

ANNOUNCEMENT

FIAP President Guillermo Arthur on the features and prospects for the development of the Chilean pension system

As part of the first panel session of the high-level international round table “Mandatory Funded and Mixed Pension Schemes Development Prospects”, which took place on September 28, 2023, on the topic “Population aging and pension reform”, moderated by Grigory Marchenko, the President of the International Federation of Pension Fund Administrators (FIAP) Guillermo Arthur (Santiago, Chile) Spoke.

The topic of his report: “The pension system of Chile: results, challenges, prospects for further development.”

In it, he emphasized that the Chilean pension system model served as the basis for reforms carried out in many countries, including Kazakhstan.

The speaker highlighted the main characteristics of the Chilean pension system, here are some of them:

- Mandatory pension contributions are capitalized on individual accounts belonging to the employee for whom they were received
- These savings are managed by public limited liability companies (AFPs), which have separate assets and are strictly controlled by a government agency
- Pension assets are invested in local and foreign instruments in order to generate profit
- Investment limits and other conditions are established by the rules, which ensures adequate diversification, investment return and safety of pension assets
- Employees can choose a management company from 5 types of funds, differing in the degree of risk exposure
- Pensions are funded by employee contributions and investment returns
- Chile's pension system is mixed, since part of the pensions, aimed at the most vulnerable segments of the population, is financed by the state (taxes).

The Chilean pension reform was carried out due to the unsustainability of the previous defined benefit system, in which fewer active workers had to provide pension benefits to a growing mass of retirees. The fragility of PAYG systems is demonstrated by the following facts over the past 27.5 years (from 1995 to June 2023): 82 countries increased their contribution rate; 66 - the retirement age was increased; 66 - frozen or reduced the amount of benefits provided.

Over the past decades, the number of countries with pay-as-you-go systems and at the same time introducing individual savings mechanisms in various forms has increased from 17 in 1999 to 51 in 2022.

Speaking about the results, Guillermo Arthur noted that over the 40 years of operation of the funded pension system, the investment return on pension funds averaged 7.2% per year, which means that the funds accumulated by the first generations of workers increased fourfold. In other Latin American countries where the Chilean system was used, return was similar to the Chilean one.

Highlighting the prospects for the development of the pension system, the speaker noted that, taking into account the factor of increasing life expectancy in the world along with the development of new forms of work of the population (self-employment, remote format), for the successful functioning of the pension system it is necessary to take the following steps:

1. Increase the contribution rate and retirement age. The 10% contribution rate has been in place for 40 years, although life expectancy has risen by 55% for men and 48% for women over the same period
2. Look for alternative mechanisms for financing pensions
3. Encourage voluntary pension savings in addition to mandatory savings.

Summarizing his report, Guillermo Arthur noted that to achieve the success of pension reform, the following factors must be taken into account:

- Distribution systems are not sustainable for demographic reasons, while funded systems contribute to the financing of pensions not only through employee contributions, but also through investment income, and also make a significant contribution to the economic development of the country

- Pension resources must be managed in a competitive environment that encourages profitability and cost reduction

- Sources of funding for pensions should be diverse and involve several levels:

- the first pillar, financed by taxes and aimed at socially vulnerable segments of the population
- second pillar, providing for mandatory pension contributions, the rates of which are automatically revised depending on life expectancy

- the third pillar, including voluntary pension contributions that complement mandatory contributions. In this case, it is advisable to use mechanisms based on behavioral economics, such as automatic enrollment. This means that employees are automatically registered upon employment to make voluntary pension contributions into their individual account, which can be supplemented by employer resources. Employees may waive this responsibility if they wish. In practice, in countries where automatic enrollment of voluntary contributions has been introduced, attrition rates are relatively low. For example, in the case of the most developed automatic recruitment system in the United Kingdom, from 86% to 92% of workers remain in the system, from 8% to 14% abandon it.

- Investment activities in relation to pension assets should have a single goal - obtaining adequate profits and ensuring their safety, which requires competent diversification of investments by instrument class, issuer and geographic region.

The UAPF was established on August 22, 2013 on the basis of GNPF APF JSC. The UAPF founder and shareholder is the Government of the Republic of Kazakhstan represented by the State Institution "Committee of State Property and Privatization" of the Ministry of Finance of the Republic of Kazakhstan. UAPF pension assets are managed by the National Bank of the Republic of Kazakhstan. From January 1, 2016, the functions for developing proposals to improve the management of pension assets were transferred to the National Fund Management Council. In accordance with the pension legislation, the UAPF attracts compulsory pension contributions, compulsory occupational pension contributions, voluntary pension contributions, pension benefits, individual accounting of pension accumulations and benefits, provides the contributor (beneficiary) with information on the status of his pension accumulations (for more information visit www.enpf.kz)