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***Comments on “The Effect of the  
Financial Crisis on Pensions in Latin  
America”***

**Revision under the AIOS  
perspective and some policy  
responses undertaken in Costa Rica**

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# SUPERVISION PRINCIPLES

## - AIOS -

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- OBJECTIVE
  - Better supervision practices, a standard conceptual and normative supervision framework.
- Supervision based on risks
  - Operative Risk, Corporate Governance, Financial Risks, Political Risk (“policy backfires”)
  - Opportunity and quality of the information
  - Better benefits to contributors



# SUPERVISION PRINCIPLES

## - AIOS -

### REGULATION & SUPERVISION

- Regulation for a transparent , efficient and effective management to protect the rights of the affiliates and beneficiaries.
- The supervisor should coordinate actions to control and regulated with the other related organisms.

### PENSION ADMINISTRATORS

- Corporate Governance measures
- Integral risk management and preventive management

### INDIVIDUAL ACCOUNT & BENEFITS

- Correct and timely accrual to individual accounts
- Correct and timely granting and payment of befits to affiliates.

### INFORMACIÓN DIFUSION

- The affiliates have the right to know, at every moment, the information of their individual accounts.
- The provided information should be truthful, objective, timely, transparent and comparable.

### INVESTMENTS

- Certification obligation for those who are in charge of investments.
- Transaction should be made in authorized markets with a proved system of fiscalization, control and available public information.
- The administrator should have Corporate Governance practices in administration policies and resource management.

# RISK-BASED SUPERVISION MODEL

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- Preventive model, based on the analysis and management of risks.
  - Definition of the risks (critic to these models)
  - Definition of robust methodologies to measure the risks
    - Backtesting
  - Simulations
  - Policies for the administration of the risks : important to know what we face
  - Do not forget about the operative risk



# RISK-BASED SUPERVISION MODEL

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- Promotion among the supervised to adopt better practices for the integral administration of risks.
  - Risk maps to direct the supervision endeavors.
  - Establishment of criteria to apply precautionary measures.
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# DISCUSSIONS ON RISKS

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- Indicators of risks in times of crisis

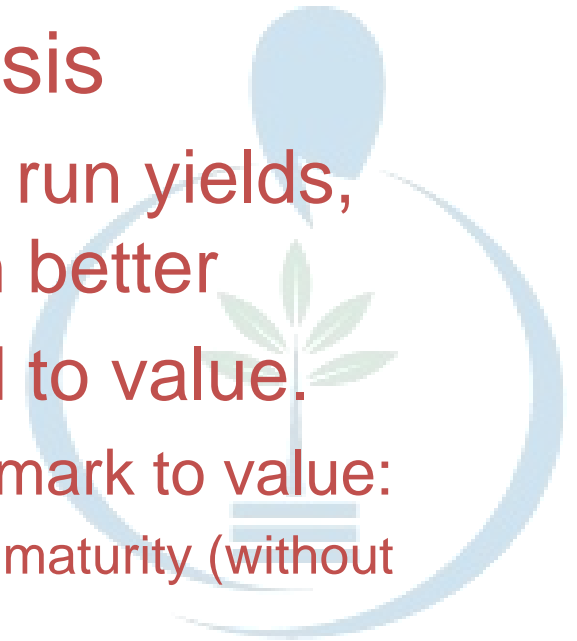
- ¿Does the regulator and the regulated have a clear idea of the relevant risks?
- Regulation on risks is very general
- ¿Should we use VaR to measure the market risk of pensions fund investments?
  - Pensions are for the long haul
  - VaR is an indication for the short run
    - ¿How to integrate these two aspects? ¿Should administrators redo their positions based on the short-run indicator?
    - ¿Should I cover my currency positions?
      - » These reduce short-run problems but do not necessarily optimize the portfolio in the long haul



# DISCUSSIONS ON RISKS

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- Risk indicators in a time of crisis
  - Continues information on short run yields, when the historic information in better
  - The portfolio should be marked to value.
    - There are pressures to abandon mark to value:
      - Leave a portion of the portfolio until maturity (without mark to market)
      - Do not mark to market during times of crisis.



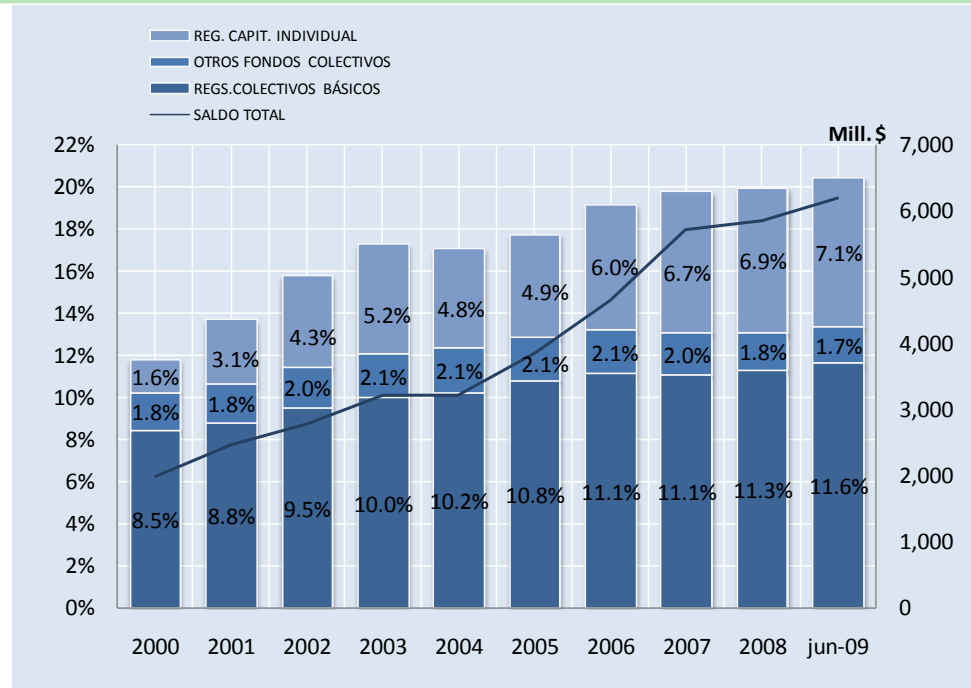
# ¿WHAT HAPPENS IN THE BENEFITS STAGE?

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- Amount of the periodic rent
  - Variable
  - It adjusts automatically (tied to an index)
  - It postpones the retirement point
  - Lifetime rents become more expensive for the retiree
- Search for other alternatives for the retiree, who lives with that pension.



# CRISIS EFFECTS ON COSTA RICA

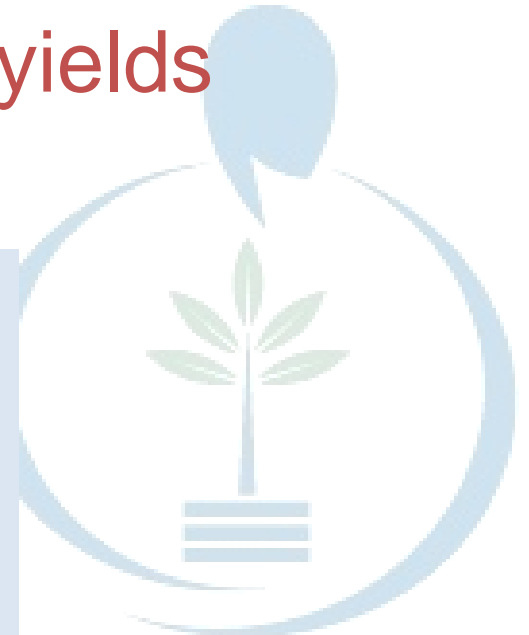
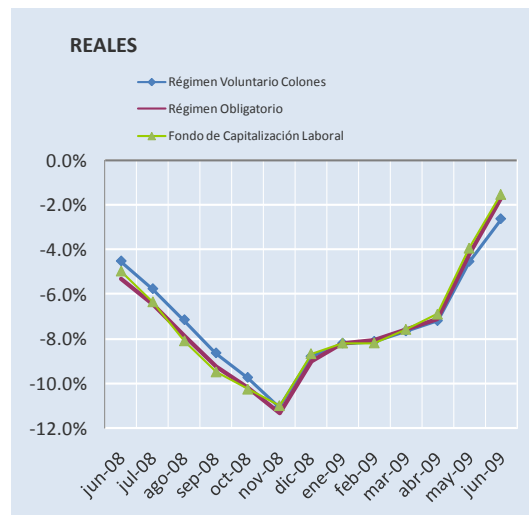
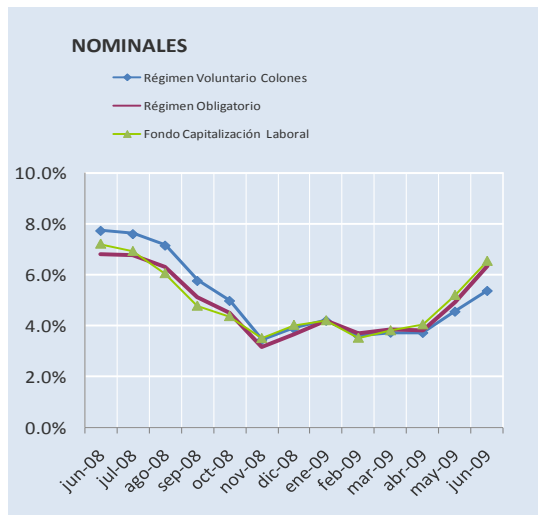


## LOWER INCREASE IN ADMINISTERED BALANCE

1. EFFECT ON CONTRIBUTIONS
2. EFFECT ON NEGATIVE YIELDS

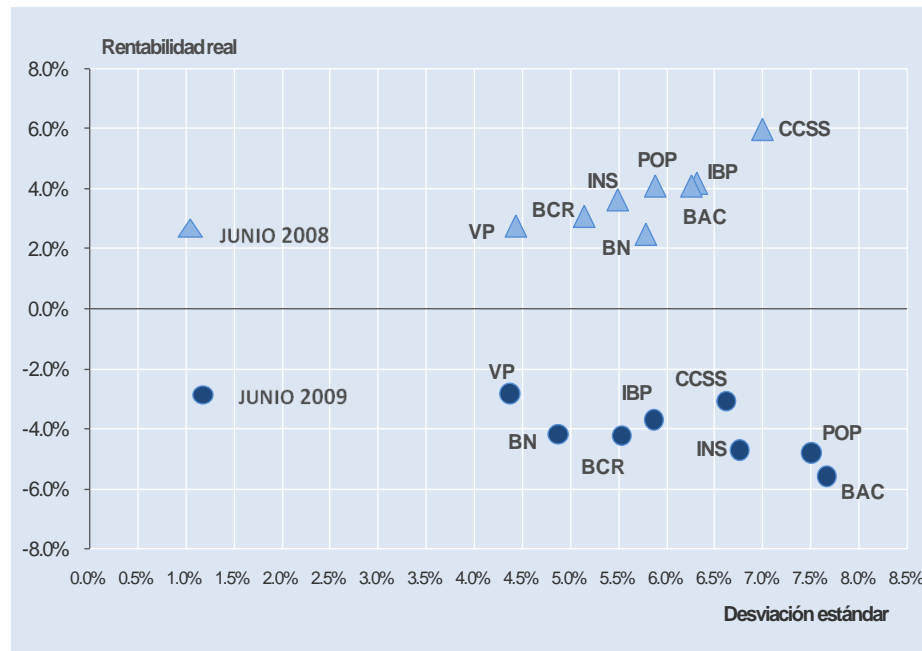
# CRISIS EFFECTS ON COSTA RICA

- Reduction in nominal and real yields



# CRISIS EFFECTS ON COSTA RICA

Administrators with lower real yield levels but risk did not decreased



# REGULATORY CHANGES

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- Performed

- Flexibility of the investment limits in Public Sector investments.
- Flexibility of concentration by issuer
- Patrimony Sufficiency of the administrators
  - Operative Risk Rating by administrator
    - Base Capital
      - » Market, Credit and Operative Risks
      - » Based Capital in function of the rating of Operative Risk
- Corporate Governance regulations.



# REGULATORY AGENDA

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- Review of the investment limit model
- Review of the indicators to measure market risk
  - Correlation Coefficients
  - Methodologies to adjust the yield levels
- New Benefits Regulation

