



SEMINARIO FIAP

- FIAP Seminar 2005-

2005

# PensionNews

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## Welcome to the FIAP Seminar 2005

# The part of each pillar in the Foresight System

The International Federation of Administrators of Retirement Funds, FIAP, Asofondos-Colombia and de publishing Committee of PensionNews welcome you at the Seminar 2005, with the initial objective of defining the part of each pillar in the solution of the problem of pensions. This event is the result of having reached the objective of FIAP of steadily improving the foresight system and the quality of life of people who reached the age of retirement.

For this issue, Guillermo Arthur, president of FIAP, spoke with PensionNews about the Seminar and its impressions regarding the foresight systems.

### What are the perspectives of the FIAP Seminar 2005?

This seminar is strongly focused on the definition of the part of each one of the three pillars in the foresight system. We, the administrators, are the second pillar. We mainly collect the formal workers' savings, we invest them, we obtain a good yield and we offer good pensions.

FIAP basically gathers the countries which reformed their foresight systems of individual savings capitalization and the private administration of said funds. There are among our countries numerous foresight problems and the main one is coverage.

Nevertheless, the coverage levels never depended on the type of foresight system, but on the characteristics of the labor market,

employment, the levels of employment, formality and informality, etc.

In Latin America, a group remains out because they are unemployed or persons with a level of great poverty. For them the first pillar, the public, the non-contributive, which must attend the necessities of said persons, must be redefined and strengthened.

**Between December, 2003, and December, 2004, the number of workers affiliated to the Administrators of Foresight Retirement Funds increased by 5.6%. According to your opinion, what did cause such increase?**

It is simply due to the fact that people, who do not feel concerned at the beginning with their retirement system, acquire a better savings discipline when they observe that a good yield is being obtained, their capital is growing and they will consequently be able to get a good pension.

**What does FIAP plan to do this year, so that said increase does not stop?**

We are permanently organizing seminars and issuing publications to demonstrate the strong points of this system. But together with the strength, we face challenges which may become problems if the other two pillars don't work well. For this reason we are concentrated on this point. We are also analyzing another theme. There are countries where investments are mainly captured by the public sector, because that

people are interested in obtaining those funds for their own profit. But we must never forget that those funds belong to the workers, and for this

reason the workers must insist to obtain that said funds be invested according to criteria of rationality, yield and security.

**What are the stones on the path toward the improvement of the pillars of the Administrators of Retirement Funds?**

Coverage, informality, employment, these prevent our system to reach more people.

**What main challenges must be faced by the retirement industry throughout the world within the next five years?**

To go ahead improving. Numerous countries have very deficient investment politics because the authorities did not allow them to diversify the instruments in which they may invest and hold them very concentrated in the State commodities. The challenge is to obtain a good diversification with investments abroad and create alternatives to be offered to the workers.

FN

BY YARA BAYUELO WATTS  
PENSIONNEWS



Guillermo Arthur  
President of FIAP

### SUMMARY

#### PROGRAM OF THE DAY:

**08:00-08:30**

The second pillar: Programs of Contribution.

**08:30-9:00**

Welcome speech.

**09:00-09:30**

Reform of pensions and public finance in Colombia

**09:30-10:15**

The three - or four? - pillars of a retirement system

**10:15-10:45**

Coffee break

**10:45-13:00**

- The First Pillar: the programs of the First Pillar in L.A.

- Labor markets and provisional coverage

- How to finance the programs of the First Pillar?

- Round Table: How to improve the design of the programs of the First Pillar in L.A.?

**13:10-15:00**

Lunch

**15:00-16:30**

- The Third Pillar: Voluntary savings plans

- Voluntary Provisional Savings: The experience of L.A.

- How to stimulate Voluntary Provisional Savings?: Lessons of the Economic Theory of Behavior.

- The experience with voluntary pension plans in the USA

- How to stimulate Voluntary Provisional Savings?: The point of view of the industry.

**16:45-17:00**

Coffee break

**17:00-18:00**

- The Second Pillar: Programs of Obligatory Contribution

- Investment of the Retirement Funds: Results and reform of the regulation

- Management of Fixed Annuities of the Retirement Funds and control of the risk of volatility.

PENSIONS UP TO DATE:

# Why the number of AFORES is still growing in Mexico?

DANIEL RESÉNDIZ  
AXAN CONSULTING, PARTNER

The first administrators of retirement funds (Afores) in Mexico appeared in 1997. After the incorporation of 17 players in the first semesters of operation of the system, a predictable consolidation process occurred. From the beginning of 2002 onwards, it seems that a stable industry was being profiled with some 11 players. Nevertheless, from the end of 2002 onwards, the Mexican regulator, the Commission of the Retirement Savings System (CONSAR), authorized five new players, and at least other two are in process of authorization. The number of players in the industry might thus be increased by more than 60% in less than four years.

What did see the businessmen who are investing their capital in these new administrators? First of all, they doubtlessly discovered, without getting discouraged, the strong concentration in the market parts of the administrators of the big financing corporation in Mexico (we can point out that there is a regulatory limit of 18% of maximum participation). The two bigger administrators, one property of Citigroup (Banamex) and the other of BBVA (Bancomer) concentrate 30% of the workers affiliated to the system and almost 42% of the resources under administration, according to data of the CONSAR as of December, 2004. Meanwhile, the enterprisers saw doubtlessly positive signals for the players who aspire to join the industry and demonstrate that, without that the scale of the administrators be determinant, between 2001 and 2004, the nominal returns on the capital invested by shareholders in the

administrators have been very high, with a nominal average in the whole system of 33.3% and having every year Afores with returns on the capital above 50% (See Graphic 1). To put said returns in perspective, it is enough to say that the annual inflation during the same period only reached an average of 4.8%.

Why so high returns can be generated in the administration of the retirement funds in Mexico? First of all, there is a very wide "umbrella of prices" (see Graphic 2) which allows even the less efficient players to generate a positive operating income.

To this phenomenon must be summed up another, the "recurrent assignments", produced by the regulator's preoccupation of creating incentives in order to reduce the commissions collected by the administrators from the workers participating in the system for administrating their money. Every trimester, the workers discharged by the labor force during the previous period and who did not choose an Afore (most of them) are "assigned" by CONSAR, electronically and free of charge for the participating administrators, to the Afores in the lowest quarter of the equivalent commissions table (almost 1.5 million workers were assigned in 2004).

These "recurrent assignments" enabled the new administrators to reach the operative point of equilibrium within a few months (See Graphic 3). Most clients of various Afores are due to those electronic dispersions. For example, the workers assigned to five of the Afores of major relative participation in the scheme explain between 55% and 98% of the total number of clients of the administrators as of December, 2004,

according to CONSAR data.

What does the future offer to this series of new administrators? This is doubtlessly a question more difficult to answer. It remains clear that no administrator will survive with assigned clients for various important reasons: their low income, their low initial balance and their low probability of keeping active like regularly contributing workers. Moreover, it remains clear that the regulation changes promoted by CONSAR began to activate the transfers between administrators. In a branch where the administrators, as a whole, made few efforts to "educate" the workers about the advantages of an Afore compared with other systems, it is possible to induce transfers with a certain level of effort to improve the service and communication with the clients, an aspect that is very clear to almost all the new players and that they are taking advantage of to induce transfers. It is also possible to compete through commissions, not only because of the wide umbrella of prices already mentioned, but because it results expensive for the leaders of the market to lower their commissions on their enormous base of present clients, which induced most of them, in a way which seems more economical than rational on the short term, to let the new players do without even trying to follow them on the way of reducing commissions. The new players, and the industry as a whole, are also meeting attractive growth opportunities, even if all of them include a high risk of regulatory uncertainty and political viability (various of the opportunities require the approbation of the Congress to be materialized).

...the enterprisers saw doubtlessly positive signals for the players who aspire to join the industry...

The main opportunities of this type are concerned with the possibility of widening the coverage to reach the greater possible number of the 44 millions of Mexicans who constitute the present economically active population. The present coverage of the System of Savings for Retirement (SAR) is of 12 millions active and 21 inactive workers, including possible duplications (evaluated between 4 and 6 millions). There are three big groups of workers who don't participate for the time being, or participate in a very incipient way, in the SAR: those of the federal, state and para-state public sector (almost 4 millions workers); and the independent and informal (who fluctuate between 10 and 25 millions, according to economical circles, who enter the formal labor force and go out of it). Various of the newcomers in the system are betting that they will take a significant part of those new segments through new products and services; voluntary savings for independent and informal workers, registry and investment of other funds of social foresight of the Mexican employers, etc.

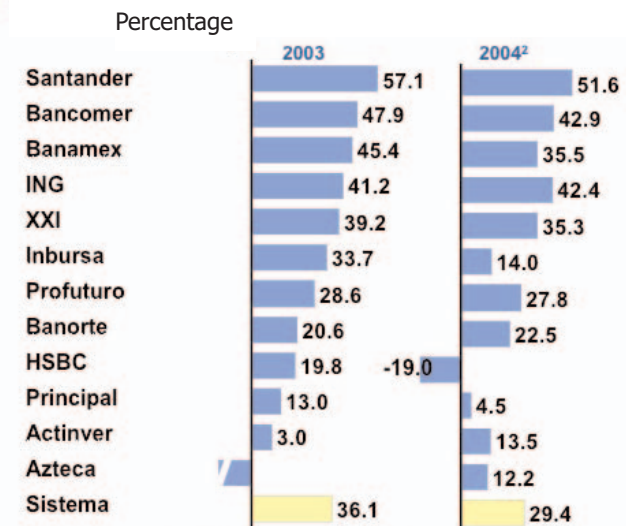
Finally, the number of administrators in Mexico is very likely to go on growing during the next months. After that, another period of consolidation will doubtlessly come. If this febrile dynamic finally results, as it is presently to expect, in favor of the Mexican workers (more competition, better service, better yields of their funds and, finally, better pensions), it will have been profitable for the industry, for its various actors and for the country in general.

**Axan** is an enterprise of professional services with an offer of assessment and investment. In the sector of the Afores in Mexico, Axan has assessed two of the newest administrators in the preparation of their business plans for their authorization steps, moreover, it is presently assessing other two possible new players.

## Graphic 1

Return on shareholders' capital in the afores.

Annual nominal average yield of the capital of the AFORES.



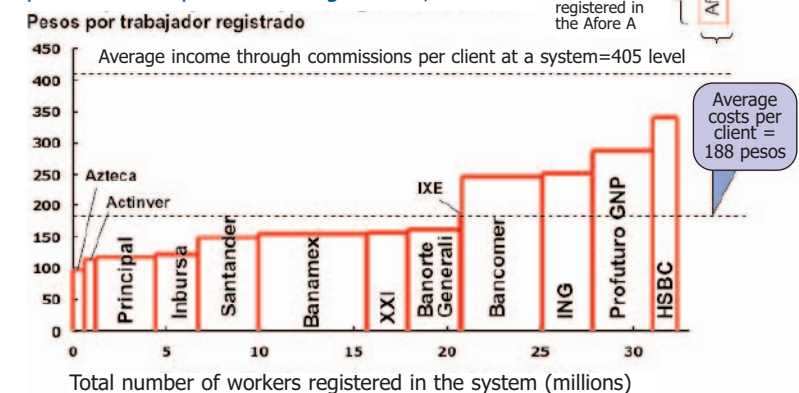
Calculated as net profit divided by average capital of the year.

IXE, which initiated operations on June 30, 2004, is no being taken in consideration. Source CONSAR; analyze AXAN.

## Graphic 2

"Umbrella of prices"

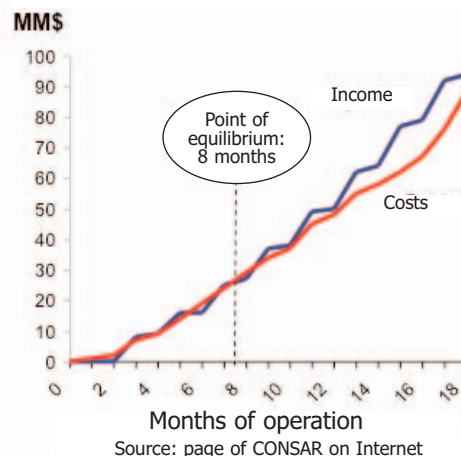
Operative costs per worker registered\*, 2004



## Graphic 3

Point of equilibrium of new Afores: the case of Actinver

Income through commissions and operation, administration and promotion costs – accumulated.







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## Amplifying the social protection of the retirement systems: The social assistance and non-contributive benefits

FABIO M. BERTRANOU. Specialist in Social Security. International Labour Organization. [bertranou@ilo.org](mailto:bertranou@ilo.org)

One of the main challenges of the pensions systems in Latin America consists of the amplification of their coverage. In some countries very few workers are qualified for old-age pensions or have sufficient savings to face the risk of the loss of income when retiring from the labor market as major adults.

In the field of pensions, the reform paradigm during recent years in the region has been the proposal of establishing multi-pillar systems. The reform have reorganized the schemes to grant different types of benefits combining defined benefits with financing schemes based on defined contributions. The main accent of the public politics have been on the reform the so-called second pillar which aims at the objectives of insurance and softening of consumption through savings. Nevertheless,

the first pillar, in its possible contributive as well as non-contributive components, drew less attention. The experience in some countries of the region, such as Chile, Costa Rica and Brazil, shows that the first pillar has been an important tool to amplify the coverage and improve the comfort of the most vulnerable and socially excluded sectors of the population.

In this way, the strategies of amplification of coverage might aim at an expansion of the second pillar as well as of the first. In the case of the second pillar, an expansion of the present systems should be looked for, incorporating workers with a minimum contributive capacity who are not presently reached by the systems. In the case of the first pillar, those persons of low contributive capacity, or with no capacity at all, might be included through subsidiary schemes or "semi-contributive" alternatives.

The experience of the ILO in analyze of the non-contributive systems in Latin America

shows that said systems have been efficient not only to close the coverage breach, but also due to their important impact on the reduction of poverty and indigence in the old age. The non-contributive schemes, including the ones with character of social assistance, enabled to reduce the social exclusion, specially of some groups of vulnerable workers, such as those of the agricultural sector.

The design of the non-contributive schemes must be congruent with the characteristics of the contributive component of the retirement system, so as to build up a true system of social protection for the old age. There are key aspects to be defined, which consist of the mechanism of election of the beneficiaries, the level of the subsidies and their entail with the second pillar. The latest will enable to minimize the possible distortions in the incentives to be contributed to said pillar.

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