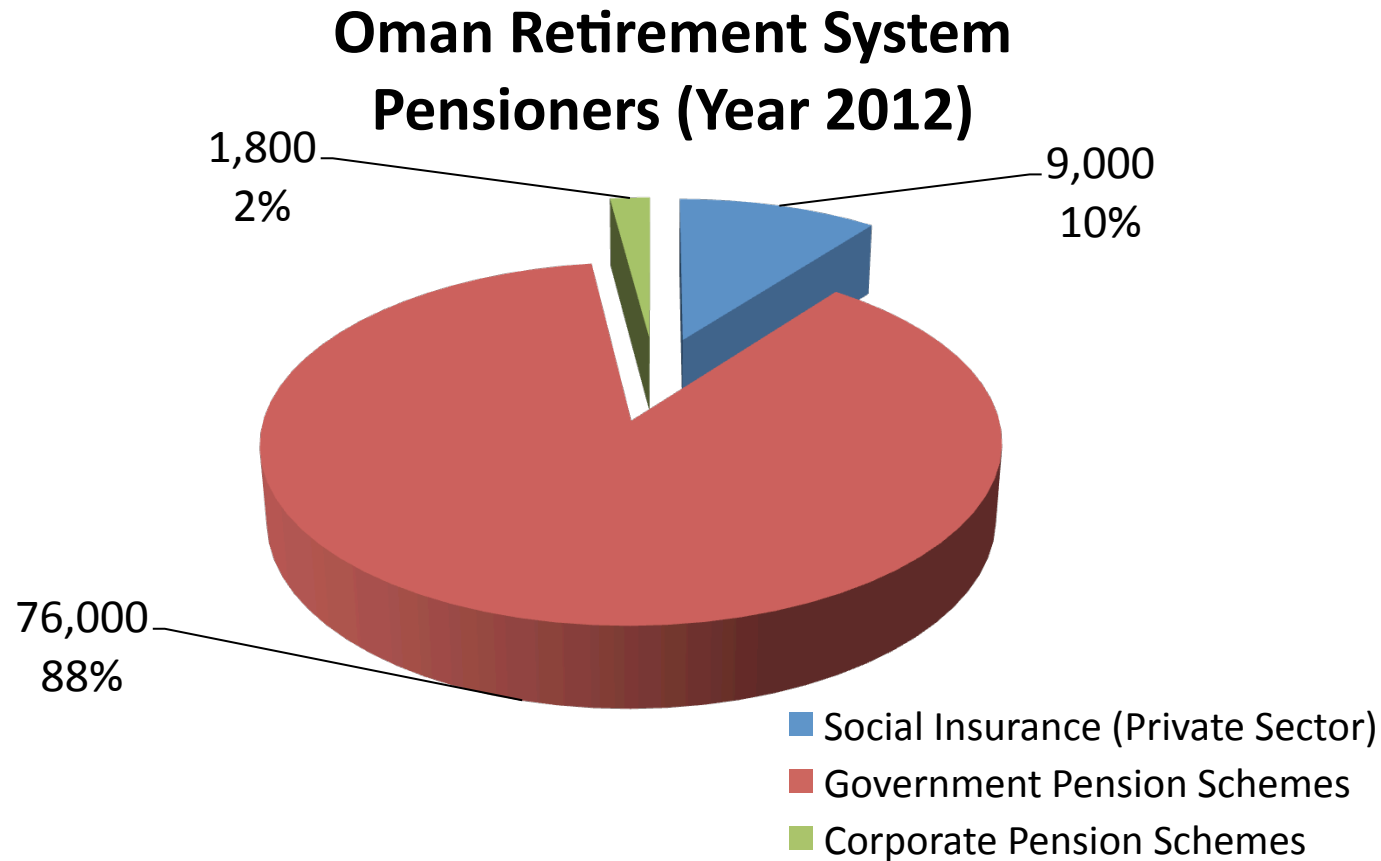
- **Oman Retirement System**
- Defined Benefit Pension Schemes which provide insurance against old age, disability and death
- Targeting an overall retirement benefit that replaces 80% to 100% of pre-retirement income
- ✓ Social Insurance for Private Sector Employees (PASI)
- ✓ Pension Funds for Government Sector Employees (8 pension funds)
- ✓ Pension Funds for employees in private corporations

Oman Pension Funds (statistics)

Oman Retirement System Scheme Contributors (Year 2012)



Oman Pension Funds (statistics)



Oman Pension Funds

- **Schemes' Financing**
- Social Insurance Scheme for the private sector and Government Pension Funds are funded on a partially basis
 - ✓ contributions collected are partly used to pay current expenditure and the remaining are used to build up a fund to meet future liabilities
- Corporate Pension Funds are fully funded
 - ✓ employees contribute a certain percentage of their salary and the employer pays the contribution rate required to cover the remaining cost for the benefit promised

Oman Pension Funds

- What is the exposure of these schemes to the local capital market?
- Information collected for the Social Insurance Scheme and the Government Pension Funds
- Reference Year: 2011

Total Assets*	\$ 11.5 billion
Total Assets Invested in the Local Stock Market*	\$ 3.8 billion (33%)
Market Capitalization**	\$ 19.7 billion
Percentage of Market Capitalization held by social insurance schemes/pension funds	19.3%

* Source: i.e. Muhanna & Co Data Base

** Source: 2012, OECD, The Role of MENA Stock Exchanges in Corporate Governance

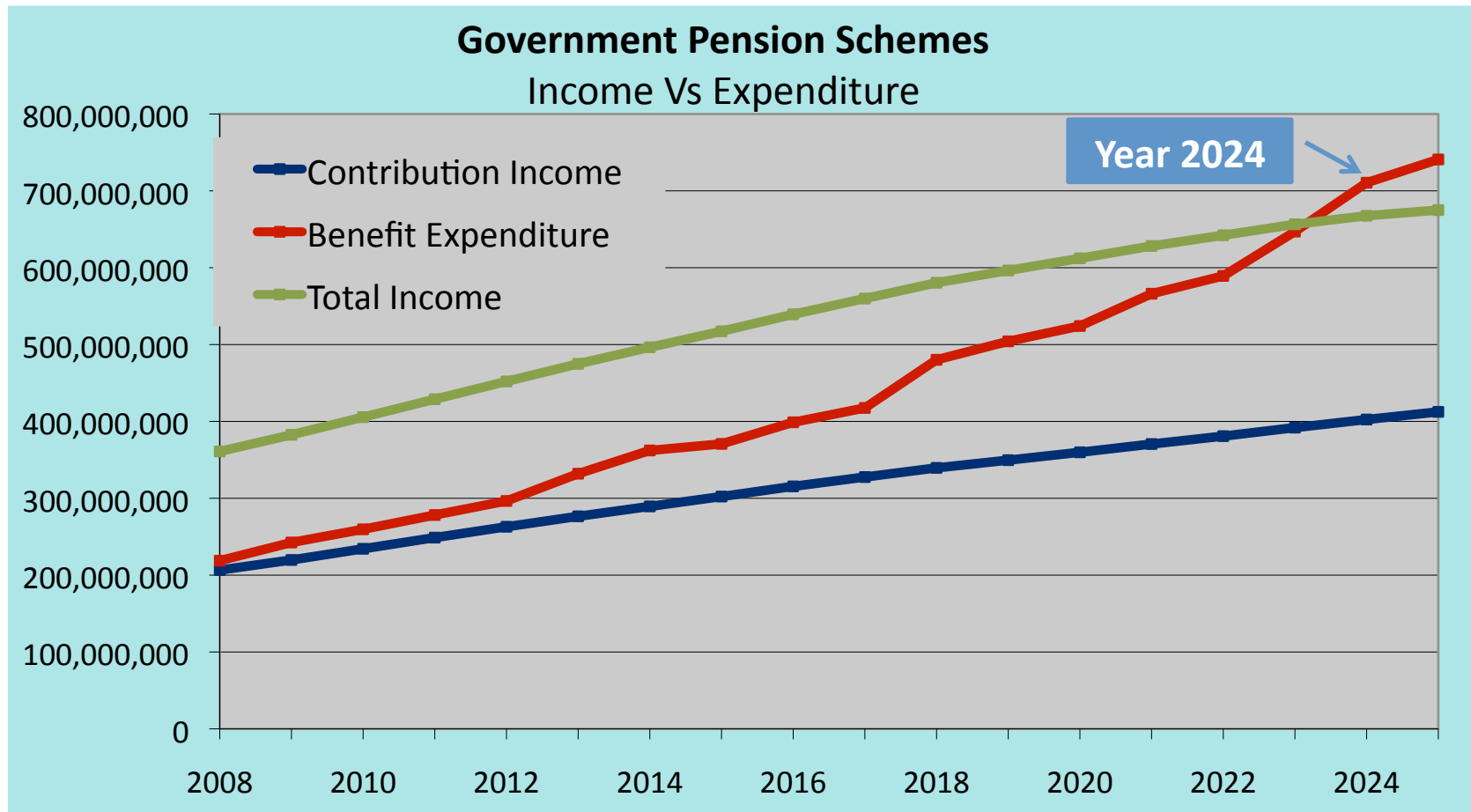
Oman Pension Funds - challenges

- **Schemes' Financial Viability**

- Pension Schemes in Oman and regional countries are characterized by the generosity of the promised benefits
- Inequality between the contribution rate paid and the benefits promised is expected to cause financial strains in the future
- Under some schemes, benefits currently being paid are higher than the contributions received.
- Actuarial Reviews carried out study the expected schemes' cashflows and aim to point out the expected dates at which:
 - ✓ Benefit expenditure is expected to exceed contribution income
 - ✓ Total expenditure (incl. administration expenses) is expected to exceed total income (incl. investment income)
 - ✓ The fund is eventually expected to be depleted

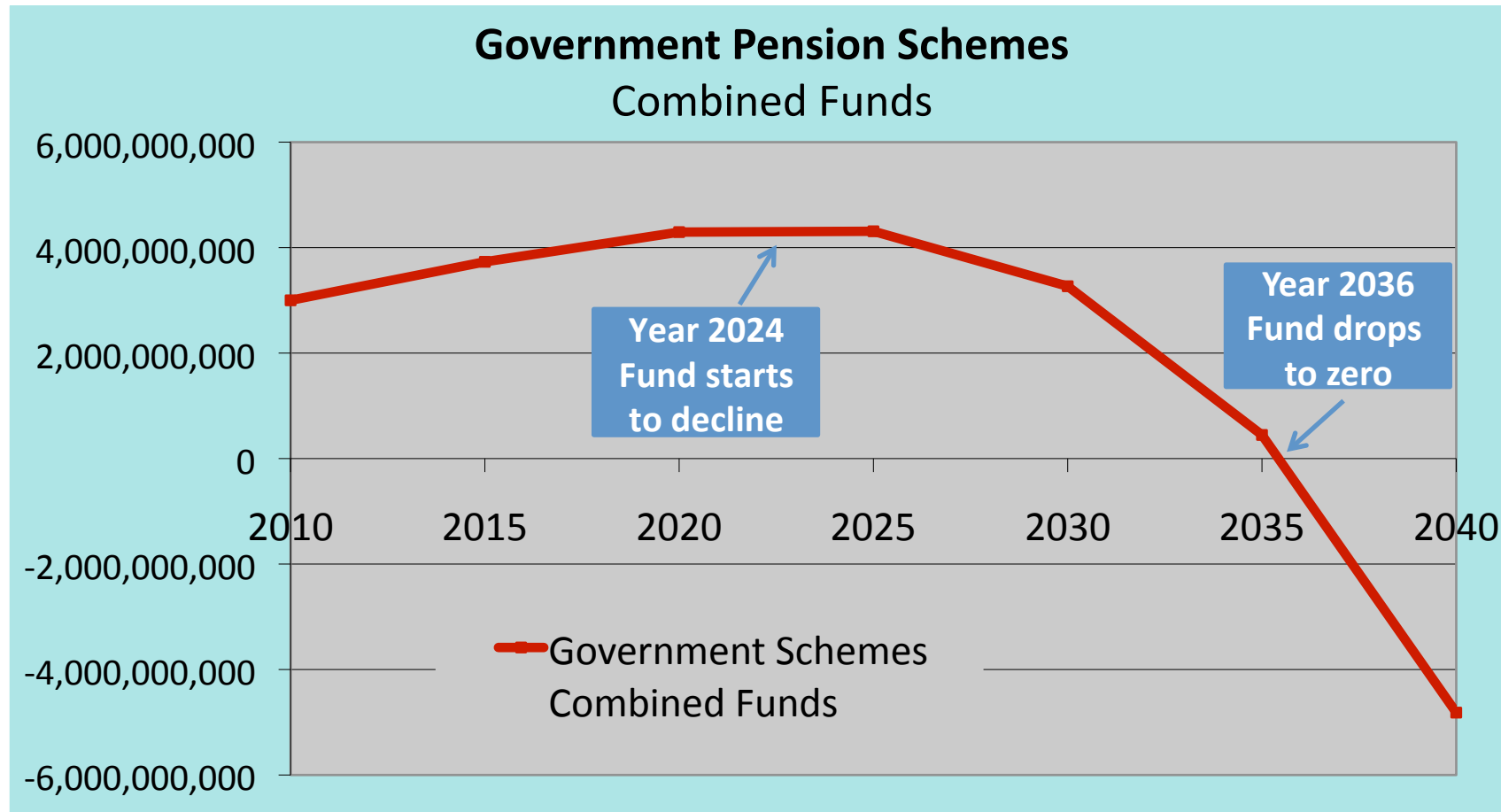
Oman Pension Funds

- **Government Pension Schemes** (Source: i.e. Muhanna & Co Act. Review 2007)
- Benefit Expenditure is already higher than contribution income. In 2024 it was expected that benefit expenditure will be higher than total income



Oman Pension Funds

- **Government Pension Schemes** (Source: i.e. Muhanna & Co Act. Review 2007)
- In 2036 it was expected that the accumulated fund will turn negative



Regional Countries Analysis

- Stock Exchanges

	Stock Exchange	Establishment	Market Capitalization as a % of GDP*
Oman	Muscat Securities Market	1988	27%
Bahrain	Bahrain Stock Exchange	1987	66%
Saudi Arabia	Saudi Stock Exchange (Tadawul)	n/a	59%
Qatar	Doha Securities Market	1997	72%
UAE	Abu Dhabi Securities Market	2000	26%
	Dubai Financial Market	2000	
	NASDAQ Dubai	2005	
Jordan	Amman Stock Exchange	1999	93%

* Source: 2012, OECD, The Role of MENA Stock Exchanges in Corporate Governance

Conclusions

- ✓ Share of market capitalisation held by young pension schemes is low – these are in the process of accumulating assets
- ✓ In countries with developed retirement schemes and multi-pillar systems, share of market capitalisation is high
- ✓ The share of market capitalisation will fall for Retirement systems with financial viability problems and decreasing funds
- ✓ Capital markets should not only seek to attract investments from the pension funds without worried about the profile of their liabilities.

Corporate Governance

- The role of Pension Funds in corporate governance has evolved in line with their growing importance as corporate owners
- As long as their equity holdings were small and diversified in a large number of companies, they were following a passive approach to corporate governance
- But with continuing growth in assets invested, pension funds have collectively become dominant shareholders of many corporations and can no longer easily “exit” without disrupting the market and suffer big falls in market prices.

Regulatory and Supervision

- In a number of countries, there are constraints set by the regulators which limit the exposure to equity capital markets (*national provident funds in Singapore and Malaysia*)
- Due to the regulatory constraints, these schemes have not contributed to the development of domestic securities markets.
- However, the value of trading in these stock markets exploded under the pressure of growing international interest (*less than 25% of GDP in the 1980s to over 150% in 1990s'. In Malaysia the value of trading reached nearly 250% of GDP in 1993, but fluctuated to less than 40% in 1997 given the volatile overseas interest*)
- In countries with over exposure to capital markets and no regulatory framework, it is expected that rebalances will be required if limits are imposed by regulators
- Due to the small number of pension funds in particular regional capital market, we encourage reciprocity arrangements between different capital markets to be set in place.

To date i.e. Muhanna Group has :

- Rendered services in **38** countries
- Provided services to **52** government & semi-government organizations
- Reviewed **18** Social Insurance Funds & Reviewed **97** Pension & Provident Funds
- Advised **63** life & general Insurance companies Provide services to **94** other private institutions
- The 1st and largest Actuarial Consulting Firm in the Region & the 4th largest Firm in the World in Social Insurance.
- The only Insurance Rating Services in the Region.
- The only Actuarial Education Foundation in the Region.

Bio – ibrahim muhanna, Lebanese



In 2007, he was awarded "**The National Order of the Cedar**" by the Lebanese President. The award is in recognition of his great service & devotion to the Nation.

- Ibrahim Muhanna founded i.e. Muhanna & co. (Actuarial & Consultants) in 1986; Omnilife insurance company in the UK in 1988; The Muhanna Foundation in 1994; & i.e. Muhanna & co. (Rating Services) in 2000.
- He graduated from the University of Michigan (1976) with a MSc in Actuarial Mathematics. Since 1986 he has advised 56 insurers, 25 governments, and other clients in 38 countries. He has written several papers & delivered over 550 presentations on actuarial, financial awareness, & governance issues in 60 countries. Mr. Muhanna provided instrumental advice to various governments while reforming their national social protections schemes.
- Since 1985 Mr. Muhanna has been a member of the International Actuarial Association (IAA) Council since 1992. He is also served as a member of the IAA Executive Committee and is actively involved in other IAA Committees & Sections. The founding member of the IAA Health Section and currently member of member of the board of International Association of Consulting Actuaries.
- The vice-chairman of the actuarial technical commission of the International Social Security Association (ISSA).
- The first Chairman of the Cyprus Actuarial Association, member of the Swiss Association of Actuaries and he is the President of the Lebanese Association of Actuaries.

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