



Swiss Pensions Conference Webinar:

What's next for Swiss Pensions?

A look at and beyond the results of the Mercer CFA Institute Global Pension Index 2020

Speakers:

Dr. David Knox, Senior Partner, Mercer

Tobias Wolf, CFA, Head of Advisory Business, Mercer Switzerland

Ivan Guidotti, PhD, CFA, Head of Investments, XO Investments and Chair, Swiss Pensions Conference 2020 Romandie

Wednesday, 25 November 2020

09:00–10:00, CET



Webinar: Order and Notes

- Speakers:
Dr. David Knox, Senior Partner, Mercer
Tobias Wolf, CFA, Head of Advisory Business, Mercer Switzerland
Ivan Guidotti, PhD, CFA, Head of Investments, XO Investments and Chair, Swiss Pensions Conference 2020 Romandie
- Use the Q&A to submit questions, if time remains, questions will be consolidated and shared
- Participants remain on mute
- The webinar is being recorded, the recording will be available in due course



MERCER
CFA INSTITUTE
GLOBAL
PENSION
INDEX

2020



Pension systems are all different but important



“People’s trust in pension systems is low.

Population ageing, low returns, low growth, less stable employment careers and insufficient pension coverage amongst some groups have been eroding the belief that all types of pension systems will deliver on their promises”

- OECD, 2018



COVID-19 compounded with existing issues that already impacted pension systems around the world, pension reform cannot be ignored

The starting framework – World Bank model

PILLAR 0

A basic public pension that provides a minimal level of protection

PILLAR 1

A public, mandatory and contributory system linked to earnings

PILLAR 2

A private, mandatory and fully funded system

PILLAR 3

A voluntary and fully funded system

PILLAR 4

Financial and non-financial support outside formal pension arrangements

Some comments on the index

- It is comparative or relative; **not absolute**
- We use **objective data** from international agencies and each country
- Subjective elements (eg community confidence) are important but **very difficult to measure** around the world
- Some desirable data is **not available** for every system
- More than **50 indicators** used; inevitably, weightings are **subjective**
- The index represents **the overall “system”**, not
 - what an individual may receive
 - the best pension fund available

The fundamental questions



ADEQUACY

What do you get?



SUSTAINABILITY

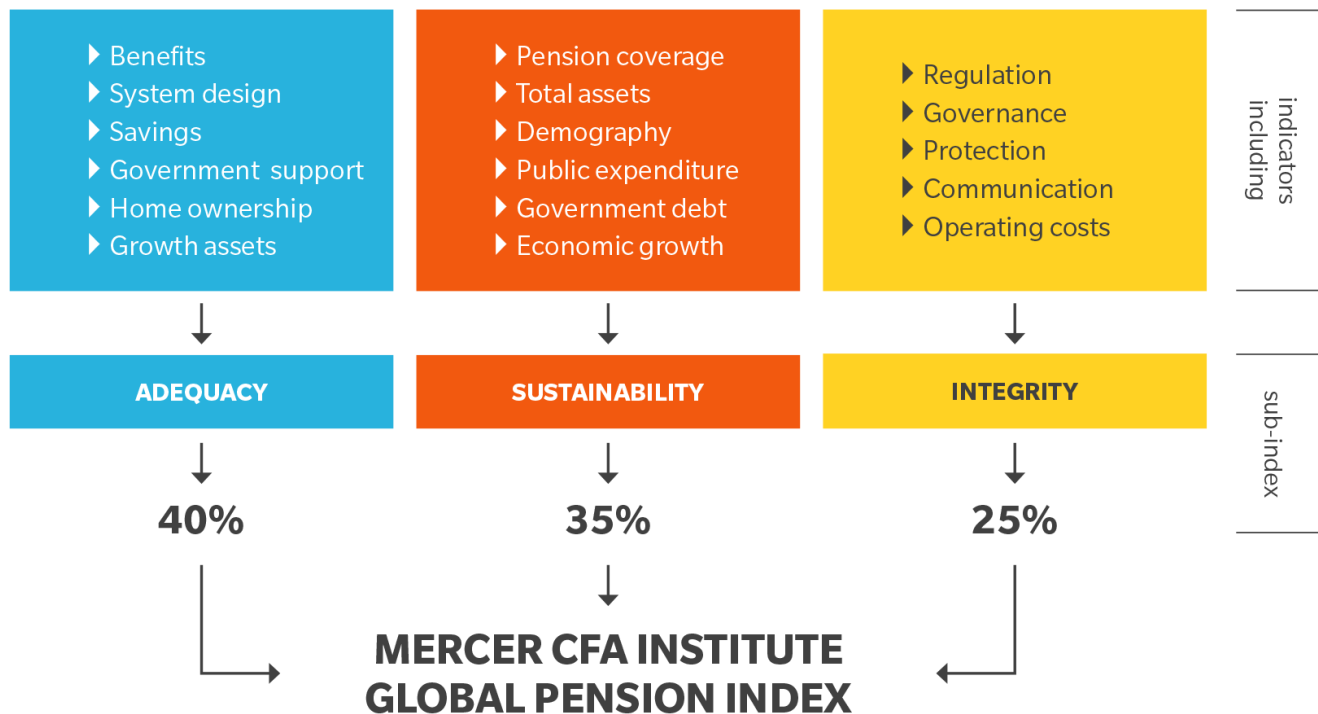
Can it keep delivering?



INTEGRITY

Can it be trusted?

Calculating the Global Pension Index



Updates from 2019 to 2020



New questions: Pension support for carers
Environmental, Social & Governance (ESG) requirements

New systems

Belgium and Israel are new additions to the 2020 report



Bringing the total to 39 retirement income systems

Adequacy

- Minimum (or base) pension
- Net replacement rate (weighted)
- System design features
- Household savings/debt
- Home ownership
- Level of “growth” assets

#1

Netherlands

81.5

#2

Denmark

79.8

#3

Germany

78.8

Switzerland: 23rd, 59.5

... India, Thailand, Mexico



Sustainability

- Coverage of funded pension plans
- Level of pension assets as % of GDP
- Demographic issues
- Mandatory contributions with funding
- Labour force participation rate at older ages
- Public pension costs/Net government debt
- Real economic growth

#1

Denmark
82.6

#2

Netherlands
79.3

#3

Australia
74.6

Switzerland: 8th, 64.2

... Brazil, Austria, Italy



Integrity

- Regulation of private pension plans
- Governance requirements for pension plans
- Protection of members' benefits
- Communication to members
- Costs of the system

#1

Finland

93.5

#2

Norway

90.3

#3

Netherlands

88.9

Switzerland: 9th, 83.1

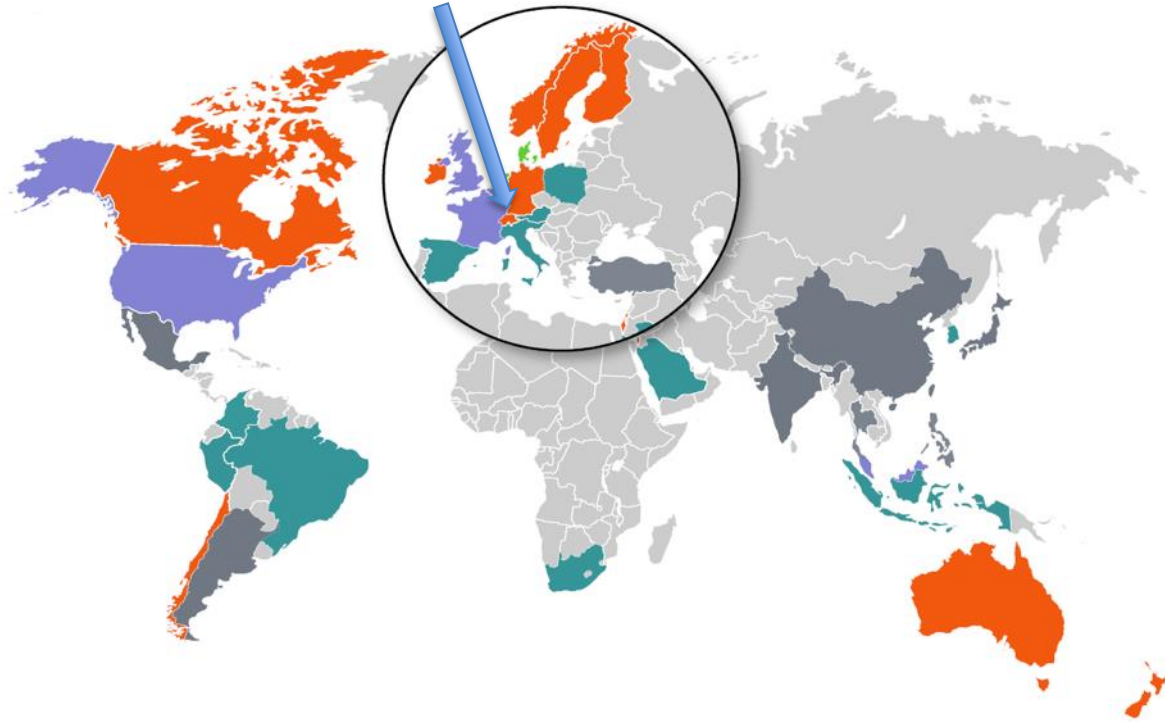
... Argentina, Mexico, Philippines



Results for 2020

67.0; 12th

Grade	Index Value
A	>80
B+	75-80
B	65-75
C+	60-65
C	50-60
D	35-50
E	<35



The impact of COVID-19: Now

Lower real economic growth

Immediate impact on index scores

- Lower sustainability sub-index score
 - Reduction of 1.2, on average, for this indicator

The impact of COVID-19: The future

Possible **future impact** on index scores



Reduced assets for retirement benefits due to several factors



Increased government debt may lead to reduced pensions



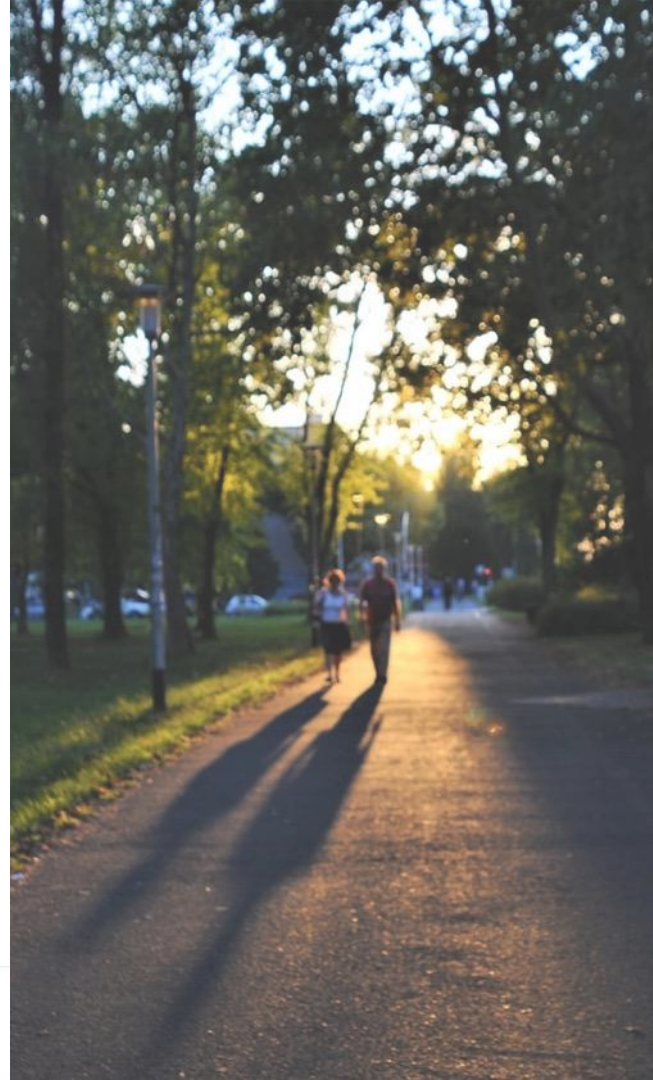
Reduced migration affecting old age dependency ratio



Household saving rates may increase

Global pension reforms are needed

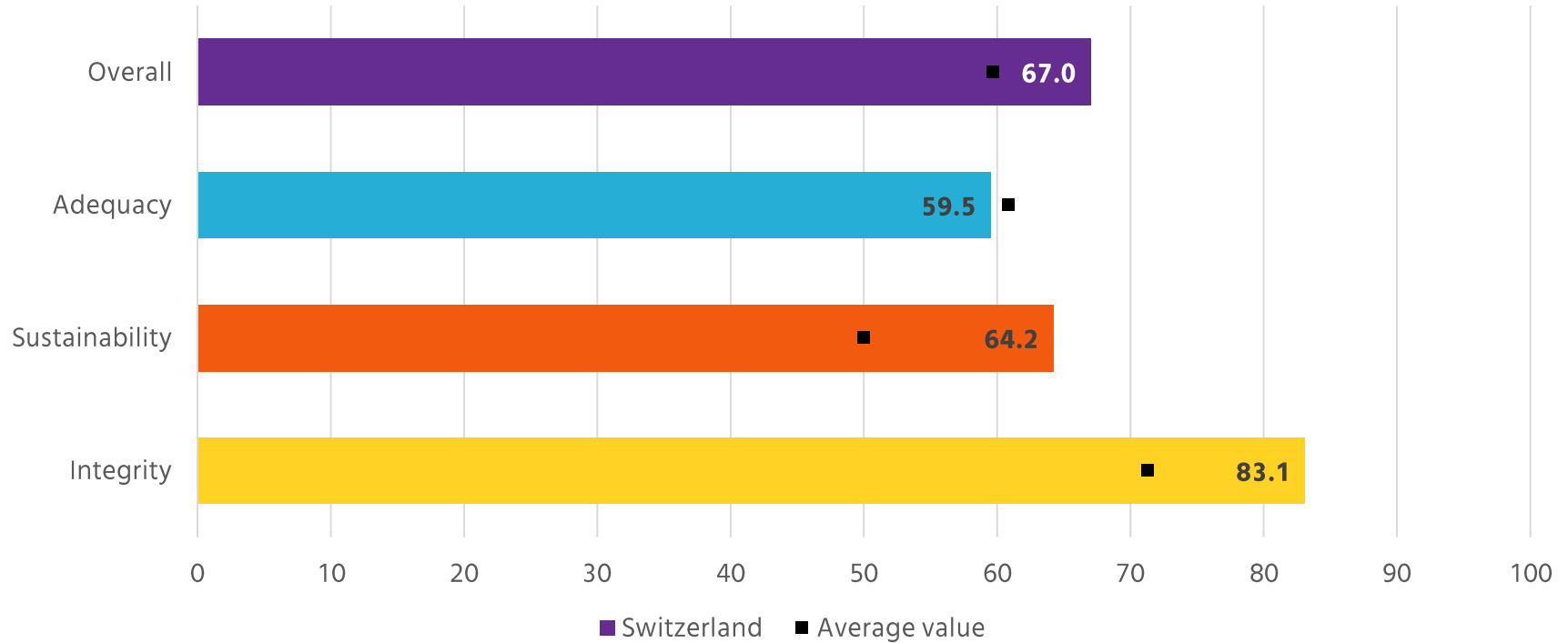
- Increase **coverage**
- Increase the **state pension age**
- Promote higher **labour force participation** at older ages
- Reduce the **leakage**
- Encourage higher levels of **private saving**
- Improve **governance** and **transparency**
- Reduce the pension **gender gap**



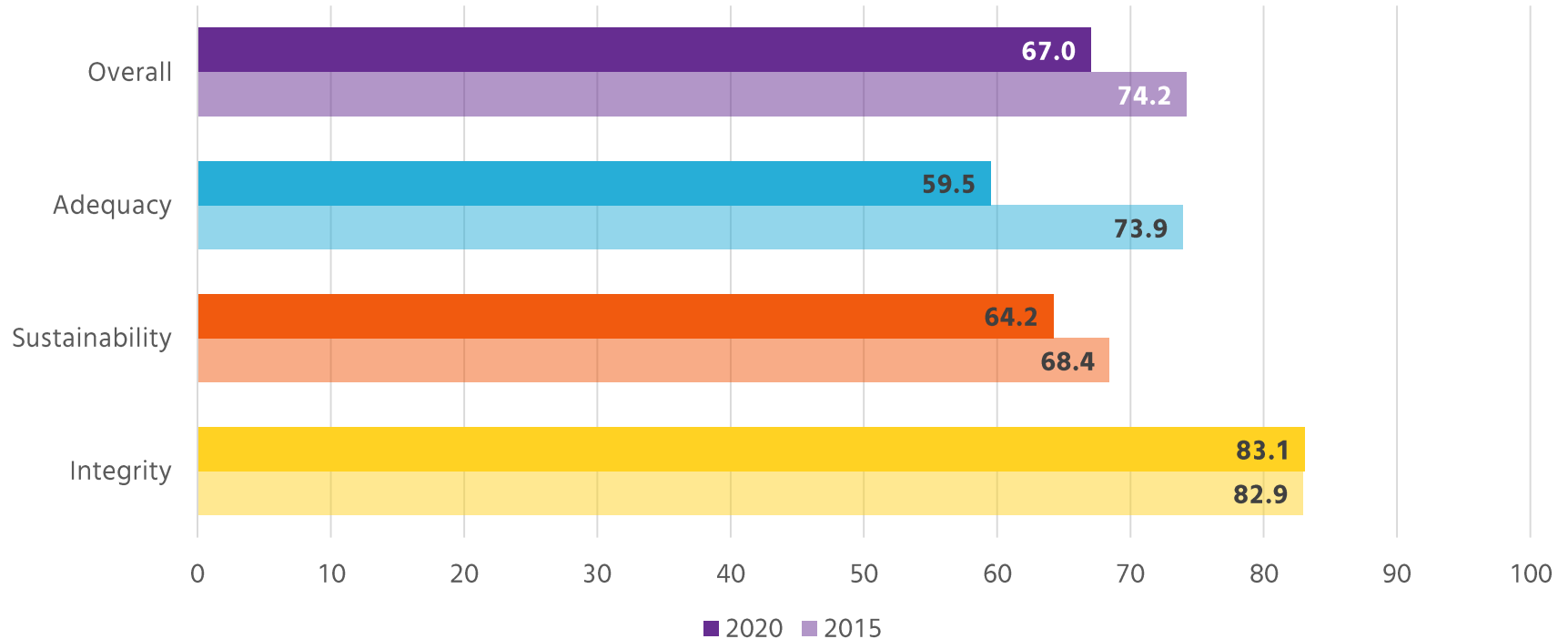
Swiss perspective

– Key challenges –

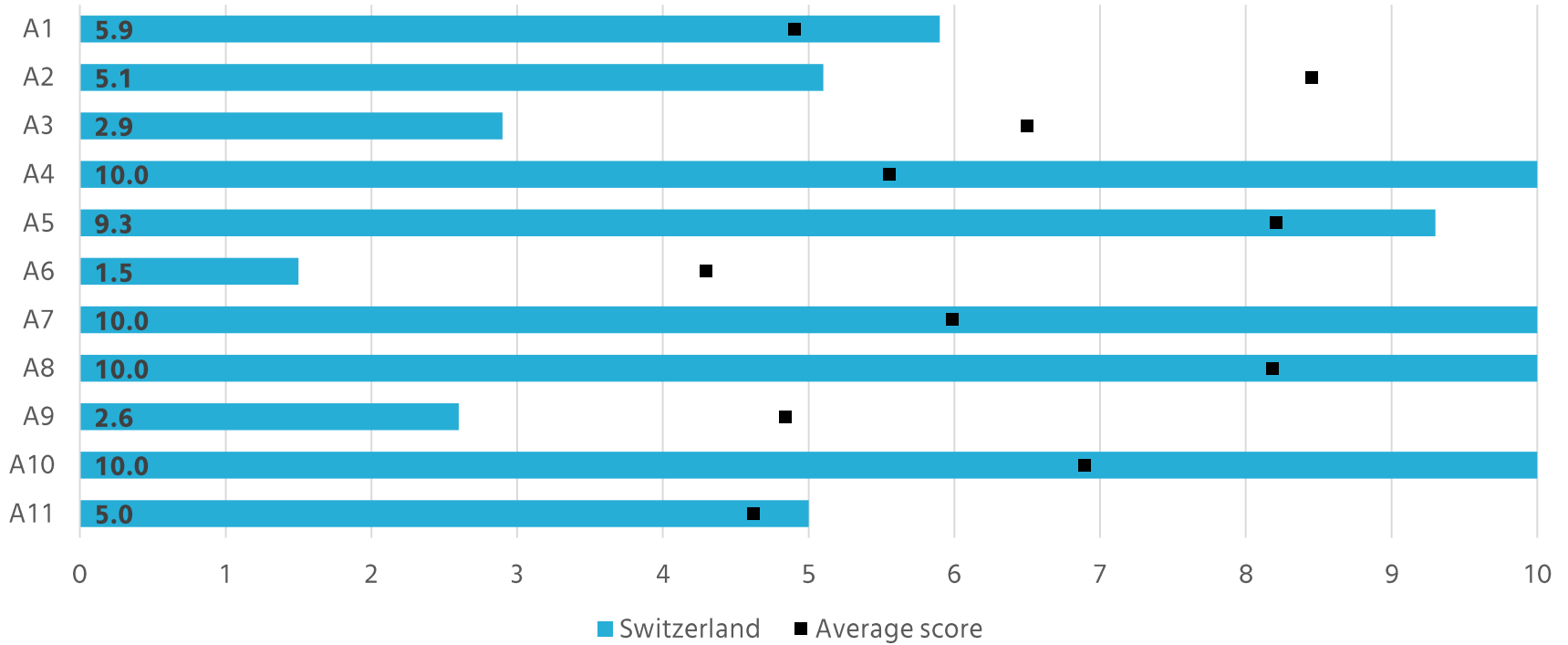
Switzerland's score 2020



Switzerland's score evolution



A closer look at adequacy

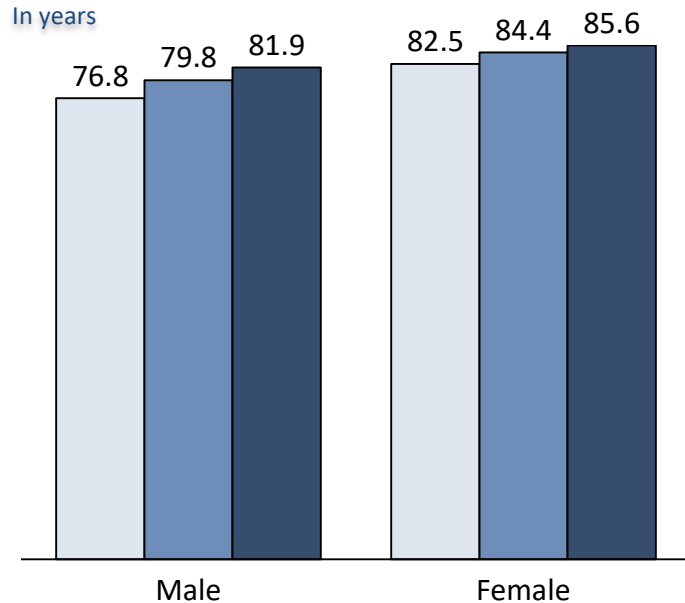


Some comments on Switzerland's score

- Relatively low **net replacement rate**
- High **household debt**
- Low **home ownership**
- No requirement to take **income streams**
- Need to recognise **increasing life expectancy**

Challenging demographic development

Life expectancy: At birth



Life expectancy: At age 65

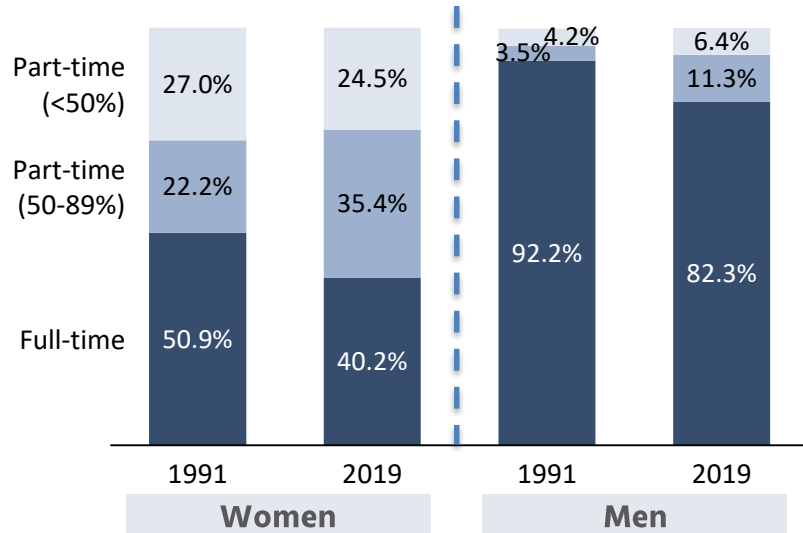


Source: Bundesamt für Statistik

1999 2009 2019

Pension gender gap

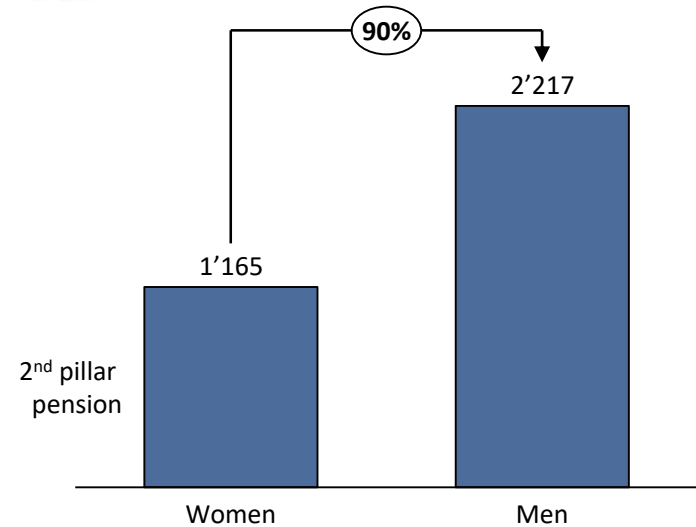
Part-time work rate by gender



Source: Bundesamt für Statistik

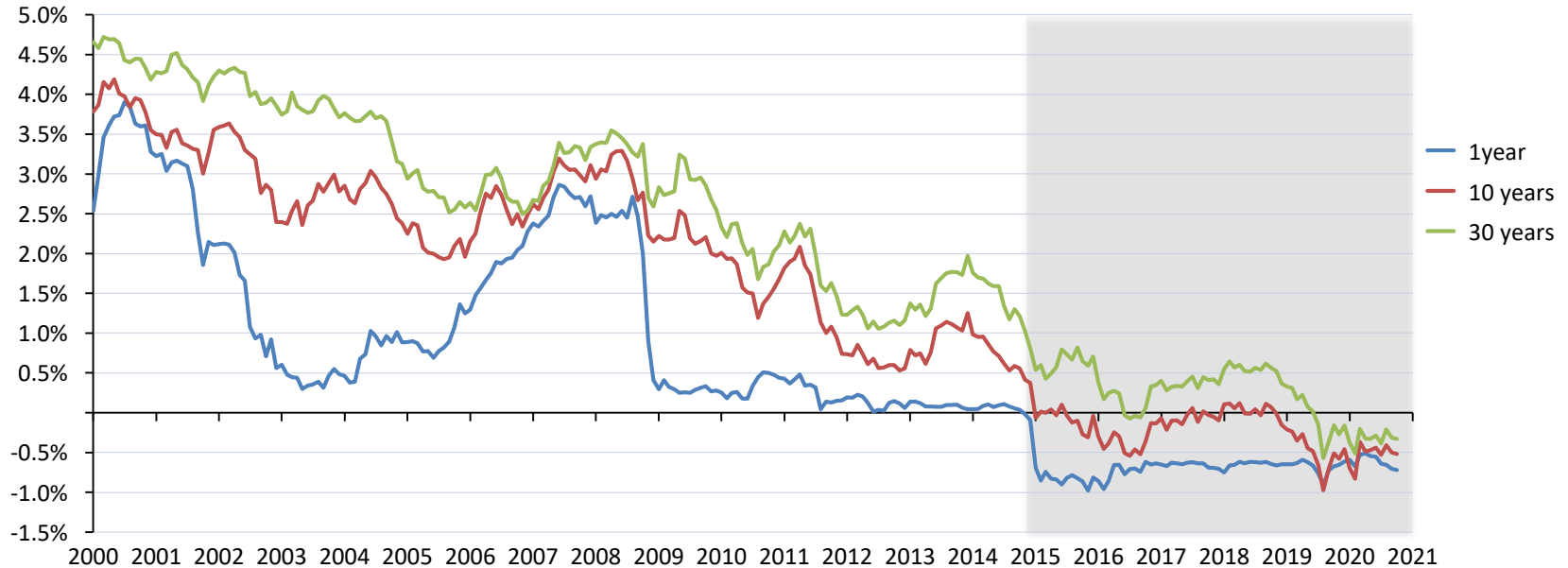
2018: New pensioners' pension by gender (median)

In CHF



Difficult market environment

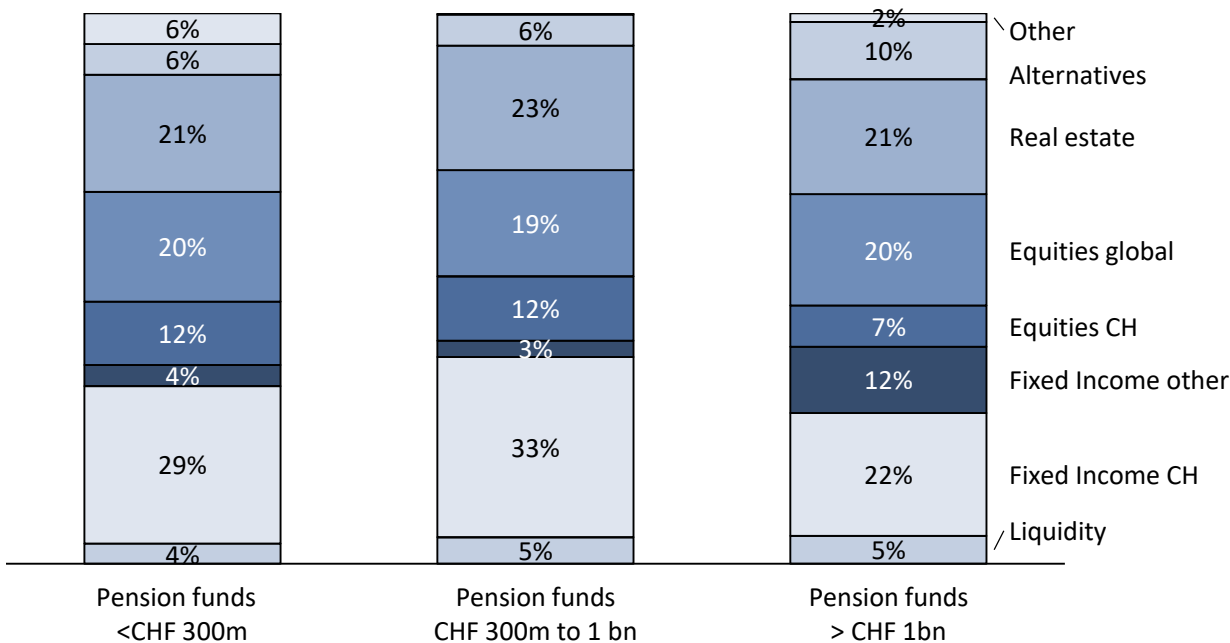
Historic yield of Swiss government bonds



Source: SNB

Inefficient allocation

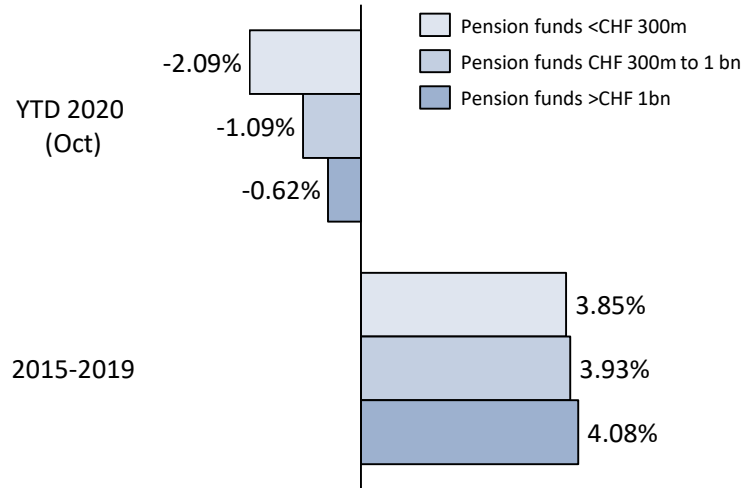
Asset allocation by pension fund Oct 2020



Source: UBS

Advice is needed

Pension Fund Performance (short & mid-term)



Risk-Return Profile (last 36 months per Oct 2020)

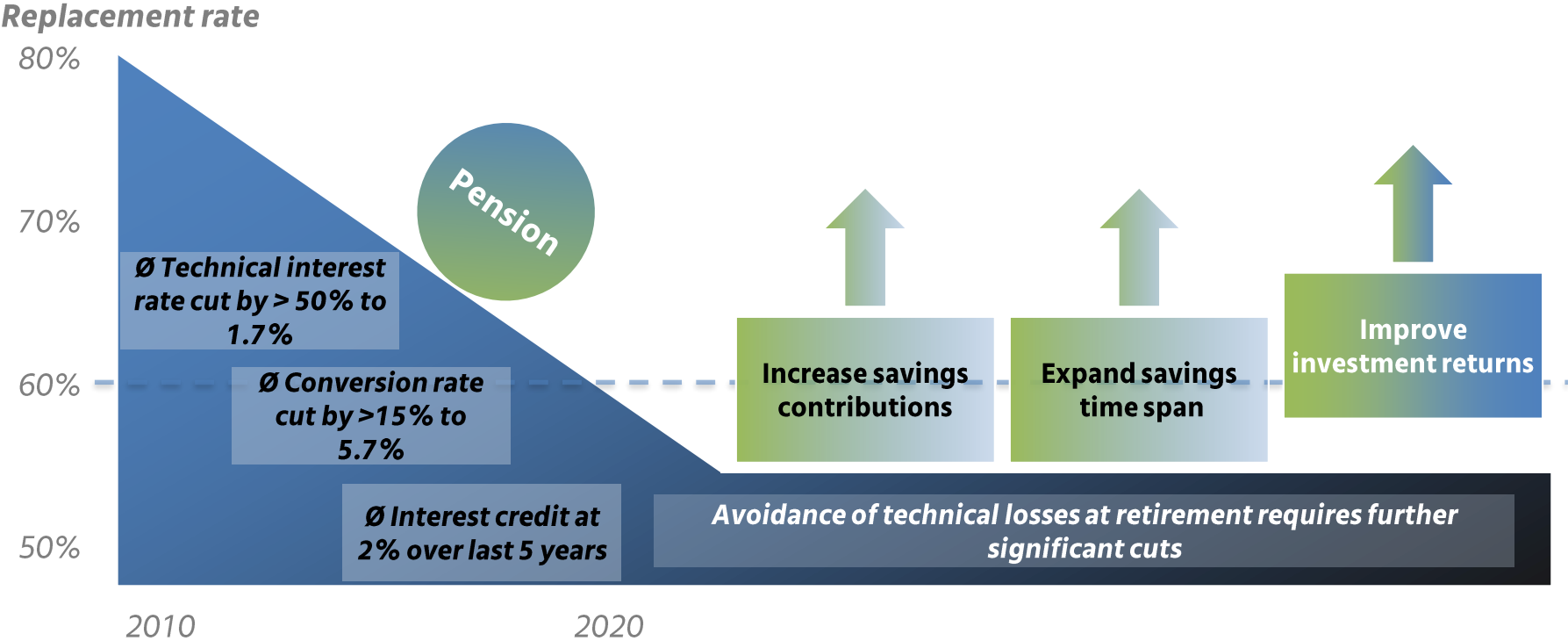
	Pension funds < CHF 300m	Pension funds CHF 300m to 1bn	Pension funds > CHF 1bn
Return annualized	1.84	2.65	2.70
Standard deviation	5.95	5.40	4.91
Sharpe Ratio	0.44	0.64	0.71

Source: UBS

Swiss perspective

– Potential measures –

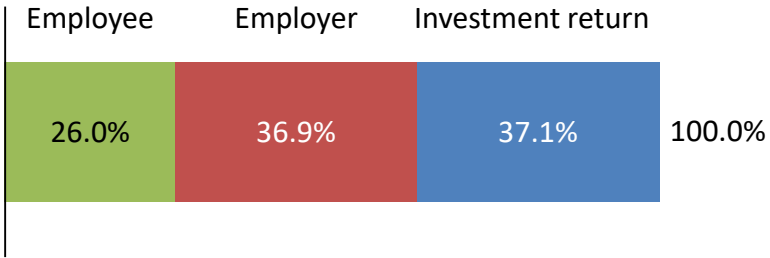
Swiss pensions face a “Race to the Bottom”



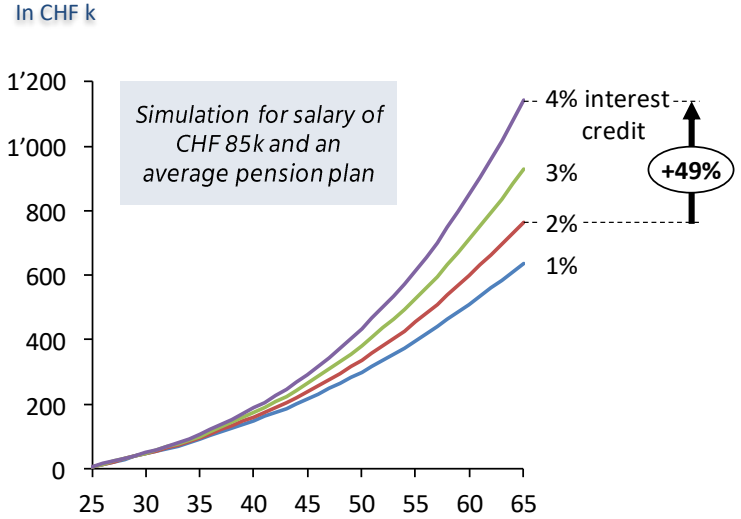
Source: 2010 & 2019 Swisscanto Pensionskassenstudie, 2025 Mercer expectation

Investment returns are a key contributor

Financing sources of pension (average)



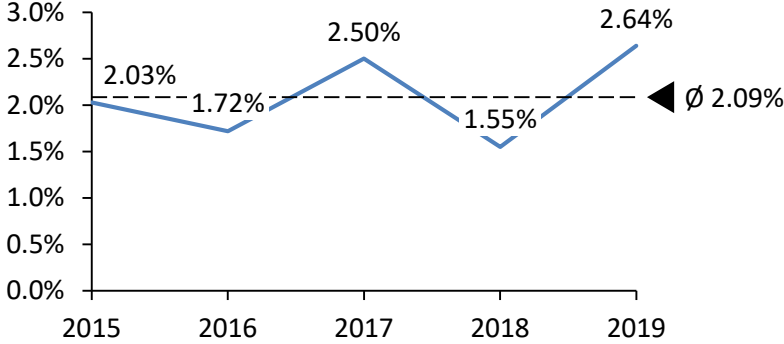
Impact of interest credit on pension savings



Source: Swisscanto Pensionskassenstudie, Mercer analysis

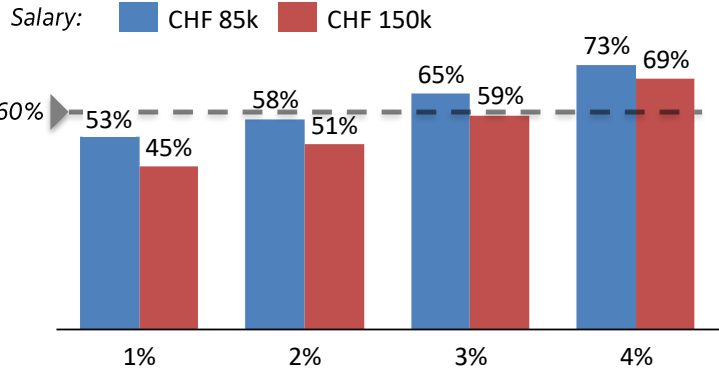
Poor interest credits put pensions at risk

Average interest credit for Actives



Expected replacement rate for average plan

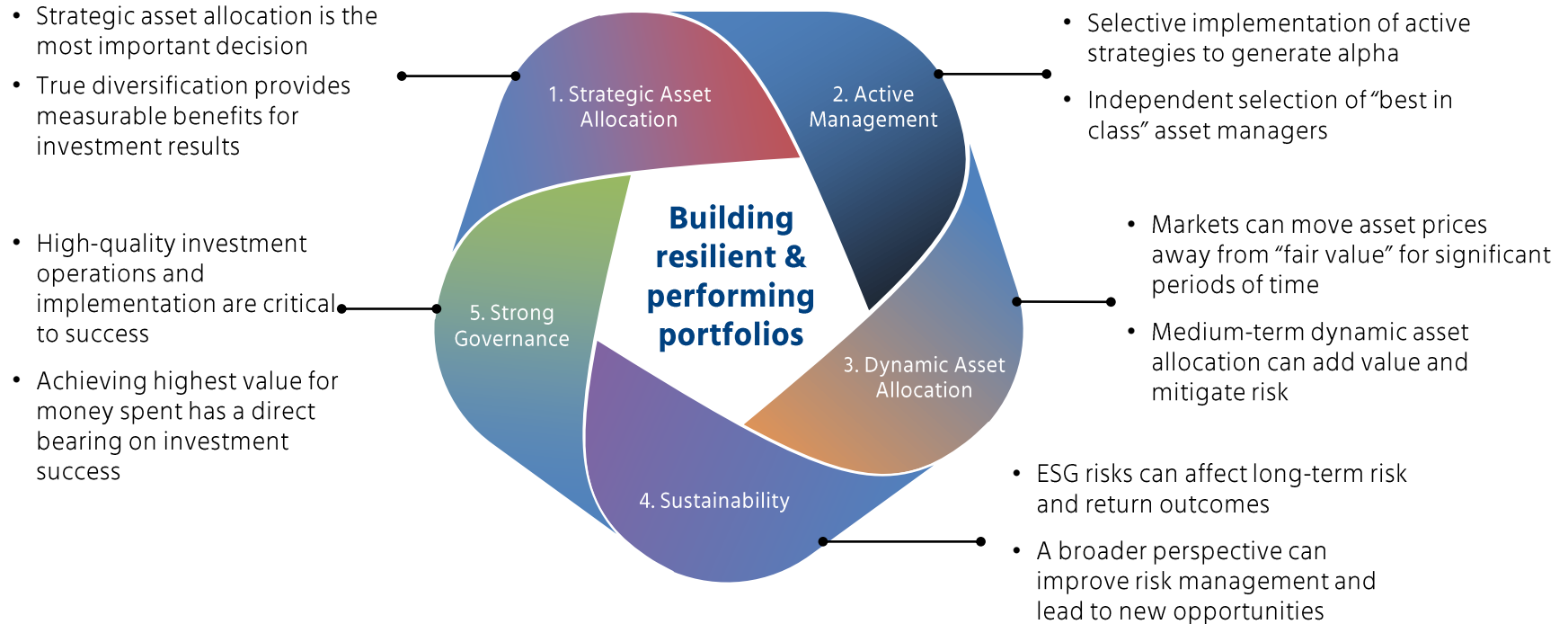
*Including 1st pillar pension;
Assumed full coordination and
conversion rate of 5%*



Average interest credit over working life

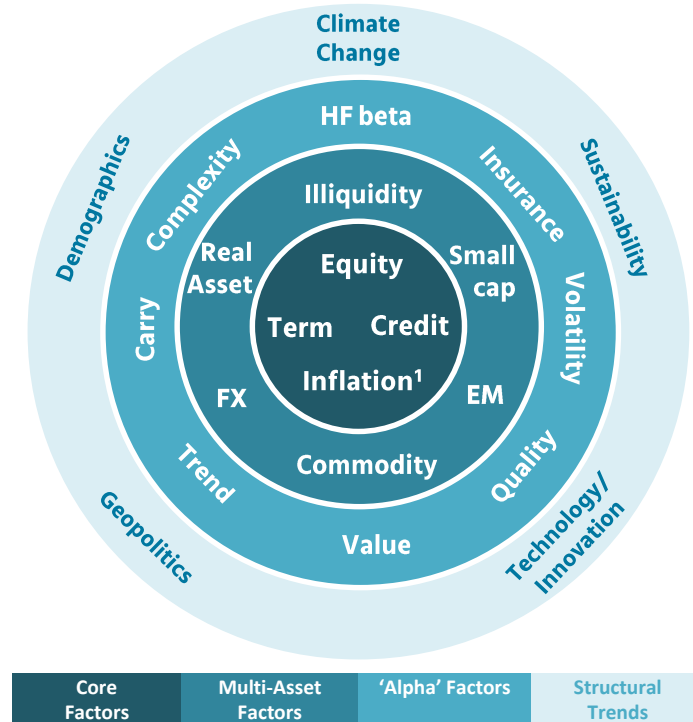
Source: Swisscanto Pensionskassenstudie, Mercer analysis

How to generate better returns for beneficiaries?



True diversification is key

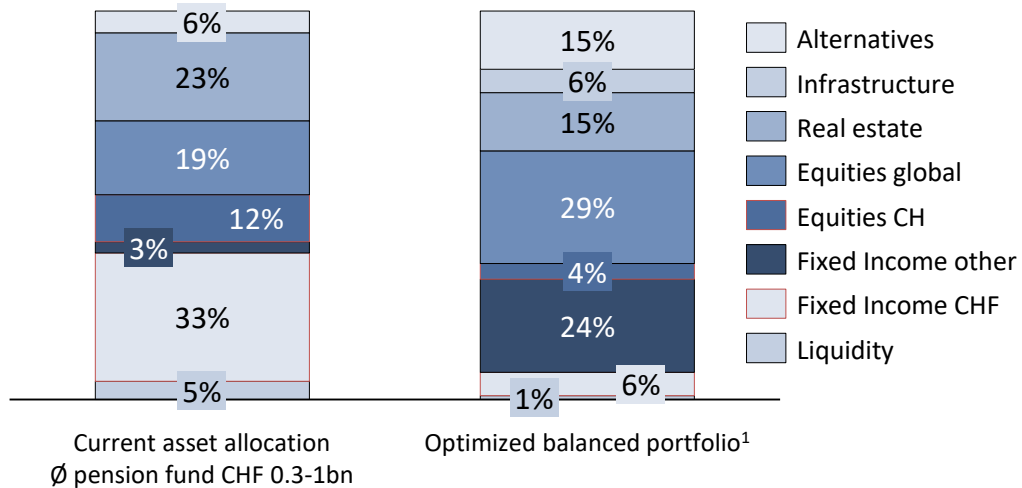
- Focus on **Factor diversification**, pure diversification by asset classes can result in unwanted concentration of certain risks
- Degree of required factor diversification may vary depending on risk tolerance and expected development of the pension fund
- Equity risk is typically the dominating portfolio risk, due to the relatively high volatility compared to other risk factors
- Risk is a multi-dimensional concept. Review of investment strategies based on scenario analysis is recommended



Source: Mercer analysis

1. Specifically Inflation 'Surprise'; Note: EM = Emerging Markets, HF = Hedge Fund; FX = Foreign Exchange

Large potential for higher investment efficiency



Key diversification drivers

- Broader core diversification by reduction of significant home bias
- Harvesting illiquidity and complexity premia through private markets investments
- Much broader diversification across multi asset factors, e.g. Emerging Markets, Small Cap

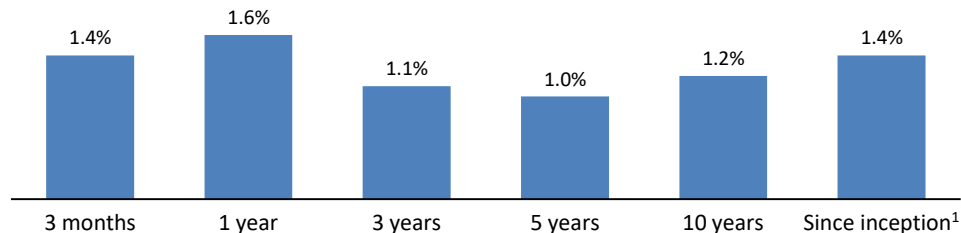
Expected return	2.2%	3.4%
Volatility	5.9%	7.5%
VaR (97.5%)	11.3%	13.0%
Sharpe Ratio	0.36	0.45

1. FX exposure increased only by 3.5% due to FX hedge

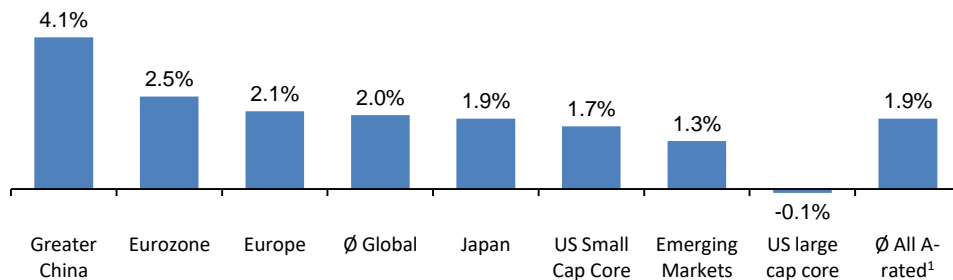
Selective use of active management drives returns

OUTPERFORMANCE POTENTIAL	EQUITIES	FIXED INCOME
H I G H	<ul style="list-style-type: none"> • Small Caps • Emerging Markets 	<ul style="list-style-type: none"> • Emerging Markets • High Yield
M E D I U M	<ul style="list-style-type: none"> • Large Caps (ex US) 	<ul style="list-style-type: none"> • Investment Grade • Aggregate
L O W	<ul style="list-style-type: none"> • US Large Caps 	<ul style="list-style-type: none"> • Government bonds

All asset classes: Value added of A-rated managers per June 30, 2020



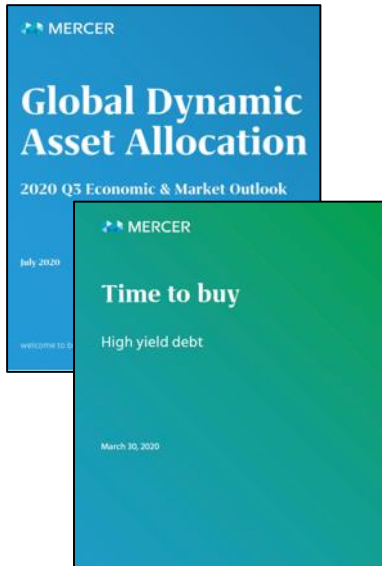
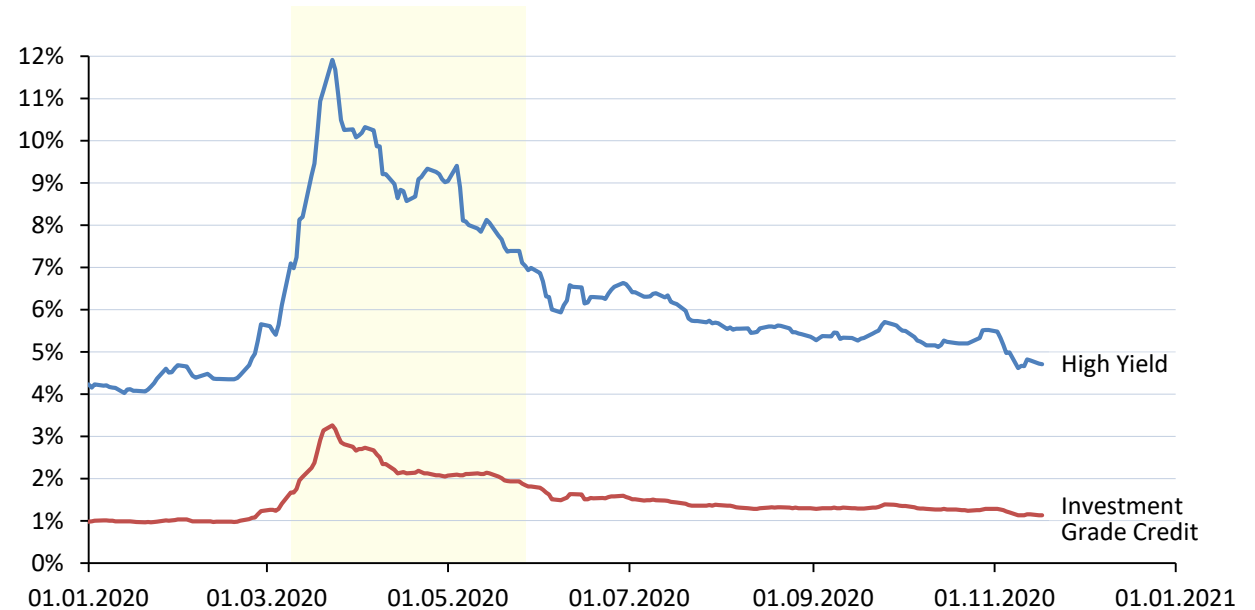
Equities: Value added (p.a.) per June 30, 2020 since inception of A-rating



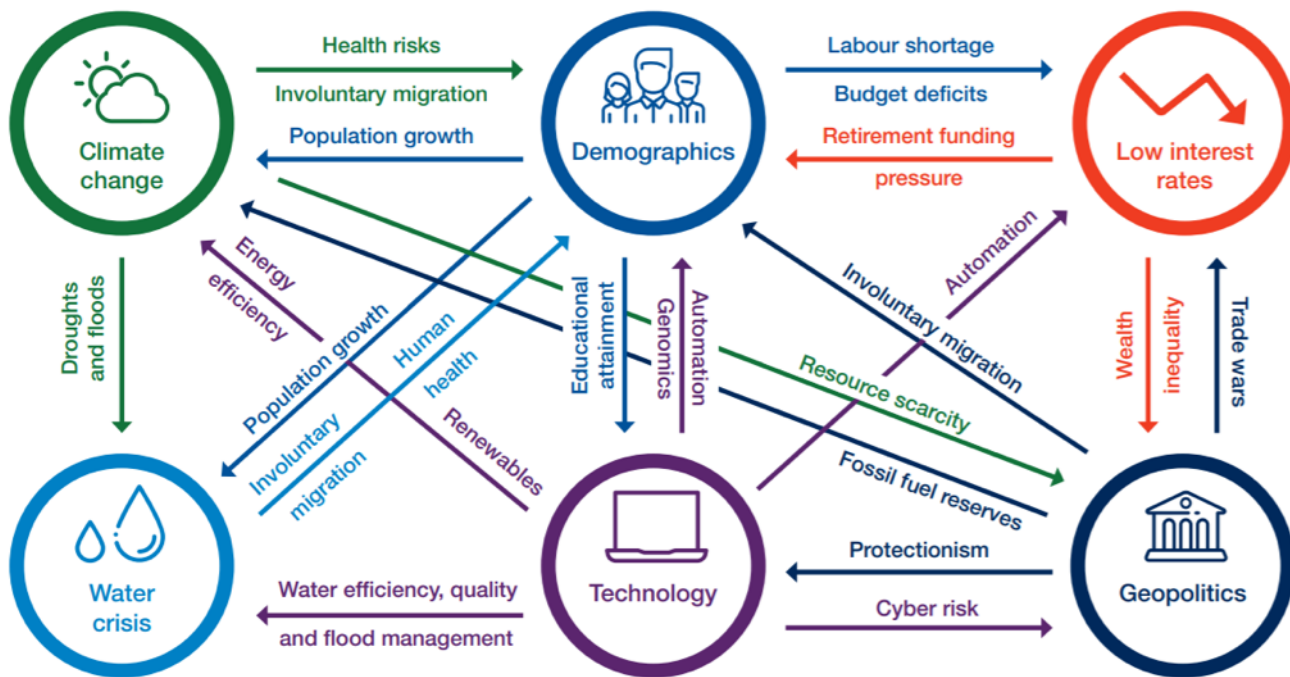
¹ Performance is gross of investment management fees and certain other expenses. Past performance is no guarantee of future results. Please see Important Notices for further information on Value Added Disclosures and Manager rating methodology.

Capturing market opportunities

Credit Spreads in 2020



Considering sustainability to achieve better returns



Source: World Economic Forum and Mercer *Transformational Investment: Converting Global Systemic Risks into Sustainable Returns* (May 2020)

Strong investment governance builds the basis



Clear strategic objectives for the pension fund's investments operations must be defined and target achievement tracked



Professional and robust organizational structure with clear roles and responsibilities that ensures checks and balances



Implement efficient and transparent investment processes, decide on inhouse delivery vs. delegation of single activities

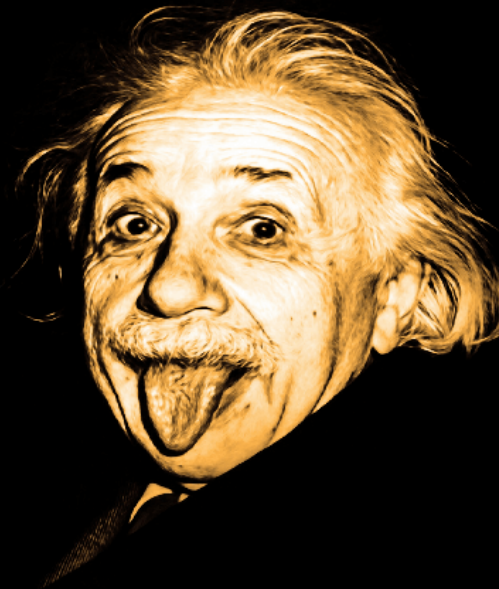


High investment efficiency, i.e. achieving target return at minimum risk and at competitive investment costs; Leverage research and purchasing power of implementation specialists

Pensions are under pressure, but well managed Investments can make a big difference!

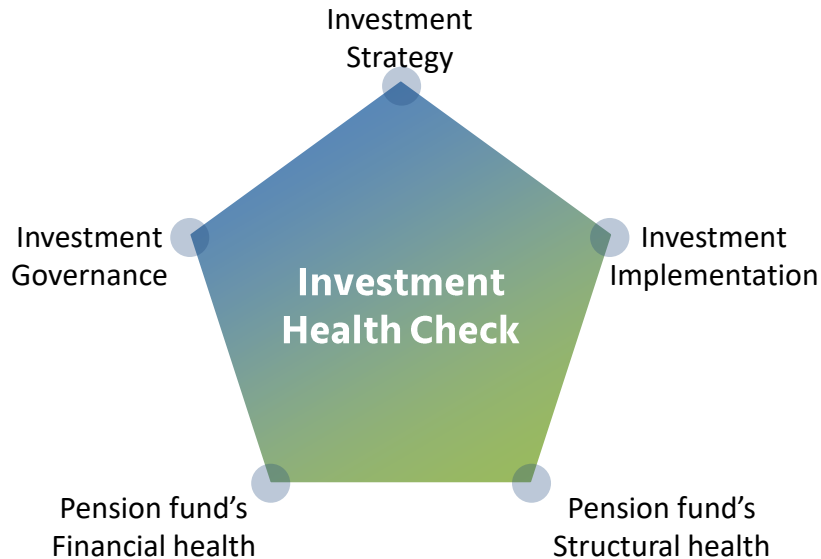
“Compound interest is the eighth Wonder of the World. He who understands it, earns it. He who doesn't, pays it.”

- Albert Einstein



Source: <https://tightwadtodd.com/power-of-compounding-interest/>

Exclusive offer of a complimentary health check



Investment Health Check output

- Status quo assessment of the pension fund's investment strategy, implementation and governance considering pension fund's individual situation
- Identification of potential points for further consideration within the pension fund's investment operations
- Individual presentation and explanation of health check results as well as potential optimization measures

If you are interested in making use of this health check for your pension fund, please send an email to tobias.wolf@mercer.com

Note: Complimentary offer is limited to the first 10 requests.

Q&A

Enter your questions via the Q&A function

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Important Notices – Value Added Disclosures

Measurement of value added through manager research recommendations as of December 31, 2019.

Mercer's Investment business has developed and implemented a methodology for measuring the value added through their manager research recommendations. This methodology and the results of the analysis, for periods to December 31, 2019, are presented below.

Measurement methodology

For most investment strategies that we research, we arrive at a rating on a four-tier scale in which the possible ratings are A, B+, B and C. When we formulate short lists of candidates for clients to consider in manager searches, these are generally drawn from the list of strategies rated A within the relevant product category. We first began maintaining formal ratings on this basis in 1995, replacing less formal methods in place, and have extended this to cover all product categories that we actively research, over the period since.

Our methodology for measuring the performance of our ratings entails calculating the average performance of the strategies that we rated A within each product category each quarter, based on the ratings as they stood at the end of the previous quarter. Therefore, there is no element of hindsight in the analysis. We then compound these quarterly results together to calculate performance over longer periods. Finally, we subtract the return for an appropriate and widely accepted benchmark index for the product category concerned to calculate value added. We also calculate a risk-adjusted measure of the value added known as the information ratio.

In essence, this methodology tracks the performance of a hypothetical Mercer client that is assumed to split its money evenly between all of the strategies rated A by Mercer within the product category concerned. This hypothetical client is assumed to have reviewed its manager lineup at the end of each quarter, based on the Mercer ratings as they stood at that point in time. A typical client would not invest in all strategies in all of the categories, as some may not be relevant to a particular client for a variety of reasons. Therefore, the actual added value of strategies selected by a client would vary from the results depicted here.

Three types of strategy are excluded from the analysis. Firstly, we exclude strategies that are sub-advised by other investment managers, to avoid double-counting. Secondly, where a manager offers two variants of what is essentially just one strategy, we only include one of these in the analysis (we used to use the one with the longer track record but in 2011 we assigned the decision on which track record to use to the researcher responsible for the strategy), once again to avoid double counting. Thirdly, if a strategy's track record relates to a benchmark that is materially different to the benchmark used in the analysis for the product category concerned, it will be excluded from the analysis to avoid distortions that could arise solely as a result of the non-standard benchmark.

Where a manager offers equity strategies in a typical long only format and a variant which includes the ability to short, we only include the long-only version.

Important Notices – Value Added Disclosures

For some product categories, where the use of custom benchmarks is prevalent, there is no single widely accepted benchmark that can be used as a basis for this analysis. We therefore use a slightly different methodology for these categories. In these cases, we carry out the analysis by first calculating value added each quarter for each track record relative to its custom benchmark, then calculating the average of these value added figures each quarter, and then compounding the quarterly value added figures to calculate value added over longer periods.

We have carried out these calculations for most of the product categories where we both maintain ratings and for which we have reliable performance data (currently 69 categories), going back in each case to when we first had a reasonable spread of ratings for the product category concerned.

Some important caveats

All of the value added figures have been calculated by Mercer, but are based upon performance data provided to Mercer by the investment managers concerned. Mercer generally does not independently verify the performance information provided by investment managers.

The methodology described above does not allow for transaction costs that an investor would have incurred if it had actually changed its panel of investment managers every quarter in line with changes to the list of products rated A by Mercer within the product category concerned. In practice, the turnover of managers incurred by such an investor would have averaged about 15% per annum (the actual averages since inception for each product category are shown in the final section of the results). We have not attempted to estimate the transaction costs that would have been incurred as this would require assumptions on a number of factors, including the investor's cash flow position and how the changes had been implemented.

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Some comments on Switzerland's score

- A relatively low minimum pension – 21% of the average wage
- No legal requirement to take income streams
- High household debt
- Need to recognise increasing life expectancy

