

Multi-funds: Four Years of a Reform that has been Successful for Members

- * **The good yields in these years have made it possible to increase each member's savings by an average of \$2.6 million.**
- * **People who have chosen higher-risk Funds A and B are under 40 years of age.**
- * **The balance of Fund A for the first nine months closed with a yield of UF + 10.03%, but it faced a high level of volatility in this period with yields of UF + 7.22% and -3.94% in real terms.**
- * **In these four years, investment in Mortgage-backed Securities, Government Securities and Foreign Fixed Income has seen a sharp decline.**

The creation of the multi-funds is undoubtedly one of the most important reforms undergone by the saving and capitalization pension system in its 25 years of existence. After four years in operation, it has been possible to increase the yield on savings substantially, bring members closer to the system and diversify investments.

As from September 2002, savings began to be invested in five types of Fund, in accordance with the decision of the members themselves, who chose between options that were differentiated by the proportion of equity instruments allowed in each portfolio. Those who did not choose were allocated by age, with 50% of their savings being transferred immediately to the fund that corresponded to them and the other half 12 months later.

Table N° 1 shows that those who opted at the beginning for A-type funds, which invest between 40% (minimum) and 80% (maximum) in equities, practically doubled their capital in four years, while those who chose the B-type funds increased their accumulated capital by two-thirds. Those who chose C-type funds increased their savings by 50%.

Table N° 1
Profit Obtained by the Multi-funds in 48 months

	Sept.02 - Sept.06 Acum. Rent. (Nominal)	Starting Capital Sept.02	Profit Obtained 48 months	Final Amount Sept. 06
A	97.97%	\$ 1,000,000	\$ 979,700	\$ 1,979,700
B	66.46%	\$ 1,000,000	\$ 664,600	\$ 1,664,600
C	50.31%	\$ 1,000,000	\$ 503,100	\$ 1,503,100
D	40.37%	\$ 1,000,000	\$ 403,700	\$ 1,403,700
E	27.18%	\$ 1,000,000	\$ 271,800	\$ 1,271,800

Note: This example gives a simple illustration of the effect of yield on an amount of savings.

In Table N° 1, the nominal yield of the period is applied to the starting capital, reflecting the increase or profit in pesos, without adjustment for inflation.

Table N°2
Real Yield of the Multi-funds*

FUNDS	Jan.06- Sept.06 (year)	Sept.02- Sept.06 (Annualised)	Sept.02-Sept.06 (Accumulated)
A	10.03%	15.27%	76.94%
B	8.29%	10.40%	48.78%
C	7.18%	7.63%	34.34%
D	5.54%	5.81%	25.46%
E	4.44%	3.24%	13.67%

*Deflated by the UF variation

92% of the people in funds A and B are under 40 years of age

Yield is a key aspect of pensions systems based on savings and capitalization. One percentage point of increased profit per year can raise the amount of the pension by between 25% and 30% after 30 or 40 years. Because of the importance of this characteristic, the Multi-funds have not been the only tool used to increase yield in the course of these 25 years. There have been other reforms in the same direction, such as those authorizing investment in shares and investment abroad.

From the time the Multi-funds came into force until September 2006, AFP investment has achieved extraordinarily positive accumulated results for the period, ranging from UF + 76.94% for A-type funds to UF + 13.67% for E-type funds (see Table N° 2).

The profits obtained in these four years have brought members an average of \$2.6 million compared with their starting savings, adding up to a total of US\$33,480 million. The pension fund today amounts to US\$80,500 million, as a result of new members, contributions during the period and yield.

Members Choose

The second effect of the Multi-funds has been the awakening of an increased awareness of the need to be concerned about saving for a future pension, with members feeling more involved with their pension savings account. This has led to an increase in pension culture.

Currently over 2 million 400 thousand members have chosen one fund or more, in which to invest their pension savings. Most have chosen fund B, followed by funds A and C (see Table N° 3).

In the past twelve months, there have been two notable changes: more members are actively choosing funds (+ 18%) and there is a noticeable migration from the more conservative funds (Types D and E) to the A and B-type funds that have a higher percentage of their investment in equities (see Table N° 3).

92% of the people in funds A and B are under 40 years of age, which means they have a long time horizon before retiring at the legal age. This time-axis for contributions minimizes the effects of possible low or negative yields, with positive results (See Table N° 4).

Yield and Risk

The AFPs make a great effort and compete to obtain the best yields for their members. The results show that the performance has been successful. However, past yield is not the only variable to be borne in mind when considering the choice of funds, because the good results are not necessarily going to be repeated in the future. There is no such thing as risk-free investment. The results depend on stock and financial markets, which are in turn affected by multiple macro and microeconomic factors, geopolitical factors, etc.

Table N°3

Number of Members who have Chosen a Fund
(Number of accounts in existence of members who have chosen funds)

Fondos	August 2006		August 2005		Variation 2006 - 2005	
	Number	%	Number	%	Number	%
A	765,830	32%	529,717	26%	236,113	45%
B	926,003	38%	777,133	38%	148,870	19%
C	597,630	25%	588,139	29%	9,491	2%
D	80,218	3%	87,438	4%	-7,220	-8%
E	60,360	2%	69,432	3%	-9,072	-13%
Total	2,430,041	100%	2,051,859	100%	378,182	18%

Source: Monthly Statistics of Members and Contributors (SAFP)

Table N°4

Number of Members in Funds A and B
by age on 30th June 2006

Age	Number	%
<= 40	3,752,802	92%
40-45	135,167	3%
45-50	95,674	2%
50-55	59,678	1%
55-60	26,163	1%
60-65	5,626	0%
65-70	606	0%
> 70	274	0%
S/I	5	0%
Total A - B	4,075,995	100%

Source: Quarterly Statistics of Members and Contributors (SAFP)

**In 48 months of operation:
A-Type Funds show a range of variation between maximum
and minimum yields of almost 12 percentage points**

As a result, in order to choose funds, it is necessary to take the age of the person into account, as also the amount of savings accumulated, the degree of risk tolerance to low or negative yields and the importance of the future pension in all the resources the person has available for his/her old age.

Figure N° 1 shows the returns of the A-type funds in the first nine months of 2006, the period in which the greatest variations in yield occurred since the Multi-funds began. At the extremes it is possible to see lows of up to –3.94% in real terms and profits of UF + 7.22%. People's ability to tolerate and understand that yield is subject to variations is extremely important when choosing a type of fund. The chart also shows how mistaken it may be to try and beat the market by changing funds as a result of short-term variations.

In the 48 months of Multi-fund operations, all funds have presented positive and negative yields. A-type funds show a range of almost 12 percentage points between the maximum and minimum. Funds with 100% fixed income – the E-type funds – show variations of 4.64 points between maximum and minimum. This reflects the degrees of risk in the different types of fund.

E-type funds, even though they invest only in fixed income, have had 14 months of negative yield in the period, due to the upward movement of market interest rates, which are in a process of monetary standardization. At the other extreme, the funds with most intensive investment in equities showed negative yields in 13 months, even as much as –4.28% in one month (see Tables 5 and 6).

Figure N° 1

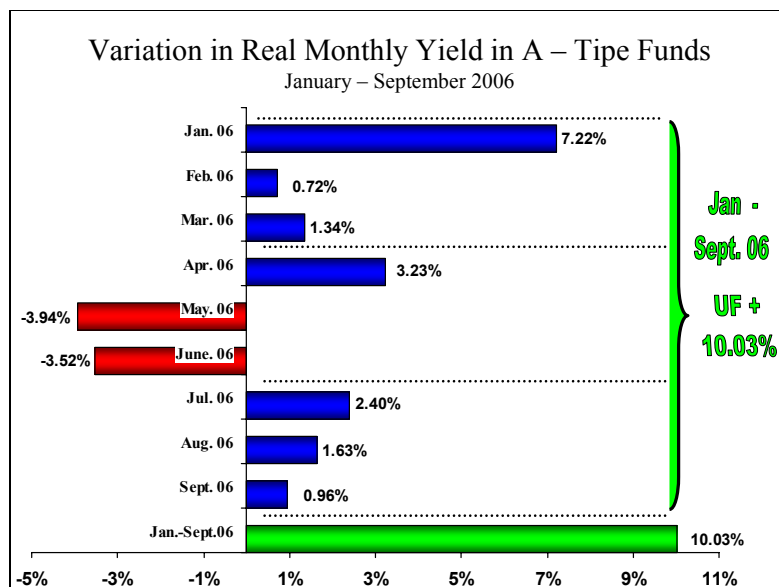


Table N° 5

**Number of Months with Positive and Negative Real Yields
(October 2002 – September 2006)**

FUNDS	N° Months Negative Y.	N° Months Positive Y.	Total Period
A	13	35	48
B	12	36	48
C	12	36	48
D	10	38	48
E	14	34	48

Table N° 6

**Real Monthly Maximum and Minimum Yields
(October 2002 – September 2006)**

	Maximum Yield		Minimum Yield	
	Date	%	Date	%
A	January 2006	7.22%	October 2005	- 4.28%
B	January 2006	5.46%	October 2005	- 3.72%
C	January 2006	4.25%	October 2005	- 3.21%
D	January 2006	2.90%	October 2005	- 2.85%
E	January 2006	1.83%	October 2005	- 2.81%

In 48 months the real accumulated yield of the A-type funds amounts to 76.94% and that of the E-type funds to 13.67%.

Table N° 7

Good Stock-Market Results in 2006

The balance of the first nine months of 2006 shows very good results, due to the fact that local and foreign stock markets recovered the losses of the second quarter in the third. This year has been very volatile both in rates and in stock markets. Due to the uncertainty generated by factors such as: inflationary pressures in the USA; rises and falls in oil prices; geopolitical conflicts in Asia and the Middle East; election periods in certain regions; concern about levels of growth in certain influential economies.

In September, the main local share index, IPSA, registered a rise of 16.1%, boosted by the positive results of companies, mainly in the electricity, retail and banking sectors. In the same way, the overseas sector contributed with high international commodity prices (mainly copper, molybdenum and others).

The balance in the USA showed a rise in the Dow Jones of 8.97% and in S&P of 7.0%. These figures represent the best third quarter for nine years. The latest figures for the progress of the North American economy and the peaceful signals given out by the FED contributed to these results.

The high growth rate visible in the world economy gave a boost to the European stock markets, especially the Madrid stock exchange which recorded a rise of 20.5% in the third quarter of 2006. Paris followed with 11.3% and Frankfurt with 11%.

Most of the emerging markets, for their part, also showed positive returns. Mexbol of Mexico rose 23.2%, Brazilian Bovespa recorded a return of

Change in Pension Fund Investments with Multi-funds

Investments	MM US\$ September 2006			Variación %	
	Aug-02	Dec-05	Sep-06	Aug.02/Sept.06	Dec.05/Sept.06
Government Securities	17,227	12,090	11,788	-32%	-4%
Local Shares	5,031	10,834	12,227	121%	3%
Inv. Fund and FICE share units	1,148	1,891	2,723	126%	37%
Bonds and commercial paper	3,432	4,968	5,824	56%	8%
Mortgage-backed securities	6,288	3,643	3,750	-42%	1%
Banks deposits and bonds	11,044	16,955	19,059	74%	13%
Forwards	-76	743	6,27		
Foreign	8,069	22,373	25,164	200%	8%
- Foreign equities	5,993	21,718	24,936	297%	10%
- Fixed income and other	2,076	655	228	-81%	-39%
TOTAL	52,163	73,497	80,542	49%	5%

8.95%, the Argentine stock exchange rose 6.1%, while Peru, with the greatest increase of the emerging markets, registered 116.4%.

Composition of the Pension Funds

In these four years, a change has occurred in the composition of the investment portfolio. Fixed income instruments have fallen from 76.8% of the portfolio in August 2002 to 50.5% at the present time.

The search for more profitable investments and the fall in availability of long-term debt instruments in the local market have been reflected in a lower share of government papers (-32%), mortgage-backed securities (-42%) and foreign fixed-income instruments (-81%). (See Table N° 7)

In August 2002, the Pension Funds had investments in equities worth US\$12,172 million, 23.3% of the pension savings. In September 2006 these investments had increased to US\$39,886 million, equivalent to 49.52% of the Fund. Thus the funds as a whole have an additional US\$27,713 million in these investments, the figures being measured at the dollar value in September 2006.

This increase is due to more purchases and the rise in the prices of this type of security in the markets.

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