Foreign Investment of Pension Funds

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Worldwide

Kotlikoff/Bodie Argument

- Global index is optimal asset allocation
- Liability considerations minor (not much in the way of asset-liability correlations)
- Total return swaps help avoid some of the country risk issues

The Ageing Argument

Domestic investment:

Invest today, receive claim on production tomorrow

Domestic PAYG:

Pay taxes today, receive claim on production tomorrow

Foreign investment:

Invest today, receive claim on foreign production tomorrow

Population Ageing

	Ratio of 60+ to People 20-59 (2000)	Growth Rate in Ratio (2000-2030, annual)	Old Age Pension/GDP in 2030
Brazil	15%	2.57%	
China	18%	3.08%	
Germany	42%	2.04%	15.5%
France	38%	1.71%	16%
India	16%	1.58%	
Japan	41%	2.18%	
Malaysia	13%	2.34%	
UK	38%	1.86%	4.3%
USA	29%	1.92%	6.2%
Switzerland	38%	2.73%	

Sources: UN Population Statistics (2000 rev.), Dang et. Al for old age pension in 2030

Limits on Pension Fund Investments

Strict

Germany
Belgium
Switzerland
Denmark
Canada
Finland
Hungary
Korea
Portugal
Sweden

Liberal

UK
USA
Netherlands
Australia

Source: OECD Survey of Investment Regulations of Pension Funds (2002)

Alternative Arguments

1. Economics of capital account liberalisation unclear - impact on exchange rate stability (Asian crisis)
2. Quantitative limit arguments – imperfect regulatory framework
3. Imperfect markets: if developed countries have limits on outward investment then potential welfare gains from responding with limits on outward investment
4. Welfare: for developing countries, prevents them from investing in ageing developed countries