

## In Spite of the Crisis: Multi-funds Have Met their Two Major Objectives

- ❖ **A total of eight countries in Latin America and Eastern Europe have adopted this system, which today manages the savings of 59 million workers.**
- ❖ **Over half the members have increased the “expected value” of their pensions and those close to retirement have reduced the risk to their savings.**
- ❖ **Multi-funds around the world manage savings worth US\$220,000 million.**
- ❖ **In seven countries, members who do not choose a fund are assigned to one by law.**
- ❖ **Chile, Mexico, Peru and Hungary assign workers who do not choose a fund on the basis of their age.**
- ❖ **Chile and Mexico have five types of fund. In Hungary and Lithuania the most risky funds can invest up to 100% in equities.**

### Introduction

Seven years after the implementation of Multi-funds in Chile (2002), this system has shown itself to be a valuable tool for managing workers' pension savings, to the point of becoming an example for the implementation of similar schemes in other parts of the world. Mexico, Peru, Slovakia, Estonia, Hungary, Latvia and Lithuania have followed similar paths and Colombia is preparing to introduce it next year.

The two main objectives of offering members differentiated portfolios are: to increase the expected value of pensions and reduce the risk of pension savings for members who are nearing retiring age.

In point of fact, it was the Asian Crisis (1997-1998) that sounded alarm bells with regard to the risks being run by the savings as a result of everything being held in a single fund, which had been the case until then. Although the fall in yield in 1998 was slight by the close of the year, it was enough to prompt the creation of a second fund for those who were nearing retirement. At the same time, studies began on a project that would link investments to members' life-cycle.

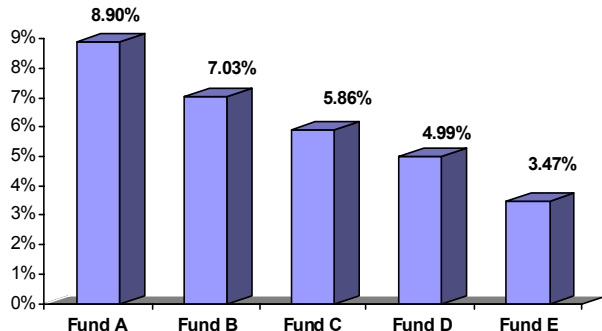
The multi-funds in Chile, despite the steep fall in the value of the funds in 2008, have met the two major objectives for which they were created.

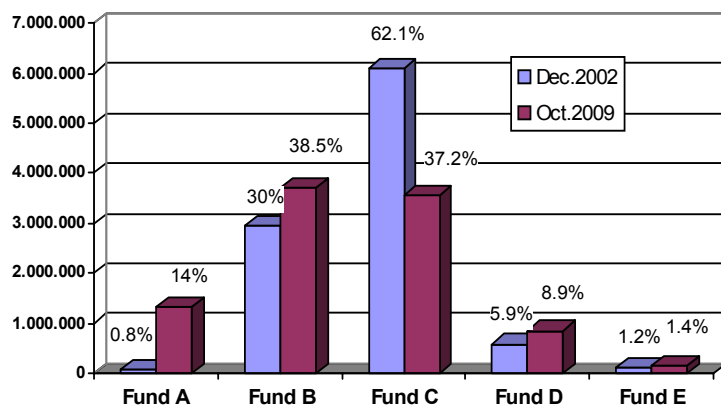
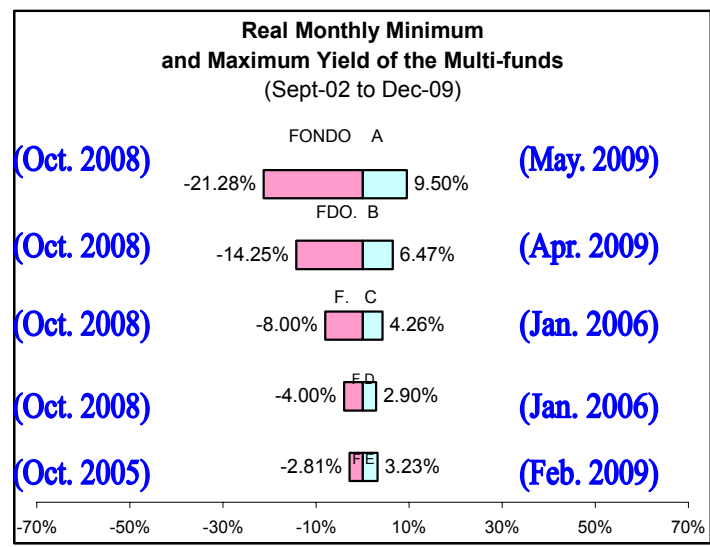
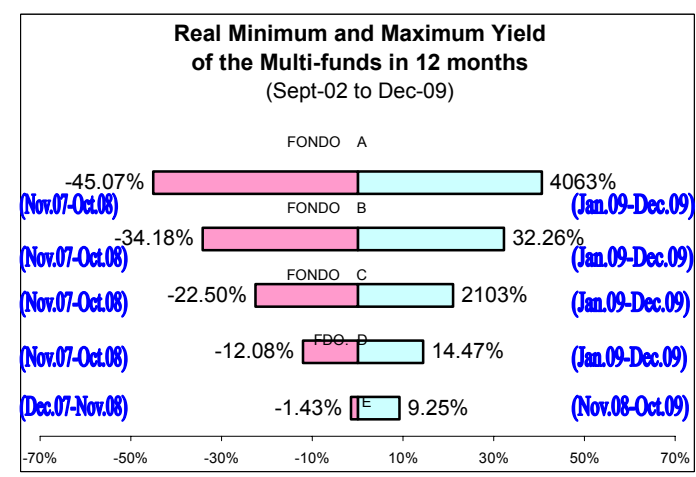
### The merit of having various portfolios

Until September 2002, in practice there was only one fund, because the other one was very small (0.13% of the savings) and was only for those very close to retirement or for pensioners receiving programmed withdrawals.

**Figure N° 1**  
**Yield of Multi-funds**

((Average annual yield over the UF, Sept.2002 - Dec. 2009))



**Figure N°2****N° of Members per Fund****Figure N°3****Figure N°4**

The continuation of the historic fund is today's Fund C. The yield of that fund is a yardstick for comparing the yield of the other funds: the more risky A and B and the more conservative D and E.

Between 2002 and 2009 (See Figure N° 1), the C-Type Fund shows an average annual yield of UF + 5.86%. Funds A and B record annual yield averages UF + 8.9% and UF + 7.03%, respectively. On the other hand, Funds D and E have obtained average annual yields of UF + 4.99% and UF + 3.47%.

Given that the majority of those who are in the riskier funds are under 40 years of age, the conclusion is that those who have benefited most from higher yields are the youngest people, who can therefore hope to improve the value of their pensions in the long term.

In point of fact, if one analyses the age of the members belonging to the various funds as of September 2009, it can be seen that the average age in Fund A is 33 years; in Fund B, 31 years; in Fund C, 45 years; in D, 57 years and in Fund E the average age is 44 years.

Another way of analysing the figures is to observe what proportion of members are under 40 years of age in each Fund. In September 2009, Fund A has 75% of its members under the age of 40; Fund B, 92%; Fund C, 25%; Fund D, 3.2% and Fund E, 38%. It is important to bear in mind that both Fund A and Fund E are chosen voluntarily by members, which explains the different age correlation with Funds B, C and D.

**How many members have benefited?**

As of October 2009, the distribution of members was 52.5% in Funds A and B; 37.2% in C and only 10.3% in Funds D and E. The above shows that over half the members have seen their savings grow over and above the yield offered by Fund C, the continuation of the Fund in which almost all members were concentrated until September 2002, when the multi-funds were launched.

**Reduction of risk**

In Figures N° 3 and N° 4 it is possible to see the minimum and maximum performance of the multi-funds, measured in monthly terms and in 12-month periods.

Clearly, the objective of minimising the risk of the savings belonging to members nearing retirement, most of whom are in Funds D and E, has been met.

Prior to the Multi-funds, almost all members were exposed to the performance of the C-Type Fund, which in monthly terms shows a fall in yield of up to UF –8.0% in October 2008 and a rise of UF + 4.25 in January 2006.

If the C-Type Fund is measured for 12 months, since the Multi-funds began, it recorded a fall of up to UF – 22.5% in October 2008 and a rise of UF + 22.53% in December 2009. Those members close to retirement, who are located mainly in Funds D and E, have reduced the risk of their funds being exposed to a heavy fall.

In point of fact, in monthly terms, the greatest fall registered in Fund D is UF – 4% in October 2008 and UF – 2.81% in Fund E in October 2005.

In 12 months, the greatest fall registered in Fund D was UF – 12.08% in October 2008 and UF –1.43% in November 2008 in the case of Fund E.

#### Multi-funds in other countries

Currently eight countries have introduced multi-funds, three in Latin America (Chile, Mexico and Peru) and five in Eastern Europe (Estonia, Latvia, Lithuania, Slovakia and Hungary). Colombia will be doing so shortly (See Table N° 1).

#### Number of funds and limits on equities

**Table N°1**

	Implementation of Individually Funded System	Implementation of Multi-funds System
Chile	1981	2002
Estonia	2002	2002
Latvia	2001	2003
Lithuania	2004	2004
Mexico	1997	2005
Peru	1993	2005
Slovakia	2005	2005
Hungary	1998	2007

Source: International Federation of AFPs (FIAP)

Chile and Mexico in Latin America have five different investment alternatives, while in Peru three funds have been authorised.

In Eastern Europe, by contrast, most countries offer three pension funds, with the exception of Lithuania which maintains four portfolios.

All the countries that offer multi-funds differentiate the options by the maximum percentage of investment that can be made in equities (See Table N° 2).

In Chile, Peru and Hungary the most conservative strategy allows a percentage of the assets to be invested in equities. In the remaining five countries, the most conservative strategy only allows investment in fixed-income instruments.

On the other hand, the maximum limit of investment in

**Table N°2**

	N° of Funds	Funds and Maximum Equities Limit				
		Fund A: 80%	Fund B: 60%	Fund C: 40%	Fund D: 20%	Fund E: 5%
Chile	5	Fund A: 80%	Fund B: 60%	Fund C: 40%	Fund D: 20%	Fund E: 5%
Estonia	3	Aggressive: 60%		Balanced: 25%		Conservative: 0%
Latvia	3	Active: 30%		Balanced: 15%		Conservative: 0%
Lithuania	4	Shares: >70%	Medium Proportion of Shares		Low proportion of Shares	Conservative: 0%
			Between 70% and 30%		Up to 30%	
Mexico	5	SB5: 30%	SB4: 25%	SB3: 20%	SB2: 15%	SB1: 0%
Peru	3	Growth: 80%		Mixed: 45%		Preservation: 10%
Slovakia	3	Growth: 80%		Balanced: 50%		Conservative: 0%
Hungary	3	Growth: 100%		Balanced: 40%		Conventional: 10%

Source: International Federation of AFPs (FIAP)

equities in the most risky funds varies from 30% in Mexico and Latvia to 100% in Hungary and Lithuania. In Chile, Peru and Slovakia the maximum in equities is 80%.

### Assigning of members who do not choose a fund

Regulations in all countries lay down norms for assigning those members who do not choose a type of fund in which to invest their pension savings when they join the pension system.

In Chile, Hungary, Mexico and Peru the rule states that those members who do not exercise their right of choice are assigned to a fund in accordance with their age or the time remaining before they retire. In Estonia, Lithuania and Latvia, members who do not choose are assigned to the most conservative fund, which invests only in fixed-income instruments. In Slovakia, choosing a fund is compulsory, but members

who are over 47 years of age cannot choose the Growth Fund - the most risky -, and those over 55 years old cannot choose the Balanced Fund. (See Table N° 3).

### Distribution of funds and members

In terms of the distribution of members and savings between the various investment options, there are differences to be observed between Latin America and Eastern Europe.

In Chile, Mexico and Peru, most of the assets and members are in balanced portfolios. By contrast, in the Eastern European countries there is a greater preference for the more risky investment strategies (See Table N° 4).

In general, the proportion of members in the most conservative fund is low, with the exception of Latvia, where 20% are registered in that fund.

**Table N°3**

ASSIGNMENT BY AGE					
<b>Chile</b>	<b>Fund A</b>	<b>Fund B</b>	<b>Fund C</b>	<b>Fund D</b>	<b>Fund E</b>
		Men and women under 35 years	Men between 36 and 55 years; Women between 36 and 50 years	Men from 56 and Women from 51 years	
<b>Estonia</b>	<b>Aggressive</b>		<b>Balanced</b>		<b>Conservative</b>
	Members who do not choose a fund are assigned to the Conservative Fund (100% Fixed Income)				
<b>Latvia</b>	<b>Active</b>		<b>Balanced</b>		<b>Conservative</b>
	Members who do not choose a fund are assigned to the Conservative Fund (100% Fixed Income)				
<b>Lithuania</b>	<b>Shares</b>	Medium proportion of shares: Between <b>70 % and 30%</b>		Low proportion of Shares Up to <b>30%</b>	<b>Conservative:0%</b>
	Members who do not choose a fund are assigned to the Conservative Fund (Govt. bonds only)				
<b>Mexico</b>	<b>SB5</b>	<b>SB4</b>	<b>SB3</b>	<b>SB2</b>	<b>SB1</b>
	Members under 27 years	Members between 27 and 36 years	Members between 37 and 45 years	Members between 46 and 55 years	Members over 55 years
<b>Peru</b>	<b>Growth</b>		<b>Mixed</b>		<b>Preservation</b>
			Members up to 60 years		
<b>Slovakia</b>	<b>Growth</b>		<b>Balanced</b>		<b>Conservative</b>
	Members obliged to choose a fund, excluding the Growth fund in the case of those over 47 years and the Balanced fund for those over 55 years				
<b>Hungary</b>	<b>Growth</b>		<b>Balanced</b>		<b>Conservative</b>
	Over 15 years from retiring age		Between 5 and 15 years from retiring age		Less than 5 years from retiring age

Source: International Federation of AFPs (FIAP)

All the multi-fund schemes allow members to transfer their balances between the portfolios of the same Administrator. Chile's is the only one in which regulations allow workers to divide their resources between two

funds in the same AFP. In the remaining countries, the savings may be kept in only one of the investment alternatives offered by each Administrator.

**Table N°4**

	DISTRIBUTION OF FUNDS AND MEMBERS				
	Fund A	Fund B	Fund C	Fund D	Fund E
<b>Chile</b> Funds MMUS\$109,905 Members 8,542,079 October 2009	Fund: MMUS\$ 22,808 Members: 14%	Fund: MMUS\$ 22,573 Members: 38.5%	Fund: MMUS\$ 46,653 Members: 37.2%	Fund: MMUS\$ 13,502 Members: 8.9%	Fund: MMUS\$ 4,370 Members: 1.4%
<b>Estonia</b> Funds MMUS\$1,034 Members: 580,000 December 2008	<b>Aggressive</b> Fund: MMUS\$ 766 Members: N/A		<b>Balanced</b> Fund: MMUS\$ 181 Members: N/A		<b>Conservative</b> Fund: MMUS\$ 87 Members: N/A
<b>Latvia</b> Funds MMUS\$930 Members: 1,065,564	<b>Active</b> Fund: MMUS\$ 686 Members: 73%		<b>Balanced</b> Fund: MMUS\$ 74 Members: 7%		<b>Conservative</b> Fund: MMUS\$ 170 Members: 20%
<b>Lithuania</b> Funds MMUS\$5,321 Members: 957,000 December 2008	<b>Shares</b> Fund: MMUS\$ 106 Members: 6%	Medium proportion of shares: Between 70 % and 30%	<b>Low proportion of Shares Up to 30%</b> Fund: MMUS\$ 4,310 between the two balanced funds	Members: 26%	<b>Conservative</b> Fund: MMUS\$ 905 Members: 12%
<b>Mexico</b> Funds MMUS\$73,109 Members: 39,063,973 December 2008	<b>SB5</b> Fund: MMUS\$ 5,118 Members: 13.3%	<b>SB4</b> Fund: MMUS\$ 21,933 Members: 37.4%	<b>SB3</b> Fund: MMUS\$ 21,202 Members: 26.1%	<b>SB2</b> Fund: MMUS\$ 16,815 Members: 14%	<b>SB1</b> Fund: MMUS\$ 8,042 Members: 9.2%
<b>Peru</b> Funds MMUS\$16,170 Members: 4,296,480 December 2008	<b>Growth</b> Fund: MMUS\$ 2,771 Members: 7%		<b>Mixed</b> Fund: MMUS\$ 11,869 Members: 90%		<b>Preservation</b> Fund: MMUS\$ 1,368 Members: 3%
<b>Slovakia</b> Funds MMUS\$3,109 Members: 1,483,026 December 2008	<b>Growth</b> Fund: MMUS\$ 2,074 Members: 69%		<b>Balanced</b> Fund: MMUS\$ 904 Members: 26%		<b>Conservative</b> Fund: MMUS\$ 131 Members: 5%
<b>Hungary</b> Funds MMUS\$9,857 Members: 2,947,860 December 2008	<b>Growth</b> Fund: MMUS\$ 4,419 Members: 52%	Savings without multi-funds MMUS\$3,845 (40%)	<b>Balanced</b> Fund: MMUS\$ 1,308 Members: 8%	Members without Multi-funds 1,142,412 (39%)	<b>Conservative</b> Fund: MMUS\$ 85 Members: 1%

Source: International Federation of AFPs (FIAP)

**Important:** The comments and statements given in this document should be taken as general orientation to increase social security culture and can in no circumstances be considered as a recommendation to take the place of personal, free and informed evaluation and decision on the part of members.

The information contained in this Bulletin may be reproduced in its entirety by the communications media. Inquiries: Research Department, The Chilean Pension Fund Administrators' Association Address: Avenida 11 de Septiembre 2155, Torre B, piso 14, Providencia, Santiago – Chile  
Telephone: (56-2) 381 1717 Fax: (56-2) 381 1721 E-mail: estudios@aafp.cl WEB: [www.afp-ag.cl](http://www.afp-ag.cl)