

International pension fund comparisons



Providing for income in retirement would seem to be essentially the same task in any country. Yet in practice it is a complex and challenging process and the variety of approaches around the world is remarkable.

Three pillars

Broadly speaking, most countries have a “three pillar” approach to providing retirement income: a state pension system, a range of occupational schemes provided by employers, and products that allow an individual to provide their own pension. The method of funding and the tax status of these pillars vary from country to country.

Some state arrangements are funded – assets are set aside that are earmarked to pay pensions for current workers. This is the case in Sweden and Japan for example. Other state arrangements are unfunded or pay-as-you-go (PAYG), whereby tax revenue from today’s workers pays current pensioners. State PAYG arrangements exist in the US, UK, Switzerland, the Netherlands and Australia. Occupational and individual pensions are generally funded but the level of accumulated assets will vary according to how long these arrangements have existed.

Funding levels

To give an overview of the funding level around the world, Figure 1 shows total pension assets as a percentage of GDP for seven major pension markets, including the UK. Funding levels have not been helped by the equity market

declines of 2000-2002 and those countries with funded pension arrangements with substantial equity investments have suffered the most.

Investment choices

In this brief sketch, the other area of interest is the investment choices made by pension funds around the world. Figure 2 summarises the approximate asset allocations of occupational schemes in the seven major markets. Ten years ago this table would have revealed huge differences between the countries covered. Pension funds in Switzerland, Sweden, the Netherlands and Japan all traditionally had very high bond allocations. Encouraged by the equity bull market of the 1990s, funds in these countries began to embrace equity investment late 1990s and early 2000s, a move that seemed by early 2003 to have been mis-timed. The general recovery of equity markets during 2003 will have restored some confidence in equities.

In the US, UK and Australia, pension funds have had larger equity weightings for some time. This was a successful strategy in the 1990s but was less so in 2000 to 2002. Partly through market movements, and partly through deliberate asset allocation moves, the equity weightings in these countries generally came down at least a few percentage points over this period. 2003 saw weightings pick up once more, largely due to market movement. The net result is that pension fund asset allocation is beginning to acquire greater similarities across the major markets, although differences still persist. ►

Figure 1. Funding levels compared

Country	Total pension assets (US\$ billion)	GDP 2003 (US\$ billion)	Total pension assets as % of GDP	Population (millions)	Total pension assets per capita (US\$)	Old age dependency rate (%) 2000	Old age dependency rate (%) 2030 (projected)
Australia	426	514	83%	20	21,657	18	32
Japan	2,463	4,301	57%	127	19,328	25	52
Netherlands	545	513	106%	16	33,820	20	40
Sweden	226	302	75%	9	25,322	27	46
Switzerland	319	316	101%	7	43,753	24	53
UK	1,266	1,795	71%	59	21,454	24	40
US	7,438	10,857	69%	289	25,773	19	33

Sources: GDP and population data from OECD. Old age dependency rate is population aged over 65/population in working age (15-64), expressed as a percentage. Total pension asset data at 31 December 2003 unless stated otherwise: Australia: APRA. Japan: Japanese Ministry of Health, Labour & Welfare, UBS Global AM estimates (31 March 2003). Netherlands: CBS (30 September 2003). Sweden: Government of Sweden. Switzerland: Bundesamt für Statistik (31 December 2002). UK: UBS Global AM estimate based on National Statistics data. US: Federal Reserve.

Figure 2. Asset allocation – major pension markets

	Domestic equities	International equities	Domestic bonds	International bonds	Cash	Real Estate	Other
	%	%	%	%	%	%	%
Australia	31	22	17	5	6	12	7
Japan	27	17	32	13	5	1	5
Netherlands	7	36	8	32	4	5	8
Sweden	21	16	29	26	2	6	0
Switzerland	12	13	30	16	10	15	4
UK	39	28	12	3	3	6	9
US	48	14	33	1	1	2	1

Sources: As Figure 1 except UK: WM, US: Callan Associates, Sweden: UBS Global AM

Global themes

There are several other discernable global themes in pension provision, the most notable being pension reform and the increasing tendency among governments to shift the burden of provision from the state to employers and individuals as the demographics begin to look difficult.

Awareness among pension providers of what's going on beyond their own national borders has heightened considerably. In Europe in particular, the moves towards a pensions directive engaged the interest of national

governments and scheme sponsors alike. Early drafts included quite prescriptive investment restrictions which were unpalatable to several member states. The cross-border pension fund rules finally approved by EU ministers in 2003 leave funds broadly free to decide their investment strategy. The Directive became EU law in September 2003.

It is clear that investment strategies, and pension provision in general, are on the road to becoming more homogeneous in Europe and, indeed, around the world. ■

UBS Global Asset Management contacts

Americas

Frank Pfeffer
+1 212 882 5099
frank.pfeffer@ubs.com

Asia Pacific

Patrick O'Sullivan
+81 3 5293 3701
patrick.osullivan@ubs.com

EMEA (ex Switzerland and UK)

Michael Strobaek
+41 1 235 5593
michael.strobaek@ubs.com

Switzerland

Andreas Schlatter
+41 1 234 8094
andreas.schlatter@ubs.com

UK

Nigel Taylor
+44 20 7901 5604
nigel.taylor@ubs.com

Alternative and Quantitative Investments

Bill Ferri
+1 212 821 5124
william.ferri@ubs.com

Real Estate

James O'Keefe
+1 860 616 9001
james.okeefe@ubs.com



www.ubs.com

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21 Lombard Street, London EC3V 9AH.

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