



Pensions and the current crisis

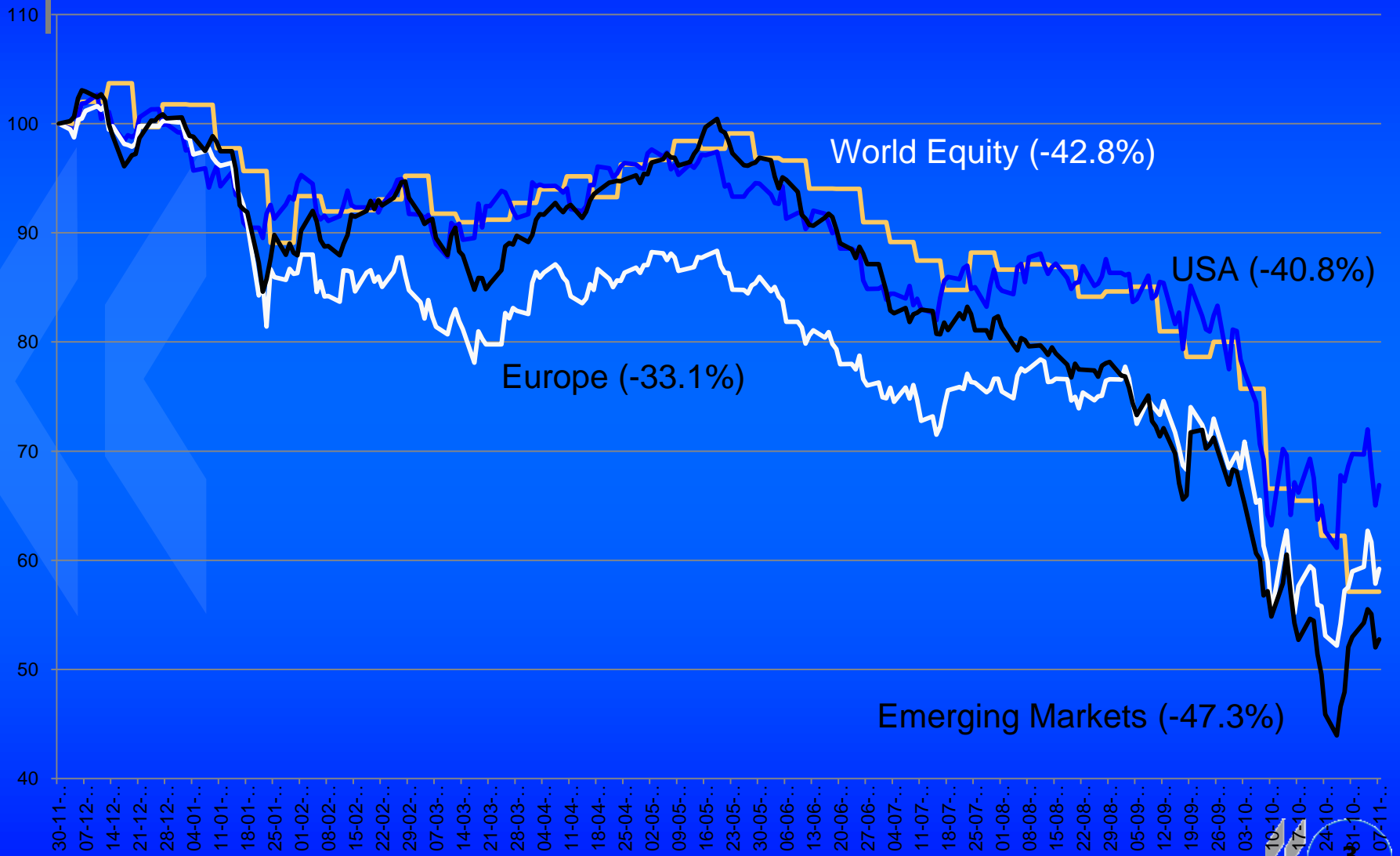
OECD Seminar on the payout phase, annuities and
financial markets

Paris, 12 November, 2008

Impact of crisis on private pension systems

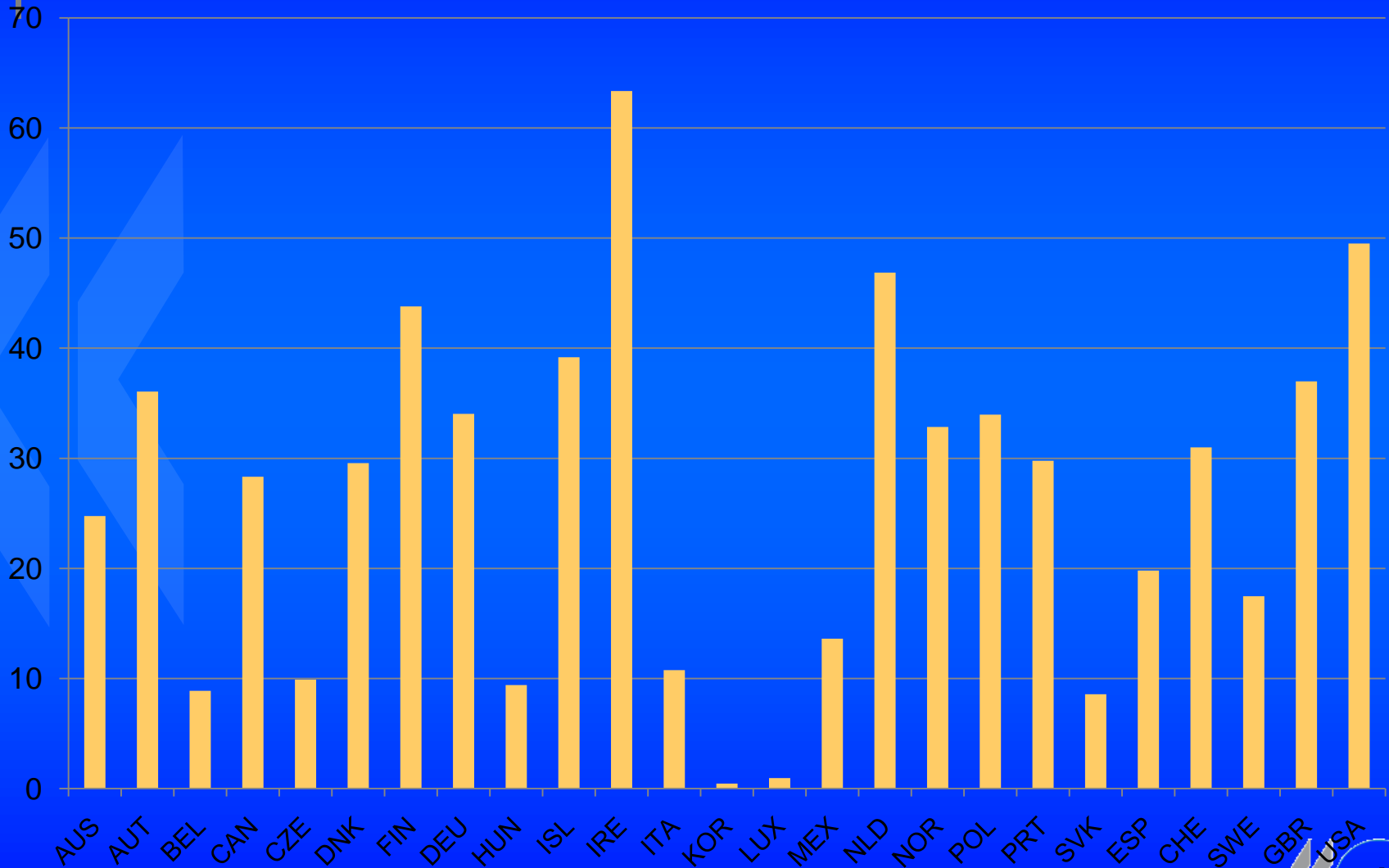
- Average OECD pension fund return -25% btw January-October 2008 (over USD 4 trillion).
- DC directly hit, worst for those close to retirement.
- Some DC default options at point of retirement >60% in equities.
- DB funding levels declined by about 5-20pp, depending on discount rate used
- “Toxic” assets estimated at less than 3% overall

Major Stock Market Indices (30Nov07=100)

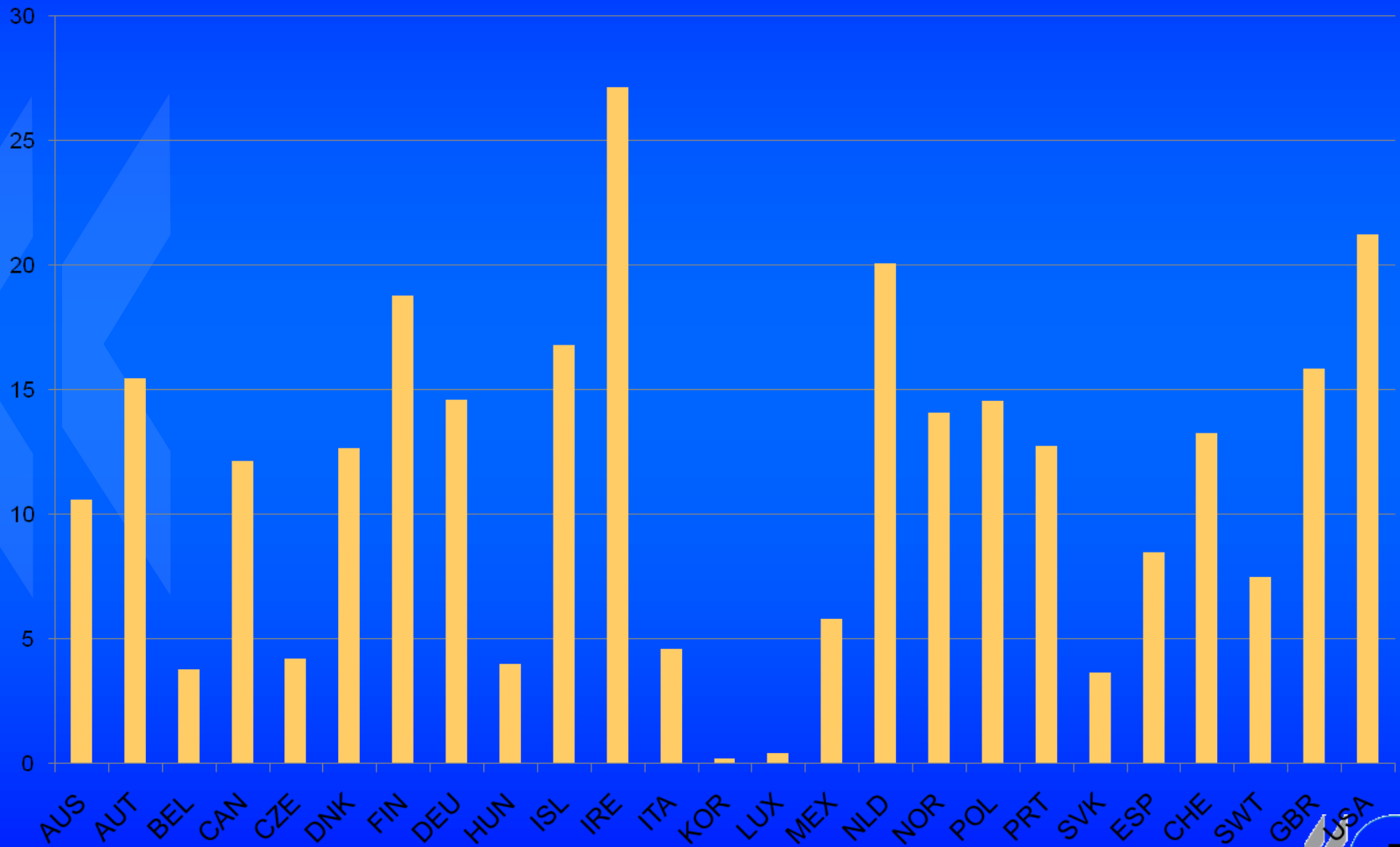


Portfolio allocation in equities

(% total assets, 2006)



Prospective losses of pension funds across OECD countries



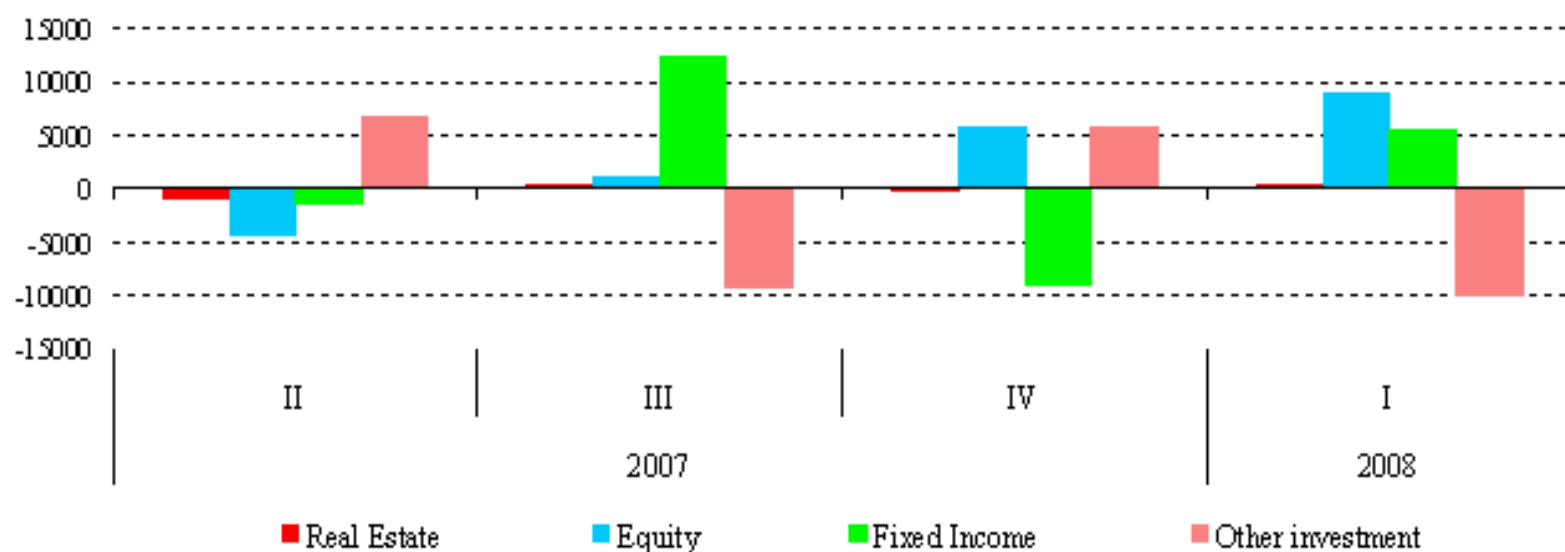
Reactions to the crisis

- Where fair value and quantitative risk-based solvency rules in place, pension funds selling equities
- Concerns over counter-party risk, pension funds shunning derivatives and swaps for risk management purposes
- Move into alternatives continues
- Private pension backlash (e.g. Argentina)

Pension funds still acting as automatic stabilisers

**Figure S.2. Dutch pension funds: Net purchase for different investment categories
EUR million**

Graph b: Dutch pension funds: Net purchase for different investment categories
EUR million

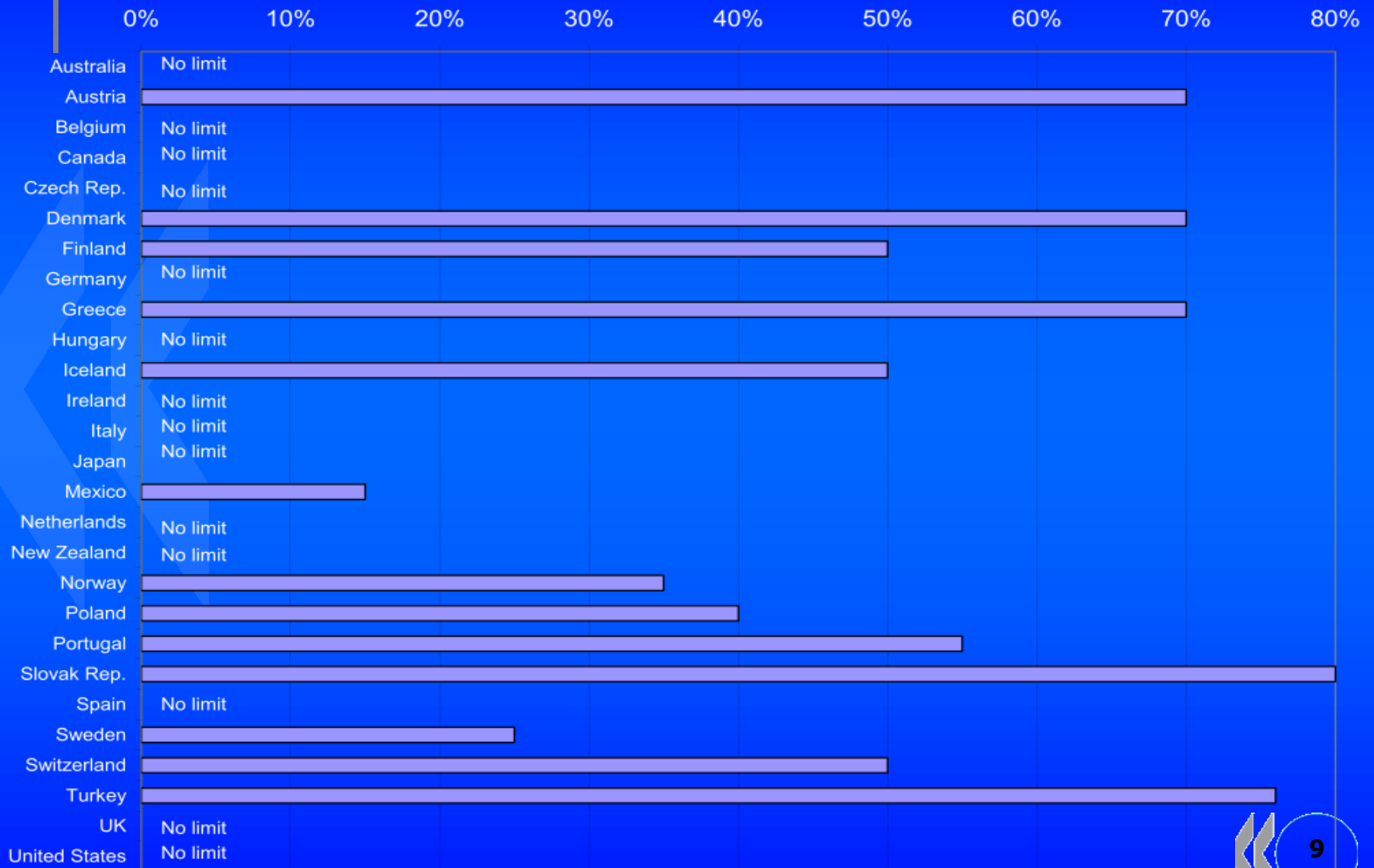


Source: DNB

Investment regulation trends in OECD countries

- Gradual relaxation of quantitative investment limits
- Implementation of prudent person standard
- Quantitative risk measures (e.g. VaR, stress tests) starting to be used in both DB and DC systems.

Limits on shares



Limits on foreign investment



Lessons from the current crisis

- Pensions are for the long-term, but short-term crisis can have damaging impact of pension funds and retirement income.
- Funding rules:
 - in the short-term introduce measures to ease them (e.g. extend recovery periods for underfunding)
 - in general, make funding requirements counter-cyclical.

Lessons from the current crisis

- Balance btw prudent person and quantitative restriction regulations.
- When DC main source of retirement income, more stringent regulation; when other sources of income, more flexibility.

Lessons from the current crisis

- Adequacy of retirement income: workers close to retirement (DC plans) face the prospect of drawing retirement income from smaller saving pot at the time of low asset values.
 - Provide default investment strategies that involve switching to less risky assets as people ages (e.g. life-styling or target date funds).
 - Extent of switch to bonds in default option should be greatest when annuities mandatory at retirement.
 - Consider deferred annuities that start paying at very old-ages as defaults.

Lessons from the current crisis

- Pension funds and annuity providers need financial instruments to hedge their risks (interest rate, inflation, longevity)
- However, they need instruments that avoid bringing in other risks such as counter-party risk.